

# The UK FCA's Test Case Concludes— What Next For Policyholders?

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Insurance Recovery

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In recent weeks, the English High Court has conducted a trial in an unprecedented test case that the UK Financial Conduct Authority (the “FCA”) commenced to resolve legal issues concerning the interpretation of common business interruption (“BI”) policy wordings (the “FCA Action”).

The judgment in the FCA Action is likely to address issues that will be among the keys to policyholders’ ability to recover indemnities for their COVID-19-related BI losses. The FCA has estimated that the case could affect 60 insurers, 700 types of policy, and 370,000 policyholders.<sup>1</sup> This alert considers the background to the FCA Action, the scope of the issues that we expect may be resolved by the FCA Action, the implications of the FCA Action for policyholders, and related steps that well-advised policyholders may want to consider.

## Background to the FCA Action

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The FCA’s mandate is to regulate the U.K. financial services industry, including the conduct of insurers in the UK. Its operational objectives include protecting consumers, and protecting and enhancing the integrity of the UK financial system. Pursuant to these objectives, the FCA took a close interest in the escalating disputes between business policyholders and London market insurers with regard to the payment of claims under BI policies. This culminated in a groundbreaking [official statement](#) on 1 May 2020 in which the FCA revealed that it intended to start proceedings in order to obtain court declarations aimed at resolving the contractual uncertainty around the interpretation of common BI wordings for the benefit of commercial policyholders.

Given the importance of the issues in dispute, and the significance of the outcome to policyholders — particularly small- and medium-sized enterprises — the regulator set an ambitious timetable for organising and resolving the FCA Action. With the agreement of the participating insurers and the High Court, the FCA has managed to meet its objective of proceeding to trial within six weeks of filing the statement of claim.

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<sup>1</sup> Draft Hearing Transcript, 20 July 2020, available from: <https://www.fca.org.uk/publication/corporate/bi-insurance-test-case-draft-transcript-day-1.pdf>.

The key procedural features of the action are as follows:

- The action involves eight defendant insurers: Arch Insurance (UK) Limited, Argenta Syndicate Management Limited, Ecclesiastical Insurance Office PLC, Hiscox Insurance Company Limited, MS Amlin Underwriting Limited, QBE UK Limited, Royal and Sun Alliance Insurance PLC, and Zurich Insurance PLC. The defendants were selected following a public consultation to identify a representative sample of policy wordings to be examined in the test case, and the insurers that use those wordings.
- The FCA and the participating insurers signed a [Framework Agreement](#) on 31 May 2020, which addresses various procedural issues, including the parties' agreement that the FCA Action is suitable for the Financial Markets Test Case Scheme, the UK statute authorising the FCA's institution of such test cases.
- Policyholders are not directly party to the FCA Action or the Framework Agreement, and they were not involved in the FCA's decision to pursue the case. However, policyholders have had the opportunity to interact with the FCA and its lawyers at various stages since the FCA Action was first announced, including prior to the FCA's submission of its pleadings.
- The Court has also permitted intervention in the proceedings by two "action groups" of mainly SME policyholders and three individual policyholders, with policies issued by Hiscox, QBE and Aviva.
- The Court will make determinations about specific issues identified in an [Agreed List of Issues and Common Ground](#) (discussed further below) that was published on the eve of the trial. The Court will consider the disputed issues against the background of a selection of sample policy wordings issued by the insurer defendants. These wordings contain identical or similar terminology to that which appears in policies issued by other insurers that are not party to the proceedings.
- In order to speed up the trial of the FCA Action by limiting the amount of factual evidence, the parties agreed a list of [Assumed Facts](#) as well as 10 sets of Agreed Facts covering various factual focal points, such as the chronology of the UK Government response to COVID-19, and the characteristics and prevalence in the UK of the disease.
- Following the commencement of the FCA Action on 9 June, the parties exchanged, first, pleadings and, then, "skeleton arguments" (detailed written submissions of law and fact) in advance of the trial, all of which are [accessible online](#).
- The parties made their oral submissions to a court comprising a Court of Appeal Judge, Lord Justice Flaux, and a High Court Judge assigned to the Commercial Court, Mr Justice Butcher. Both judges were formerly barristers with significant insurance coverage practices.
- The judges have indicated that they hope to make a draft judgment available to the parties by the middle of September, which is likely to mean that the judgment will be issued and published in final form by the end of that month.
- The Framework Agreement contemplates that the losing party or parties may attempt to appeal, and provides that an appealing party will seek to have an appeal heard on an expedited basis and will explore the possibility and appropriateness of seeking a leapfrog appeal to the Supreme Court, by-passing the Court of Appeal.

We next consider the key issues that will be determined by the FCA Action.

