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U.K. SUPREME COURT RULES ON FCA BUSINESS INTERRUPTION INSURANCE TEST CASE

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The U.K. Supreme Court has recently handed down judgment in *Financial Conduct Authority v Arch & Others*,[1] the highly anticipated test case regarding insurance coverage for business interruption losses arising out of the COVID-19 pandemic. The test case is significant for a number of reasons, not least because of the potential impact for the insurance coverage available to SME businesses arising from the pandemic.

The case has continued its swift progress through the courts: first issued in June 2020, the case was heard by the High Court some six weeks later, with first instance judgment handed down in September 2020.[2] You can find our thoughts on that judgment here. Permission was then granted for a leapfrog appeal, and the Supreme Court heard oral argument in mid-November 2020. As such, it has taken a mere seven months to obtain a final decision of the Supreme Court on the issues raised by this case—a rapid-fire turnaround by any measure. As the court itself noted *"[i]t is a testament to the success of the Test Case Scheme procedure that it will have enabled the important legal issues raised in this case to be finally decided following a trial and an appeal to the Supreme Court in just over seven months."* That momentum and the willingness of all parties to cooperate in achieving swift resolution were in no small part due to the huge significance of the issues at stake and the fact that many insureds were facing imminent financial ruin due to the COVID-19 pandemic.

The FCA had been largely successful at first instance, with the High Court agreeing with its position on most of the issues of contractual interpretation. Accordingly, the majority of issues in the appeal were brought by the insurers. However, the FCA also appealed four issues on which it did not succeed at trial. Overall, the issues on appeal can be categorised as follows:

1. issues of construction relating to:
    a. **"Disease Clauses"** (those which can be triggered by the occurrence of COVID-19, typically within a specified distance of the insured's premises);
    b. **"Prevention of Access Clauses"** (those triggered by public authority intervention preventing access to, or use of, premises); and
    c. **"Hybrid Clauses"** (those clauses which contain wording from both Disease and Prevention of Access Clauses); and
2. whether the High Court was correct:
    a. to apply certain counterfactual scenarios in relation to the operation of the clauses in relevant policies that provided for loss adjustments (the "**Trends Clauses**"); and

b. in its analysis of *Orient-Express Hotels Ltd v Assicurazioni Generali S.p.A,*[3] which concerned the application of a trends clause to a hotel's business interruption losses arising out of Hurricanes Katrina and Rita. In this case, the High Court held that hurricane damage to the surrounding area (and the resultant loss of tourism) was part of the counterfactual and so could form part of the loss adjustment when calculating the hotel's losses.

The Supreme Court's leading judgment was given jointly by Lords Hamblen and Leggatt (with whom Lord Reed agreed). Lord Briggs gave a short minority judgment (with which Lord Hodge agreed), in which he departed from the reasoning of the majority on *"one major and one minor point"*, but agreed with the conclusions to which they had come. Lord Briggs considered that he would have agreed with approach to construction taken by the High Court; however, as there was no practical difference in the result reached by the Supreme Court, his dissent is mild.

Reading the first half of the majority judgment, which addresses the issues of contractual construction, one might be forgiven for thinking that the Supreme Court was going to find in favour of insurers, having departed from the High Court's decision on most points of contractual construction. However, the Supreme Court chose to deal with the issues in a different way, via causation, and ultimately reached a result that provides cover for the business interruption consequences of the COVID-19 pandemic. As such, there is limited practical difference for policyholders arising from the differing approach taken by the Supreme Court. However, the decision will be of interest to academics and practitioners alike for the Supreme Court's striking comments on "but for" causation where there are multiple concurrent causes.

The judgment is lengthy and detailed (over 100 pages)—please therefore see the **Speed Read** below for a summary of the key issues.

SPEED READ

This case continues to be of great interest to litigators as the first case to be brought under the Financial Market Test Case Scheme (under Practice Direction 51M of the Civil Procedure Rules). The swift progress of the case—from issue of the claim in June 2020 to the Supreme Court handing down final judgment in January 2021 (a mere seven months)—demonstrates the success of the Test Case Scheme procedure, allowing an important legal issue affecting thousands of individuals to be determined very quickly. Given the success of the Scheme, it is to be expected that the FCA will seek to make further use of it in the future.

