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A New Approach to Causation? The UK's Supreme Court Hands Down Judgment in the Business Interruption Insurance Test Case

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On 15 January 2021, the Supreme Court handed down its hotly-anticipated judgment in the business interruption insurance test case (*FCA v Arch and others [2021] UKSC 1*). Hailed as a further "victory" for thousands of holders of business interruption ("**BI**") insurance policies, the judgment extends, in certain respects, findings in favour of certain policyholders of BI insurance made by the High Court in its judgment of 15 September 2020. In the High Court, it was held that policyholders in respect of 12 of the sample of 21 BI policy wordings (the "**Sample Policies**") examined in the case (each of which purported to cover BI losses that do not relate to physical damage to premises) were, in principle and to some extent, covered in respect of BI losses resulting from COVID-19 and the response to it. Elements of the High Court's judgment were appealed by both the FCA (acting on behalf of policyholders of the Sample Policies) and the defendant insurers.

The Supreme Court judgment, partly due to a different interpretation of the law of causation, allowed the FCA's appeal in every aspect (although in some respects, the grant of the appeal was qualified), and expanded (from 12 to 14) the number of Sample Policies under which certain policyholders could claim BI losses arising from COVID-19.

The headlines from the Supreme Court's judgment have been widely reported. In this client alert, we focus on the implications of the Supreme Court judgment for causation issues in insurance law and the wider law. We also address the implications of the judgment for various key stakeholders. For further context on the developments that caused the FCA to take action on behalf of policyholders, and our update on the High Court's judgment, see our previous publications. For a summary of the Supreme Court judgment, including its findings on certain policy wordings, see the press summary of the judgment.

The Causation Question

As a reminder, for the purposes of the test case, the "*non-damage*" policy wordings in issue were divided into three categories:

1. Prevention of access clauses ("**POA Clauses**"). These clauses provide coverage where there has been a prevention or (more rarely) a hindrance of access to or use of the premises, as a consequence of government or local authority action or restriction. For instance, the Arch policies, considered in the test case, provided that: "*[w]e will also indemnify You in respect of reduction in Turnover and increase in cost of working as insured under this Section resulting from… (7) Prevention of access to The Premises due to the actions or advice of a government or local authority due to an emergency which is likely to endanger life or property.*"

2. Disease Clauses. These clauses broadly provide coverage in respect of BI losses in consequence of, or following, or arising from, the occurrence of a notifiable disease within a specified radius of the insured premises. In the test case, the policies in the category termed RSA 3 provided that: "*[w]e shall indemnify You in respect of interruption or interference with the Business during the Indemnity Period following: (a) any… iii. Occurrence of a Notifiable Disease within a radius of 25 miles of the Premises*".

3. Hybrid Clauses. These clauses refer to both restrictions imposed on the premises, and the occurrence or manifestation of a notifiable disease. In the test case, the policies in the category termed Hiscox 1 provided that: "*[w]e will insure you for your financial losses and other items specified in the schedule, resulting solely and directly from an interruption to your activities caused by… 13. Your inability to use the insured premises due to restrictions imposed by a public authority during the period of insurance following… b. an occurrence of any human infectious or human contagious disease, an outbreak of which must be notified to the local authority*".

As is clear from their wordings, coverage under each of these clauses is, to some extent, dependent on the cause of the claimed losses.

In respect of the Disease Clauses, the Court was asked to decide what causal connection was required between the "*[o]ccurrence of a Notifiable Disease within a radius of 25 miles of the Premises*" and the "*interruption or interference with the Business*". The answer to that question had to be consistent with the fact that, for any given business, there were almost certainly a great many more cases of COVID-19 outside a 25-mile radius than inside it, and those cases outside the radius may have had an equal or greater effect on the BI, by giving rise to government intervention, as the cases within the radius.

There was lengthy argument before both the High Court and the Supreme Court on the effect of the decision in *Orient-Express Hotels Ltd v Assicurazioni Generalis SA [2010] EWHC 1186 (Comm)*. That case concerned cover for BI losses to hotels in New Orleans arising from Hurricanes Katrina and Rita. The claimant's insurance policy covered "*loss due to interruption or interference with the Business directly arising from Damage*", with a trends clause (governing quantification of the claim) providing that the amount of cover "*shall represent as nearly as may be reasonably practicable the results which but for the Damage would have been obtained during the relative period after the Damage*". The judgment in *Orient-Express* held that the policy did not provide cover in respect of the BI suffered by the hotels following the hurricanes. This was because the BI was caused jointly by (i) physical damage to the property, and (ii) damage to (and loss of attraction of) the surrounding area, meaning that there was no 'but for' causational link between the physical damage to the property and the BI.

