"But for" and Business Interruption

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In a recent appeal from an arbitration award in a case concerning business interruption losses, the Commercial Court has held that the arbitration tribunal had correctly applied the "but for" test as the appropriate test of causation. On a further point, the Court held that the tribunal had reached the correct conclusion regarding the construction of a business trend clause.

Hurricanes Katrina and Rita in Autumn 2005 caused significant damage to the Gulf of Mexico, and in particular to New Orleans, Louisiana. In *Orient-Express Hotels Limited v Assicurazioni General S.p.A. (UK Branch) t/a Generali Global Risk* [2010] EWHC 1186 (Comm), the court considered an appeal under section 69 of the Arbitration Act 1996 against an arbitration award.

Background

Orient-Express Hotels (OEH), a luxury-hotelier and holiday operator, was the owner of a hotel situated in the Central Business District of New Orleans. Generali Global Risk was its insurer under a combined property damage and business interruption (BI) policy.

The hotel suffered significant physical damage from wind and water as a result of the hurricanes. The hotel was closed throughout September and October 2005 re-opening on 1 November 2005. OEH sustained significant business interruption losses. A state of emergency was declared and a curfew imposed on 27 August. On 28 August a mandatory evacuation of New Orleans was ordered (with limited exceptions) and again (without most of the prior exceptions) on 6 September 2005. New Orleans was re-opened and the curfew lifted by the beginning of October 2005.

The Tribunal's Decision

According to the arbitration tribunal, *"[T]he Insuring Clause defined "Damage" as (in effect) "direct physical loss destruction or damage" to the Hotel. Cover for Business Interruption is for "loss due to interruption or interference with the business directly arising from Damage" ... The condition for cover is that there has been Damage and that "the Business be in consequence thereof interrupted or interfered with"."*

OEH claimed that it was entitled to an indemnity under the primary indemnity provisions of the Policy for all BI loss resulting from an interruption or interference caused by insured damage to

the hotel, even if such BI loss was also concurrently caused by damage to the vicinity (or the consequences of such broader damage to the vicinity) resulting from the same hurricanes.

Generali submitted, and the tribunal accepted, that OEH could only recover in respect of loss which could be shown would not have arisen had the damage to the hotel not occurred - the "but for" test of causation. To assess the correct level of loss would mean putting OEH in the position of an owner of an 'undamaged hotel' in an otherwise damaged city. The tribunal held that, because an undamaged hotel would have suffered the same loss as a damaged hotel in September 2005 due to the damage to New Orleans, there was no indemnity under the primary insuring clauses of the Policy in respect of such loss.

The Appeal

The question was how the policy responded where both the hotel and the wider area (what the judge referred to as '*the vicinity'*) were damaged and where, as OEH contended, its BI loss was caused both by the damage to the Hotel and by damage to the vicinity (and the consequence of such damage to the vicinity, such as broader loss of attraction), both of which had been caused by the same hurricanes.

OEH appealed on two questions of law. Mr Justice Hamblen was asked to consider:

- Whether on its true construction, the Policy provided cover in respect of loss which was concurrently caused by: (i) physical damage to the property; and (ii) damage to or consequent loss of attraction of the surrounding area
- Whether on the true construction of the Policy, the same event(s) which caused the damage to the insured property which gave rise to the business interruption loss were also capable of being or giving rise to 'special circumstances' for the purposes of allowing an adjustment of the same business interruption loss within the scope of the "Trends Clause".

Causation Issues

It was accepted that the normal rule when looking at issues of causation was the application of the "but for" test. OEH submitted that there were exceptions when it was appropriate to depart from this established test.

OEH referred the judge to exceptions where the *"but for" test should not apply, namely "[t]he typical situation where an extension of liability may prove necessary in the interest of fairness and reasonableness, with a consequent departure from the "but for" test, is where two of more acts or events or agencies are involved and the wronged claimant is unable to prove which act, event or agency has caused the harm."*

OEH also referred to the opinion of Lord Nicholls in *Kuwait Airways Corpn v Iraqi Airways Co* (Nos 4 and 5) [2002] 2 AC 883 where his lordship stated that *"the "but for" test can be over-exclusionary. This may occur where more than one wrongdoer is involved. The classic example is where two persons independently search for the source of a gas leak with the aid of lighted*

candles. According to the simple "but for" test, neither would be liable for damage caused by the resultant explosion."

OEH, whilst accepting that the cases in which it had been held inappropriate to apply the "but for" test had been cases in tort, submitted that the same approach should be applied in appropriate cases in contract. OEH submitted that this was a case of two concurrent independent causes and the application of the "but for" test would lead to "*the untenable conclusion that neither of the causes caused the business interruption loss." Applying the "but for" test to the case, OEH submitted that they would "recover neither under the main Insuring Clause (because "but for" the Damage the loss would still have occurred due to the vicinity damage or its consequences) nor under the POA [Prevention of Access] or LOA [Loss of Attraction] (because "but for" the prevention of access and/or loss of attraction the loss would still have occurred due to the Damage to the Hotel)."*

This submission by OEH relied on there being two concurrent independent causes. However OEH was unable to support this assertion with anything other than cases involving two concurrent interdependent causes.

The judge held that as a general rule the "but for" test was a necessary condition for establishing causation however there may be cases in which fairness and reasonableness required that it should not be a necessary condition.

The judge stated that there was considerable force in OEH's submission, but in this case, it could not be established that the tribunal erred in law in adopting the "but for" approach to causation which they did. He did so on three grounds:

- It was a Policy under which it had been agreed that a "but for" approach to causation should be adopted to the assessment of loss of revenue.
- The question of whether "fairness and reasonableness" required that the "but for" test should not be applied was a matter for the tribunal of fact, rather than for the court on an appeal limited to questions of law.
- He was not satisfied that it had been shown that "fairness and reasonableness" required that the "but for" test should not be applied, specifically, that none of those alternatives contemplated *"would appear to be more fair and reasonable than the "but for" test adopted by the Tribunal, still less so as to require the discarding of that test."*

The Trends Clause

The Trends Clause provided that loss adjustments were to be made *"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 relevant period after the Damage."*

The Tribunal had rejected OEH's submissions on this point stating that it was not necessary *"to go behind the Damage and consider whether the event which caused the Damage also caused damage to other property in the City." The Tribunal added that "the fact that there was other damage which resulted from the same cause does not bring the consequences of such damage within the scope of the cover."*

On appeal, OEH made a number of submissions, none of which found force with the judge who held that he agreed with the tribunal. The judge agreed that *"the clause is concerned only with the Damage, not with the causes of the Damage. What is covered are business interruption losses caused by Damage, not business interruption losses caused by Damage or "other damage which resulted from the same cause" [emphasis added]. The judge held that "[t]he assumption required to be made under the Trends Clause is "had the Damage not occurred"; not "had the Damage not occurred and whatever event caused the Damage not occurred.""*

The judge held that OEH's construction required words to be read into the clause or for it to be re-drafted. The judge found that the Tribunal's construction and application of the Trends Clause was correct.

Impact of the Case

The decision is of interest because it is a rare, reported decision on an issue often covered in arbitration. Despite finding that as a general rule the "but for" test was a necessary condition for establishing causation in fact, there are circumstances where fairness and reasonableness may require that the "but for" test should not be applied. However, those circumstances were not present in this case and the decision offers little in the way of guidance to insurers in assessing when to depart from the general position.