The judgment of the Supreme Court can be usefully considered under three headings: (i) **contractual construction**; (ii) **causation**; and (iii) **trends clauses**.

Although the Supreme Court disagreed with the High Court on contractual construction (given that each contract is to be construed on its own words rather than by reference to previous authority), the Court's decision is unlikely to be of wider relevance outside the sphere of business interruption insurance. However, the approach of the Court to issues of causation is a divergence from the usual "but for" test, and may well have a far wider impact on how issues of causation will be viewed in the future.

Contractual construction

The Supreme Court noted that this is a case where the standard rules of contractual construction apply—i.e., what would the reasonable observer, with all the relevant background knowledge available to the parties at the time, have understood the contract to mean. This was not an instance where the wording used by the parties had gone so wrong that it required correction or the substitution of words in order to identify what must have been intended.

Interestingly, the Supreme Court overruled the High Court on the correct interpretation of the Disease Clauses, holding that such clauses only cover relevant effects of cases of COVID-19 that occur at or within the specified radius of the insured premises. As such, the Supreme Court took a much narrower view of such clauses and so the Court's view on causation is crucial for policyholders seeking to claim under a Disease Clause.

In relation to the Prevention of Access Clauses, the Supreme Court disagreed with the High Court's restrictive view on the meanings of *"imposed by a public authority"*, *"inability to use"* and *"prevention of access"*, holding that: (i) *"imposed"* does not require the force of law; and (ii) *"inability to use"* and *"prevention of access"* can mean inability to use/prevention of access to a discrete part of the premises or to whole or part of the premises for the purposes of a discrete part of the policyholder's business activities. This will be welcome news for policyholders seeking to make a claim under this sort of clause.

Causation

The Supreme Court suggested that *"proximate cause"* or the *"efficient cause"* of an event can be described as the cause that *"made the loss inevitable in the ordinary course of events".* This is a helpful clarification of the term *"proximate cause"*, which, in previous authorities, was simply considered to be a matter of judicial common sense.

As to causation in general, the Supreme Court recognised that, in situations where there may be multiple causes (say 20,000 or more occurrences of a disease such as COVID-19), "but for" causation may prove an inadequate test for identifying the true cause of the loss. Instead, the Court considered that: *"[w]hether an event which is one of very many that combine to cause loss should be regarded as a cause of the loss is not a question to which any general answer can be given. It must always depend on the context in which the question is asked. Where the context is a claim under an insurance policy… All that matters is what risks the insurers have agreed to cover… this is a question of contractual interpretation… answered by identifying (objectively) the intended effect of the policy as applied to the relevant factual situation."*

Trends Clauses

The Court considered that the simplest way to construe a Trends Clause is to recognise that the aim of such clauses is to arrive at the result that would have been achieved by the business but for the insured peril and circumstances arising out of the same underlying or originating cause. As such, adjustments should be made only for trends or circumstances that are unrelated or unconnected to the insured peril.

Finally, the Supreme Court took the opportunity to consider the decision of the High Court in *Orient Express*, which has long been considered a problematic decision for policyholders. The *Orient Express* decision clearly does not fit well with the approach taken by the Supreme Court in the present case, and so it is perhaps no surprise that *"on mature and considered reflection"* the Court held that *Orient Express* was wrongly decided and should be overruled.

Recap on the first instance decision

At first instance, the High Court found for the FCA on the majority of issues of interpretation. Our detailed analysis of the first instance decision is available here.

In summary, the High Court held as follows:

- In respect of the majority of the Disease Clauses, the outbreak of the disease could not be separated into local occurrences and was indivisible. Accordingly, *"there would be no effective cover if the local occurrence were a part of a wider outbreak and where, precisely*

because of the wider outbreak, it would be difficult or impossible to show that the local occurrence(s) made a difference to the response of the authorities and/or public".