The High Court Judgment

The High Court's answer to the causation question largely arose from the Court's interpretation of the insured peril in each case.

In respect of the Disease Clause in RSA 3, for instance, the High Court found that the insured peril was the Notifiable Disease (i.e., COVID-19) of which there had been an occurrence within a 25-mile radius. RSA's position had been that the insured peril was the effect(s) of only the local occurrence(s) of a Notifiable Disease. However, this was held to be inconsistent with the language of the policy, and with

the nature of covered diseases such as SARS, which are capable of widespread dissemination and therefore often engender regional or national action from authorities.[1]

As a result of its interpretation of the insured peril, the High Court held that RSA 3 provided cover for the BI effects of the disease COVID-19 (whether occurring within or outside the relevant area). It considered that the proximate cause of such BI losses was the notifiable disease, of which the individual outbreaks formed indivisible parts, meaning that even on a 'but for' analysis, the relevant counterfactual for assessing loss was not just one in which the local occurrences had not occurred, but rather one in which the national outbreak of COVID-19 had not occurred.

The High Court also offered an alternative (and according to it, less satisfactory) analysis in which each individual occurrence was a separate but effective cause of the public measures taken at a national level to reduce transmission of COVID-19. This analysis, although not consistent with a 'but for' approach to causation (since no individual case was a necessary condition for the BI caused), would later be picked up by the Supreme Court.

With respect to the decision in *Orient-Express,* the High Court (in overruling *Orient-Express*) held that there were several problems with the reasoning, the most important of which was that the Court in that case had misidentified the insured peril. Hamblen J (as he then was) had held in *Orient-Express* that "*the relevant insured peril is the damage; not the cause of that damage*" (para. 52). The High Court in *FCA v Arch* commented that the policy in *Orient-Express* did not insure against damage in the abstract, but against damage caused by a covered fortuity, and therefore the hurricanes (in parallel to COVID-19 in the current case) were an integral part of the insured peril, and not separate from it. As such, the counterfactual set up in the trends clause for comparative purposes ("*had the Damage not occurred*") should be interpreted as setting up a counterfactual in which "*both the damage to the hotel and the hurricanes and their effect generally were to be stripped out*" (para. 527). That is to say, the insurers in that case, according to the High Court in *FCA v Arch*, should not have escaped liability for the hotel's BI losses on the basis that the insured event (the hurricanes) had caused interruption through other pathways as well as through the physical damage to the property.

The Supreme Court Judgment

On appeal, the Supreme Court engaged in a novel and theoretical discussion about the nature of causation and the meaning of a cause. The analysis was required because of the Supreme Court's conclusion on the insured peril, which was that RSA 3 (for instance) provided cover for the effects of cases of COVID-19 occurring within a 25-mile radius of the insured premises only (and not, as the High Court had held, for the effects of all cases of any relevant disease of which at least one case occurred inside the relevant radius). It was therefore crucial for the Supreme Court to determine which events or circumstances could be said to have been caused by events within that radius of a business.

The Supreme Court began their analysis with a discussion of proximate causation, a test developed by the common law and codified in respect of marine insurance by section 55(1) of the Marine Insurance Act 1906 (but more widely treated as stating the law applicable to insurance in general). Although the term 'proximate' cause was originally used to mean a 'near' (or perhaps 'immediate') rather than 'remote' cause, it has subsequently taken on more of the meaning of Aristotle's 'efficient' cause, which as the Supreme Court wrote, meant "*something that is the agency of change*" (para. 165). A 'proximate' cause,

[1] See paras.102-107 of the High Court's judgment for further exposition on this point.

the Court reminded us, can remain so even when intervening events appear to have directly caused the loss.

For instance, in *Reischer v Borwick [1894] 2 QB 548*, a ship collided with an object floating in a river, which caused a leak. After a temporary repair, a tug was sent to tow the ship to the nearest dock, but in the course of towing, the effect of the motion through the water was that the leak was re-opened and began to sink. To save the crew's lives, the ship was then run aground and abandoned. In that case, the Court of Appeal held that the proximate cause of the loss of the ship was the original collision, notwithstanding that at least one other cause (the towing of the ship) was partly responsible.

Subsequent cases developed the concept of 'proximate' cause as describing a "*common sense*" approach to causation; what the "*man in the street, and not… either the scientist or the metaphysician*", would understand to be the cause of something.

Though these cases were considered in the Supreme Court's judgment, the judgment arguably sets out a wholly new test for determining whether an event or circumstance is the 'proximate' or 'efficient' cause of a loss, the test being whether "*it made the loss inevitable… in the ordinary course of events*" (para. 168).