## Issues to be Determined by the FCA Action

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### Overview

It is important for policyholders to understand the limits of the FCA Action, as made clear in the Statement of 1 May 2020 and the documents that have since emerged in the action:

- The proposed action by the FCA is not intended to encompass all possible disputes, but only to resolve some key uncertainties relating to the interpretation of the BI provisions of insurance contracts. In particular, it will not determine how much is payable under individual policies, although it will address issues that are relevant to such calculations.
- The action was not intended to prevent individual policyholders from pursuing their own claims through the courts or arbitration, or from taking eligible complaints to the Financial Ombudsman Service. Nevertheless, in practice, insurers and many policyholders are awaiting the outcome of the FCA Action before progressing claims that may be affected by the test case.
- The FCA action encompasses only so-called non-damage extensions to normal BI policies. The FCA is not seeking declaratory judgments regarding the meaning of damage under BI wordings that require property damage. The action also does not address any issues arising under event cancellation policies, even though those policies may present some similar disputes of principle under (for example, in relation to the effect of the “trends” provision discussed below, which is relevant to the calculation of loss).

### The Issues

The FCA Action will review key areas relevant to the existence and scope of insurers’ liability under non-damage extensions to BI policies, including the following:

- Coverage Grant Language: whether the wordings that require a “disease” trigger and those that are triggered by government action have indeed been triggered in all the circumstances and taking into account the respective wordings.
- Exclusions: whether certain policy exclusions may apply, based on the agreed and assumed facts.
- Causation: whether the loss under each policy is proximately caused by an insured peril—a key issue of general insurance law. The defendant insurers deny that any of the COVID-19-related loss suffered by policyholders is caused by an insured peril.
- Quantification and trends clause: most of the policies considered in the FCA Action contain provisions that insurers claim require the court to take into account the effect of prevailing economic circumstances, independent of the specific covered peril, and the alleged impact of such circumstances on policyholders before their policies were triggered. The High Court will necessarily interpret these clauses, taking into account the

first instance ruling in the case of *Orient-Express Hotels*<sup>2</sup>, on which insurers have relied as a precedent and which they contend is helpful to them.

Notably, the FCA Test Case is not intended to resolve the following types of coverage disputes (among others):

- coverage issues relating to clauses that recite an exhaustive list of covered diseases omitting COVID-19;
- coverage issues relating to clauses that require the disease to be present on the insured premises;
- issues concerning mis-selling of policies; and
- other issues flowing from the determination of the questions in the test case, such as additional fact-specific causation issues, or the specific quantum of any particular policyholders' losses.

## The FCA's Insurer Guidance About Affected Claims

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Outside the context of the FCA Action, the FCA issued [guidance](#) requiring insurers exposed to COVID-19-related coverage claims to carry out the following obligations:

- identify the potential implications of the FCA Action on their decisions regarding claims and complaints;
- keep policyholders informed about the test case and its implications; and
- treat policyholders fairly during the pendency of the test case and afterwards.

This guidance applies to all insurers that underwrote relevant non-damage business interruption policies prior to 9 June 2020, as well as certain other market participants who performed services in relation to such policies. More specifically, the guidance requires insurers to:

- determine for each relevant coverage clause in their relevant non-damage business interruption policies whether the outcome of claims may be affected by the final resolution of the FCA Action;
- consider how they can meet their policyholders' information needs about the FCA Action, including whether to provide information via brokers;
- identify any claims or complaints for business interruption losses related to the COVID-19 outbreak that may be wholly or partially affected by the final resolution of the FCA Action, including any such claims and complaints received before the guidance was agreed;
- individually notify any relevant policyholders whose claims or complaints are outstanding or have been denied, whether or not those claims or complaints may potentially be affected by the FCA Action; and
- provide updates to policyholders regarding the FCA Action.

Additionally, the guidance addresses how insurers should approach the resolution of affected coverage claims or complaints while the FCA Action is ongoing, and after the final determination

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<sup>2</sup> *Orient-Express Hotels Ltd v Assicurazioni Generali SpA* [2010] All ER(D) 282

of the FCA Action. For example, insurers are expected to handle and assess all outstanding potentially affected claims and complaints and apply the judgment as far as relevant.

## What Next For Policyholders?

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We recommend the following to any policyholder with a COVID-19-related BI insurance claim awaiting the outcome of the FCA Action:

1. As a threshold issue, the policyholder should ensure that it has provided comprehensive and timely notification to the insurer that complies with the policy wording, since the insurer may be able to contend that this is an absolute precondition of the insurer's liability (for example, if the policy makes compliant notification a condition precedent of the insurer's liability).
2. In view of the likely rush to get claims paid if the FCA Action determines that some or all of the test cases merit coverage, policyholders whose claims will be affected by the judgment should ensure that:
  - a. they have all necessary information and documents to progress the claim as speedily as possible, including progressing the claim to the extent possible with any loss adjuster already appointed by the Insurer; and
  - b. they have clearly identified in what respects the FCA Action may affect their claim and, just as importantly, may not affect it.
3. Where it is not clear whether the FCA Action may affect a claim, but insurers are delaying providing their coverage position, policyholders should press their insurer to confirm its view regarding the possible effect of the FCA Action.
4. Policyholders should ensure in particular that their insurers adhere to the FCA Guidance for Affected Claims, and seek advice from their broker or legal counsel if they believe that their insurer has taken an incorrect position regarding the possible effect of the FCA Action on a particular claim or complaint.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our Insurance Recovery practice:

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