- However, in relation to two wordings contained in policies granted by QBE Insurance (referred to as **"QBE2"** and **"QBE3"**), the court took a different approach. The court considered that these wordings only envisaged coverage for a specific localised event because of the use of the word *"events",* which has been defined in previous case law as something occurring at a particular time, in a particular place and in a particular way.

- In relation to the Prevention of Access Clauses, an action by an authority that prevents access requires steps that have the force of law; it must convey a restriction that is mandatory and not merely advisory. Where *"prevention"* of access is required, there must have been a closure of the premises for the purposes of carrying out the business.

- In relation to Hybrid Clauses, the High Court took a similar approach to the 'disease' part of the clause and rejected the insurers' arguments that the coverage should only respond to local outbreaks. However, as with the 'prevention of access' wordings, the High Court construed the 'prevention of access' part of the clause restrictively, holding that *"restrictions imposed by a public authority"* require a mandatory restriction and *"inability to use"* requires something more than an impairment of normal use.

- In relation to Trends clauses, the High Court held that, in order to determine the trends of the business and the wider market, the insured damage must be completely removed from the counterfactual.

The Supreme Court's approach to contractual construction

1. <u>The Disease Clauses</u>

First, the Supreme Court considered the Disease Clauses and, in particular, a clause from an RSA policy that read as follows:

> *"We shall indemnify You in respect of interruption or interference with the Business during the Indemnity Period following: (a) any*
>
> *(i) occurrence of a Notifiable Disease (as defined below) at the Premises or attributable to food or drink supplied from the Premises;*
>
> *(ii) …*
>
> *(iii) **occurrence** of a Notifiable Disease **within a radius of 25 miles** of the Premises;"*

"Notifiable Disease" was defined in relevant part as *"an 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."* COVID-19 was made a Notifiable Disease in England on 5 March 2020.

Although there were, of course, variations in the wording between the RSA clause under review and the other policy wordings in issue, the Court made clear that none of the differences in language materially altered the correct interpretation of the clauses.

The Court explained from the outset that there was no doubt or dispute about the principles of contractual construction that applied when interpreting the policies. The core principle (most recently discussed in *Wood v Capita Insurance Services Ltd*[4]) is that an insurance policy, like any contract, must be interpreted objectively by asking what a reasonable person, with all the requisite

background knowledge that would have been available to the parties when they entered into the contact, would have understood the contract to mean.

The Supreme Court also emphasised that this was not one of those rare situations in which the Court, being satisfied that something must have gone wrong with the language, can engage in verbal rearrangement or correction of the words used when attempting to identify what must have been intended. In the present case, the Court considered that there was no ambiguity in the description of the insured peril. In particular, the Supreme Court found that the words *"within a radius of 25 miles"* could not be read in the manner put forward by the FCA (and with which the High Court agreed). In particular, it found that to interpret the clause as covering the business interruption consequences of a Notifiable Disease, wherever the disease occurs but provided there is at least one case of illness within the 25-mile radius, was not what the reasonable reader would understand the words to mean. The Supreme Court considered that to interpret the clause in this way would be to *"stand the clause on its head".*

In reaching this conclusion, the Court noted that, in insurance law, the words *"occurrence"* and *"event"* bear a specific meaning, namely *"something which happens at a particular time, at a particular place, in a particular way"*.[5] A disease that spreads does not operate in this way; it occurs in different places and presents in different ways (i.e., with different symptoms and severity) at a multiplicity of times. As such, the contraction of the disease by different people, in different towns and from different sources throughout England (or the U.K.) could not be realistically described as an *"occurrence"* of a Notifiable Disease: it comprises thousands of separate occurrences. Accordingly, the Court held that the wording of the policy requires there to be an occurrence of the disease within the 25-mile radius specified in the clause.

As noted above, at first instance, the High Court had separated out the policy wordings of QBE2 and QBE3 because they specifically contained the word *"event"*. On this basis, the High Court distinguished between the policy wordings of RSA (and others) and the QBE2 and QBE3. The Supreme Court ruled that there was no difference in meaning between the words *"occurrence"* and *"event"*, and therefore the distinction was untenable. All of the disease clauses considered should be similarly interpreted as requiring an occurrence of the disease within the radius specified by the clause.