A question arising from this analysis is that of multiple causes. In *Reischer v Borwick*, for instance, could it be said that there were multiple proximate causes of the loss? Subsequent case law has more explicitly considered cases of multiple causes, and held that a loss could be caused by two proximate causes. Even if only one of those causes in a case was an insured peril, the insurers would be liable for the loss (unless the non-insured peril was expressly excluded from cover, in which case they would not be). In cases such as these, it could not be said that either of the potentially causative events or circumstances on its own had been a sufficient condition to render the loss inevitable, as each cause operated in combination with the other to cause the loss.

Moreover, as the Supreme Court noted, cases exist where a loss has no cause that was a *necessary* condition to bring about the loss. A hypothetical example (from the Canadian case *Cook v Lewis [1951] SCR 830*) is the case where two hunters shoot into fog, both hitting an innocent bystander, of which either bullet would have caused the bystander's death. Neither shot can be said to be a 'but for' cause of the death, as 'but for' either bullet, the other would still have killed the bystander. However, although 'but for' causation cannot be shown for either hunter, it is intuitively wrong to say that neither hunter caused the death of the bystander. Thus, although the 'but for' test is often described as a minimum threshold test of causation, it sometimes (as in this hypothetical case) fails to identify even one cause of an event.

As well as cases without a *sufficient* cause, and cases without a *necessary* cause, there are also cases with neither. These cases often involve many separate 'causes'. The Supreme Court borrows an instructive example from the work of Professor Jane Stapleton. The example postulates 20 individuals who work together to push a bus over the cliff, a task which, in fact, only requires 13 or 14 individuals. No individual is a necessary cause of the bus going over the cliff (the group could achieve this without any particular individual); and no individual is sufficient to cause the bus to go over the cliff by themselves. In order to assign any responsibility for the fate of the bus, the 'but for' or 'necessary' test must be disregarded. As Professor Richard Wright argued similarly of a million teaspoonfuls of water which come together to constitute a flood: "*[d]enying that any of the teaspoonfuls… contributed to the destruction of the property that was destroyed by the flood… would leave its destruction as an unexplained, non-caused miracle.*"

The Supreme Court reminds us (in para. 191) that there is nothing in principle to prevent the conclusion that one insured event, though it works in combination with many (potentially millions of) other uninsured events, could be a proximate cause of a loss, so long as there is some sufficient causal connection (depending on what is required in the policy) between the insured event and the loss. It was argued by certain insurers that cases within the 25-mile radius of a business could not have been a cause of BI loss by causing the government to impose national restrictions; the lockdowns, they argued, would have been imposed, and loss would have been suffered, even 'but for' those cases.

On the basis of its causation analysis, the Supreme Court rejected this contention and concluded that, under RSA 3, cases of COVID-19 within the relevant radius were each an effective cause of the lockdown and, therefore, of the resulting BI loss. The resulting BI loss was therefore recoverable, regardless of how many (uninsured but non-excluded) events - that is, cases outside that radius - were concurrent causes of that loss.

Accordingly, the Supreme Court joined the High Court in overruling *Orient-Express,* although for different reasons. The Supreme Court held that the High Court in *Orient-Express* had erred by deciding that coverage only extended to losses which "but for" an insured event would not have come about. Instead, in a case such as this, where loss has two concurrent causes (both physical damage to the hotel and damage to the surrounding area), one of which is an insured peril, it held that, provided that damage proximately caused by the uninsured peril (in this case, the damage to the surrounding area) is not excluded, loss resulting from both causes operating concurrently should be covered (para. 309). As to quantum of cover, the Supreme Court also held that a trends clause in such a case should be construed such that it would not reduce the quantum of cover in respect of any circumstances with the same underlying or originating cause as the insured peril (so despite the 'but for' wording in the *Orient-Express* trends clause, that clause should not be interpreted to exclude coverage for any other damage done by the hurricanes which caused physical damage to the hotel in question, such as their effect on the relevant market in the general area).

Implications of the Supreme Court's Judgment

The Supreme Court's judgment clarifies, and arguably reformulates, the principles governing causation, both in insurance law and, potentially, in English law at large. It will be carefully dissected in future cases involving contested issues of causation.

At the time of writing, the declarations of the Supreme Court following the judgment, which will prescribe how, and to what extent, the Sample Policies respond to BI losses arising from COVID-19 (and the response to it), are awaited. However, it is clear that the judgment and declarations will have a substantial impact on a range of insurance industry stakeholders.

Policyholders under the Sample Policies

To assist policyholders in understanding whether they are, in principle, entitled to recoveries, the FCA has introduced a BI insurance 'Policy checker', an online tool that walks policyholders through aspects of their policy to determine whether they might be covered for BI losses due to COVID-19. This tool (alongside the FCA's summary table) is likely to be useful to policyholders in the wake of the judgment.