As a result, the Supreme Court observed: *"the correct interpretation of all the relevant clauses, [is that] they cover only relevant effects of cases of COVID-19 that occur at or within a specified radius of the insured premises. They do not cover effects of cases of COVID-19 that occur outside the geographical area"*.

2. <u>Prevention of Access Clauses and Hybrid Clauses</u>

The Supreme Court considered the Prevention of Access Clause as set out in the policy of Arch Insurance, which required *"loss resulting from the prevention of access to the insured 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".* The Hybrid Clauses also contained a restriction of access element, but a notifiable disease within a certain radius of the premises must have caused this restriction of access.

The Supreme Court, perhaps unsurprisingly, considered that the *"disease"* elements of the Hybrid Clauses should be interpreted in the same way as the Disease Clauses: that they cover only relevant effects of cases of COVID-19 that occur at or within a specified radius of the insured premises.

In relation to the *"prevention of access"* element of the clauses, the FCA had appealed the High Court's finding that the *"restrictions imposed by a public authority"* had to be expressed in mandatory terms and have the force of law. The High Court's reasoning for this was that the word *"imposed"* would be understood as ordinarily meaning mandatory measures and connotes compulsion. The

Supreme Court agreed with that reasoning but considered that a restriction need not always have the force of law before it becomes *"imposed".* In particular, the Court considered that an instruction given by a public authority may amount to a restriction imposed if, from the terms and the context of the instruction, compliance with it is required without the need for recourse to legal powers. The Supreme Court also agreed with the High Court's reasoning that a prohibition on people leaving their homes without reasonable excuse was capable of being a *"restriction imposed"* for the purposes of the policy wording: there was no need for the restriction to be directed at the policyholder or its use of the insured business, as insurers had sought to argue.

A number of the so-called Prevention of Access Clauses specified that loss would occur where there was *"an inability to use"* the relevant premises. The High Court held that these words meant a complete inability to use the premises save for use that was *de minimis*. The FCA appealed this point and argued that the requirement of *"inability to use"* should be satisfied if the policyholder has suffered an inability to use the premises for the ordinary purposes of its business. The Supreme Court agreed with insurers and the High Court that an inability to use has to be established, not merely an impairment or hindrance in use. However, the Supreme Court did not accept that the inability had to be an inability to use any part of the premises for any business purpose. Instead, 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 business activities".* For example, a department store where every part of the store except the pharmacy was shut would nevertheless be an instance of *"inability to use"* for this purpose.

This reasoning also applied to *"prevention of access"* wordings, in that partial prevention would qualify for cover. Further, prevention of access did not have to be physical prevention. Therefore, a restaurant that was prevented from accessing its dining area but was still able to access the kitchen for takeaways would be covered under such a clause. As a result, prevention of access to a discrete part of the premises, or to the whole or part of the premises for the purpose of carrying on a discrete part of the policyholder's business (e.g., table service in a restaurant), was covered by the policy.

Finally, on contractual interpretation, the Supreme Court confirmed the conclusion of the High Court that *"interruption"* in the context of business interruption insurance does not mean a complete cessation of business, but includes an interference or disruption. The Supreme Court added that the possibility that the interruption may be partial is inherent in the policy provisions that deal with the calculation of loss and envisage that the business may have continued to operate but at reduced income or increased costs of working.

Conclusion on contractual construction

The Supreme Court overruled the High Court on the correct interpretation of the Disease Clauses, holding that such clauses only cover relevant effects of cases of COVID-19 that occur at or within the specified radius of the insured premises. As such, the Supreme Court took a much narrower view of these clauses and its view on causation (see below) is critical in considering cover for policyholders seeking to claim under a Disease Clause.

In relation to the Prevention of Access Clauses, the Supreme Court again disagreed with the High Court's restrictive view on the meanings of *"imposed by a public authority"*, *"inability to use"* and *"prevention of access"*, holding that: (i) *"imposed"* does not require the force of law; and (ii) *"inability to use"* and *"prevention of access"* can mean inability to use/prevention of access to a discrete part of the premises or to whole or part of the premises for the purposes of a discrete part of the policyholder's business activities. This will be welcome news for policyholders seeking to make a claim under this sort of clause.

Causation

Given the Supreme Court's determination on the correct interpretation of the Disease Clauses, questions of causation became of crucial importance. Put simply, as the Disease Clauses would cover only the effects of cases of COVID-19 occurring within the specified radius of the insured premises, the critical question becomes: what connection must be shown between a case of the disease and the business interruption loss for which an insurance claim is made?

The Court began its causation analysis by reiterating well-known principles of causation, including the uncontroversial view that the causation requirement can generally be described as the legal effect of the contract as applied to the specific facts, and will rarely turn on specific words of the contract. In the realm of insurance, the law will generally require a *"proximate"* or *"efficient"* cause, but this requirement can be displaced if the policy provides for some other causal test.

The purpose of the *"proximate"* or *"efficient"* cause is the fact that the law is only concerned with the immediate cause of loss. However, this does not mean the most recent in time. The efficient cause may be preserved even though other causes have arisen in the meantime, but the efficient cause is still prevalent. Previous authorities had suggested that determining the *"proximate"* or *"efficient"* cause was a matter of applying judicial common sense. However, the Supreme Court suggested that this is in fact a concept that is capable of some analysis and proposed the following test: *"the question whether the occurrence of such a peril was in either case the proximate (or efficient) cause of the loss involves making a judgment as to whether it made the loss inevitable… in the ordinary course of events"*. This consideration of the proximate or efficient cause analysis is likely to be highly significant for practitioners in the future analysis of insurance coverage where causation is at issue.

The Supreme Court then went on to consider the orthodox position in respect of concurrent causes, i.e., where there are two or more proximate causes, both of equal effect. It has long been established in insurance law that so long as one of the proximate causes is an insured peril, there will be insurance coverage. For example, if a yacht is insured against *"external accidental means"* and sinks because of a combination of causes, adverse sea conditions and design flaws that rendered the yacht unseaworthy, the first cause (adverse sea conditions) would be covered by the insurance, but the second cause (defect in design) would not. In this case, there would be coverage for the loss because one of the proximate causes is an insured peril.

However, the position is reversed where one of the causes is an insured peril but another is specifically excluded from cover: the exclusion trumps the insured peril (as per the decision in *Wayne Tank*[6]). For example, if a ship that is insured against perils of the sea, but acts of war are explicitly excluded from cover, is hit by a torpedo and simultaneously caught in a terrible storm, with the effect that the torpedo and the storm acting together cause the ship to sink, the act of war exclusion would trump the insured damage with the result that the policyholder would have no cover.

The Court then considered what the correct causation analysis is where it is the combination of multiple causes that makes the subsequent events inevitable (i.e., not two causes, but hundreds or thousands of causes). It was necessary to ask this question because, in the present case, it could not be said that any individual case of COVID-19 caused the U.K. government to introduce the restrictions that led to the business interruption. The government measures were taken as a response to information about all the cases of COVID-19 in the country as a whole: all the cases were therefore equal causes of the imposition of national measures.

The issue with this analysis of COVID-19 is that it cannot be said that but for an individual case of illness resulting from COVID-19, the government measures would not have been taken. Of course, in the vast majority of matters, in any field of law or in ordinary life, the "but for" test will be essential

in determining causation. That said, the Court recognised that "but for" causation is not without limitations:

> *"The main inadequacy, in other words, of the 'but for' test is not that it returns false negatives but that it returns a countless number of false positives. That explains why it is often - and for most purposes correctly - described as a minimum threshold test of causation. It has, however, long been recognised that in law as indeed in other areas of life the 'but for' test is inadequate, not only because it is over-inclusive, but also because it excludes some cases where one event could or would be regarded as a cause of another event."*

The court gave a number of illustrative examples from case law and academic commentary, which demonstrated the sort of situation where the "but for" test was inadequate:

1. a case of two fires, started independently of each other, which combine to burn down a property—it is natural to regard each fire as a cause of the loss even if either fire would by itself have destroyed the property, so that it cannot be said of either fire that, but for that peril, the loss would not have occurred;

2. two hunters simultaneously shoot a hiker who is concealed by bushes and medical evidence shows that the hiker would have been killed instantly even if the other bullet had not been fired. When the "but for" test is applied, the result is that neither hunter's shot caused the hiker's death. This result is manifestly inconsistent with common sense;

3. twenty individuals combine to push a bus over a cliff, but only thirteen people would have been needed to achieve that result. The participation of any given individual was neither necessary nor sufficient to cause the destruction of the bus. However, we would say that each person's involvement was a cause of the loss: *"[t]reating the "but for" test as a minimum threshold which must always be crossed if X is to be regarded as a cause of Y would again lead to the absurd conclusion that no one's actions caused the bus to be destroyed"*;

4. directors of a company unanimously vote to put a dangerous product on the market that causes injuries, although the decision only required the approval of a majority. It cannot be said that any individual director's vote was either necessary or sufficient to cause the product to be marketed and yet it is reasonable to regard each vote as causative rather than to say that none of the votes caused the decision to be made; and

5. multiple polluters discharge hazardous waste into a river. Each individual contribution is capable of being regarded as a cause of the harm, even though it was neither necessary nor sufficient to cause the harm by itself.

The situation becomes more complex with the number of potentially causative variables or *"Multiple Concurrent Causes".* One example given by academics would be adding a teaspoon of water to a flooding river. It might well be correct to disregard such a trivial contribution—but it was nevertheless a contribution. What if the flood was caused by a million people adding a teaspoon of water to the river? On a "but for" causation analysis, not one of the million people who added a teaspoon of water would be said to have caused the flood and accordingly it would be without a cause.

This is where the Court performed a judicial sleight of hand and held that:

> *"Whether an event which is one of very many that combine to cause loss should be regarded as a cause of the loss is not a question to which any general answer can be given. It must always depend on the context in which the question is asked. Where the context is a claim under an insurance policy, judgements of fault or*

> *responsibility are not relevant. All that matters is what risks the insurers have agreed to cover. We have already indicated that this is a question of contractual interpretation which must accordingly be answered by identifying (objectively) the intended effect of the policy as applied to the relevant factual situation."*

As such, the Supreme Court considered that the causation question was dependent on what insurers had agreed would be covered; that is, whether the proximate cause or concurrent cause was sufficient causation for coverage to attach was dependent on what had been agreed between policyholder and insurer in the contract.

In this way, the factual tapestry of the pandemic comes to the fore: can it be said that in providing cover for "Notifiable Diseases", insurers did not envisage cases of the disease spreading outside the area specified in the policy and the government action to control the disease that applied nationally? Both parties must be understood to have anticipated this when taking out such cover. To hold otherwise would lead to *"whimsical results"* where a case of COVID-19 outside the area specified in the policy acted as a countervailing cause, whereas a case within the relevant radius would be causative of loss. As such, the orthodox "but for" test would lead to results that could not possibly have been intended by either party and so the orthodox approach should be dismissed in favour of a commercially sensible alternative.

Accordingly, the Supreme Court found 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 of the individual cases of illness resulting from COVID-19 which had occurred by the date of any government action was a separate and equally effective cause of that action… [this] is a conclusion about the legal effect of the insurance contracts as they apply to the facts of this case."*

This analysis would also be applicable to Hybrid Clauses which contained, as an element, an occurrence of an infectious disease, with the Court holding that the application of the "but for" test would be inappropriate given that there were concurrent proximate causes. The Court considered that the elements of the insured peril (the *"prevention of access"* caused by *"occurrence of a Notifiable Disease"*) were inextricably connected in the sense that those elements arose from the same original cause: the COVID-19 pandemic. As such, the hybrid wordings must be read to indemnify the policyholder against *"the risk of all the elements of the insured peril acting in causal combination to cause business interruption loss: regardless of whether the loss was concurrently caused by other (uninsured but non-excluded) consequences of the pandemic which was the underlying or originating cause of the insured peril."*

As for pure Prevention of Access Clauses, this analysis would also apply.