For policyholders of the Sample Policies in respect of which coverage in principle has been confirmed, the Supreme Court's judgment is binding on the insurers. Whilst, for these policyholders, the judgment

undoubtedly represents a major step towards recovery of their BI losses, it is likely that, even for "successful" policyholders whose entitlement in principle to recoveries has been established, this is just the first step. In some cases, there will be further issues that need to be resolved before the quantum of the policyholder's claim can be determined. For example, successful policyholders will still be required to establish, as a factual matter, the extent of their losses (which can lead to disputes with insurers). In addition, uncertainty may arise regarding the extent to which government support received by the policyholder during the pandemic is to be accounted for in the calculation of any losses. These, and other issues, may lead to disputes and delays in the recovery of losses, notwithstanding the favourable judgment for these policyholders.

Other BI Policyholders

For BI policyholders whose policies were not part of the test case, the judgment and the consequential declarations may nevertheless lead to successful claims where such policies contain similar wording to one or more of the Sample Policies in respect of which liability for COVID-19 BI losses has been confirmed. However, the coverage of each policy will depend on its particular wording, and given the wide range of BI policies available in the market, there remains scope for disagreement between these policyholders and their insurers on the effect of the wording of the particular policy, as well as the issues around the quantum of the losses as referred to above.

Holders of non-BI Insurance Policies

The Supreme Court's broader formulation of causation principles may benefit holders of other types of insurance policy who have suffered losses as a result of COVID-19 (and the response to it). This is particularly so where such policyholders may have encountered difficulties establishing causation under the rigid application of the "but for" test.

Insurers

The FCA has made clear that, following the Supreme Court's judgment, it expects insurers to progress and pay valid claims quickly. In a 'Dear CEO' letter to insurers on 22 January 2021, the FCA stated that "*[i]t is essential that insurers reassess and settle claims quickly in the light of the Supreme Court judgment*", and that this would include making interim payments in appropriate cases. The FCA added that, where insurers do not meet the expectations set out in that letter, it will use "*the full range of [its] regulatory tools and powers to ensure they do so.*"

Whilst the FCA's expectations of insurers are clear following the judgment, as noted above, it is conceivable that, in certain cases, further claim-specific issues and uncertainties will arise that will require resolution, and which could generate further disputes with policyholders. Insurers and their advisers will be required to balance, on the one hand, the need to calculate and progress (or dispute) claims properly and in accordance with their legal and professional duties, and on the other hand, ensure that, in doing so, they do not fall foul of regulatory obligations, including the FCA's expectation that they progress valid claims promptly. Additionally, it remains to be seen whether insurers will face claims from policyholders who may allege that an insurer's failure to pay out in respect of BI losses when claims were made (pending the outcome of the test case litigation) has caused additional losses to the policyholder.

Insurance brokers

Insurance brokers will be presently engaged in advising policyholders on the outcome of the test case and the extent to which BI policies will respond to losses arising from COVID-19. In addition, it remains to be seen whether brokers will face claims from policyholders where, for example, the policyholder has been recommended a policy by a broker that has been determined not to cover BI losses arising from COVID-19, but where they would have been eligible for another policy that has been determined to cover COVID-19 losses.

Concluding Thoughts

The Supreme Court's judgment, together with the proceedings that generated it, marks a seminal moment in the development of English insurance law and is one that potentially has wider ramifications beyond insurance law. At a practical level, the judgment represents, for thousands of BI policyholders, a significant step towards recovery of losses arising out of COVID-19 and, for the insurers, clarity on liability in respect of certain existing policy wordings. However, as noted above, even for successful policyholders, there remains scope for uncertainty in relation to issues not covered by the test case (such as the quantification of losses), which could lead to further delays in the resolution of existing claims, and which may yet generate further disputes. Furthermore, there are BI policyholders for whom there remain outstanding questions as to availability of cover and quantum of any such cover. Thus while this judgment brings one chapter to a close, we anticipate that the COVID-19 insurance story is far from over.

More generally, it is noteworthy that the Financial Markets Test Case Scheme allowed the case to proceed from the FCA's initial statement that they would be seeking court declarations (on 1 May 2020), to final judgment in the Supreme Court ('leapfrogging' the Court of Appeal), in just eight and a half months. The BI test case provides a clear illustration of the FCA's ability and willingness to advance issues on behalf of those whose interests it represents (something which we have seen echoed in actions by other regulators, such as in the Competition and Markets Authority's pursuit of lastminute.com to secure refunds to its customers for cancelled holidays). The case also illustrates the effectiveness of the English court infrastructure for the expedited resolution of wide-ranging and highly complex "test case" issues of public importance. Market participants will be closely monitoring whether further test cases may be or should be on the horizon.

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