Conclusion on causation

The Supreme Court suggested that *"proximate cause"* or the *"efficient cause"* of an event can be described as the cause that *"made the loss inevitable in the ordinary course of events"*. This is a helpful clarification of the term *"proximate cause"* which, in prior authorities, was simply considered to be a matter of judicial common sense.

As to causation in general, the Supreme Court recognised that in situations where there may be multiple causes (say 20,000 or more occurrences of a disease such as COVID-19), the "but for" test may prove inadequate for identifying the true cause of the loss. Instead, the Court considered that: *"[w]hether an event which is one of very many that combine to cause loss should be regarded as a cause of the loss is not a question to which any general answer can be given. It must always depend on the context in which the question is asked. Where the context is a claim under an insurance policy… All that matters is what risks the insurers have agreed to cover… this is a question of contractual interpretation… answered by identifying (objectively) the intended effect of the policy as applied to the relevant factual situation."*

This analysis applied equally to the Disease Clauses, Prevention of Access Clauses and Hybrid Clauses.

Trends Clauses

As discussed in our analysis of the first instance decision here, so-called 'Trends' clauses are a method by which the business interruption indemnity can be adjusted via a contractual quantification mechanic. In essence, a Trends Clause asks: if the insured event had not occurred, how would the business be doing? The purpose of the clause is to examine the counterfactual and adjust the indemnity amount accordingly with the aim of achieving a more accurate figure for the insured loss than would be achieved by merely making a comparison with the prior period.

The Court emphasised three points on the proper interpretation of Trends Clauses:

1. the clauses are part of the machinery contained in the policies for quantifying loss—they do not address or seek to delineate the scope of indemnity;

2. the clauses should, if possible, be construed consistently with the insuring clauses of the policy; and

3. they should be construed so as not to take away the cover provided by the insuring clauses to avoid a quantification mechanic being transformed into a form of exclusion.

One particular application of these principles was that such clauses often include a reference to "but for" causation analysis: e.g., *"the amount that we pay for loss of gross profit will be amended to reflect any special circumstances or business trends affecting your business… in order that the amount paid reflects as near as possible the result that would have been achieved if the damage had not occurred*". This had raised a question of whether "but for" causation must be applied to the policy in general. However, the Supreme Court held that references to "but for" causation (e.g., *"if the damage had not occurred"*) in the Trends Clause was just a reference to how the calculation was to be carried out once it was determined that cover applied and an indemnity was payable: the reference did not go to the question of whether there was cover in the first place.

The Court considered that the simplest way to construe a Trends Clause is, absent clear wording to the contrary, to recognise the aim of such clauses is to arrive at results that would have been achieved by the business but for the insured peril and circumstances arising out of the same underlying or originating cause. As such, the trends for which adjustments should be made will be construed to mean trends or circumstances that are unrelated or unconnected to the insured peril.

The Court considered that this approach ensures that the Trends Clauses are construed consistently with the insuring clauses, and therefore do not take away cover *prima facie* provided by the insuring clauses. This is good news for policyholders, whose claims for indemnity will not be limited by circumstances related to the pandemic being included as part of the counterfactual.

Finally, the Supreme Court took the opportunity to consider the decision of the High Court in *Orient Express*, which has long been considered a problematic decision for policyholders. The decision arose out of claims submitted by a hotel due to the damage caused by Hurricanes Katrina and Rita. The claim for physical damage to the hotel was not disputed by insurers but, when it came to the hotel's claim for business interruption losses, insurers argued that there was no coverage because, even if the hotel had been undamaged by the hurricane, it would have suffered business interruption in any event as the devastation to the local area meant there was no tourism. The High Court held (on appeal from an arbitral tribunal) that this counterfactual was the correct application of the causal test. Lords Leggatt and Hamblen, who gave the majority judgment in the present case, were both involved in the *Orient Express* decision (Lord Leggatt sitting as arbitrator and Lord Hamblen hearing the case on appeal under section 69 of the Arbitration Act 1996).

The *Orient Express* decision clearly does not fit well with the approach taken by the Supreme Court in the present case, and so it is perhaps no surprise that Lord Leggatt and Lord Hamblen, when asked to consider the point, held *"on mature and considered reflection"* that *Orient Express* was wrongly decided and should be overruled. In reaching this conclusion, the Supreme Court considered that, applying its own analysis on causation, the business interruption loss arose because of two concurrent causes: (i) the hotel was damaged; and (ii) the surrounding city was also damaged. These concurrent causes arose out of the same underlying fortuity (the hurricanes) and so, provided that the damage to the rest of the city is not excluded from cover under the policy, the loss from both causes operating concurrently would be covered. As to the operation of the Trends Clause in *Orient Express,* it should have been construed so as to exclude from assessment all circumstances which had the same underlying or originating cause as the damage, namely, the hurricane.

Lord Leggatt and Lord Hamblen concluded by saying: *"we invoke whatever ways by which we may 'gracefully and good naturedly' surrender 'former views to a better considered position'"*. With that graceful recantation, the problematic decision of *Orient Express* has been consigned to the judicial scrap heap.

Comment

Overall, the decision of the Supreme Court might be said to represent a high degree of judicial pragmatism—reaching the right result through what might be considered judicial sleight of hand. Fortunately, in exceptional cases, the common law has proven itself to be flexible enough to be shaped towards an overall "right" or "fair" result in all the circumstances, but in such a way so as to preserve the certainty of the rule of law. Arguably, addressing the issue via a causation route is more satisfactory than the contractual construction approach of the High Court, which seemed more at odds with generally accepted construction principles. Regardless of how the result was eventually reached, the decision will be welcome news for policyholders who have faced great uncertainty as to whether their business interruption losses would be covered by their policies.

As for the Supreme Court's causation analysis, it is unorthodox, but it can probably be reconciled with our general understanding of causation principles. Although litigants in a wide variety of cases could seek to rely upon the Court's causation analysis in future, arguing that "but for" causation is not a necessary element of legal causation, it seems more likely that it will only be appropriate in exceptional cases and the lower courts will seek to restrict its application to a small sub-set of cases of limited wider relevance. However, only time will tell whether such arguments will be successful or not.

Of more day-to-day significance, from a causation perspective, is the new test for *"proximate"* cause as the cause that *"made the loss inevitable in the ordinary course of events"*. In prior authorities, the question of whether a cause was to be considered *"proximate"* was a matter of judicial common sense—a highly uncertain and unsatisfactory position that has hopefully now been resolved.

Thankfully, the Supreme Court also took the opportunity to resile from the problematic decision in *Orient Express*, a step that was somewhat inevitable given the Court's well-considered position on causation and the operation of Trends Clauses in this judgment. This problematic decision can now be reserved for the history books.

Last, but not least, it is worth taking a pause to note the remarkable success of the first use of the Financial Market Test Case Scheme. It seems that the Scheme has operated exactly as intended: to enable a claim raising issues of general public importance to financial markets to be determined, without the need for a specific dispute between the parties, where immediately relevant and authoritative guidance is needed. The FCA had estimated that in addition to the policy wordings expressly considered by this decision, some 700 policies across 60 different insurers and 370,000 policyholders could be affected by the outcome of this litigation. The fact that so many policyholders have some measure of legal certainty over their right to an indemnity for business interruption losses in just over seven months since the test case was incepted is to be applauded. Given the success of this first use of the Test Case Scheme, it may well be that we see the FCA initiate more cases of general public importance to financial markets under this regime in future.

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[1] [2021] UKSC 1.

[2] *Financial Conduct Authority v Arch & Others* [2020] EWHC 2448 (Comm).

[3] [2010] EWHC 1186 (Comm).

[4] [2017] UKSC 24.

[5] See *Axa Reinsurance (UK) plc v Field* [1996] 1 WLR 1026 (per Lord Mustill).

[6] *Wayne Tank & Pump Co Ltd v Employers Liability Assurance Corpn Ltd* [1974] QB 57.