

---



---

## Commentary

# FCA's Test Case Could Expedite the Resolution of Thousands of Business Interruption Insurance Claims in the UK

---

### DBRS Morningstar

June 4, 2020

---

Marcos Alvarez  
Senior Vice President, Head of Insurance  
Global Financial Institutions Group  
+1 416 597-7553  
marcos.alvarez@dbrsmorningstar.com

Elisabeth Rudman  
Managing Director, Head of European FIG  
Global Financial Institutions Group  
+44 20 7855 6655  
elisabeth.rudman@dbrsmorningstar.com

---

### Key Takeaways

- BI typically covers losses resulting from physical damage to the insured premises; however, certain BI policies might cover losses in the absence of physical damage, including those caused by the actions of a civil authority.
- The FCA is moving forward with a court case that will examine a representative sample of BI policy wording in the UK. The FCA's goal is to provide clarity on the interpretation of BI policies across the British insurance industry.
- DBRS Morningstar believes that the court case could expedite the resolution of unresolved or denied claims in the UK, which could ultimately affect the global insurance industry given the relevance of the London market.

---

### Overview

On May 1, 2020, the UK Financial Conduct Authority (FCA) announced that it would seek legal clarity on business interruption (BI) insurance policies to resolve concerns from small to medium-size enterprises (SMEs) that face uncertainty on their claims. On June 1, 2020, the FCA confirmed that it had selected a number of representative BI policies and agreed with several UK insurance companies to court action aimed to provide clarity to all parties involved in this dispute. In DBRS Morningstar's opinion, the court case will provide insurance companies with an opportunity to present their technical arguments in an impartial forum. This will also significantly reduce litigation costs as the FCA expects the court case to provide interpretation guidelines for BI policy wording across the entire British insurance industry.

### BI Losses During a Pandemic

BI is a type of commercial insurance that protects insured customers against the loss of income that a business suffers as a result of a covered peril that triggers a suspension of its activity. A typical BI policy would cover lost profits, fixed costs, and extra expenses incurred during the affected period. Originally, BI policies were designed to protect against the loss of income caused by a peril covered under the property insurance policy, such as a fire, earthquake, or flood. Over time, BI coverage has extended, in certain circumstances, to cover the loss of income even in the absence of physical damage to the insured premises, including BI losses caused by the actions of a civil authority. Following the severe acute respiratory syndrome (SARS) outbreak in 2003 that caused millions of dollars in BI claims, many insurers began adding exclusions to standard commercial policies for losses caused by viruses or bacteria. For a sophisticated insurance market, such as the UK, our expectation is that most insurers and reinsurers have implemented tighter policy wording to exclude most losses caused by pandemics in the majority of their contracts. Given the ongoing impact of the Coronavirus Disease (COVID-19) pandemic on business activity and daily life on an unprecedented global scale, many commercial insurance clients are looking into their BI policies to determine whether they cover this event. Significant supply chain disruptions, mandatory or voluntary quarantines, social distancing measures, and restricted travel are taking a direct toll on many businesses that have been forced to shut down their operations.

### FCA's Actions Could Resolve BI Coverage Uncertainty

According to the FCA's initial statement, the UK conduct regulator believes that, in the majority of cases, insurance for SMEs focuses on property damage and only includes basic coverage for BI as a consequence of physical damage. In these cases, BI insurance will likely not cover losses caused by the current pandemic. On the other side of the spectrum, there are a number of policies under which the FCA believes it is clear that insurance companies have an obligation to pay out and insurance companies

acknowledge that BI coverage is valid. For these cases, the FCA expects claims to be assessed and settled quickly. Other policies, however, have sparked disagreement between insurers and customers because there is genuine uncertainty about whether the policy covers this particular situation. For instance, some policies might cover infectious/notifiable diseases, non-damage denial of access, and civil authority-mandated closures and restrictions. Whether BI losses related to the current pandemic constitute valid claims depends on a number of factors, including the relevant policy wording. One of the main challenges in assessing the validity of these claims is that there is a broad range of wording and types of coverage in the BI market — a situation that is common not only in the UK, but globally.

During May 2020, the FCA approached 56 insurance companies in the UK and analyzed over 500 individual policies, including feedback from over 1,200 policyholders and brokers. Consequently, the FCA selected a representative sample of 17 policy wordings from 16 different companies that encompass the key issues in dispute (see Exhibit 1 for a list of these companies).

---

**Exhibit 1** Representative BI Policy Wording and Participating Companies in Test Case

<b>Insurance Company</b>	<b>Representative Sample Policy Wording</b>	<b>Participant in Test Case</b>
Allianz Insurance Plc	X	
American International Group UK Limited	X	
Arch Insurance (UK) Limited	X	X
Argenta Syndicate Management Limited	X	X
Aspen Insurance UK Limited	X	
Aviva Insurance Limited	X	
Axa Insurance UK Plc	X	
Chubb European Group SE	X	
Ecclesiastical Insurance Office Plc	X	X
Hiscox Insurance Company Limited	X	X
Liberty Mutual Insurance Europe SE	X	
MS Amlin Underwriting Limited	X	X
Protector Insurance UK	X	
QBE UK Ltd.	X	X
Royal & Sun Alliance Insurance Plc	X	X
Zurich Insurance Plc	X	X

---

Source: FCA.

The FCA will examine the representative sample of policy wording in the test case before the High Court of England and Wales. Furthermore, the FCA has asked eight insurance companies to assist in the procedure by participating in the test case. The goal of this procedure is to provide an impartial forum where the FCA will examine a sample of representative policy wording in more detail. This FCA designed this exercise to avoid multiple courts of law ruling in an inconsistent manner if individual policyholders contested their insurance companies' decisions in different instances. This procedure also seeks to reduce litigation costs for both policyholders and insurance companies and to set a precedent that for

other policy wording, even if the insurance company in question is not part of the High Court test case. The FCA estimates that the test case could be finalized by the end of July 2020.

In DBRS Morningstar's view, the FCA's actions could expedite the resolution of thousands of BI claims which UK insurance companies have denied or on which they have not yet rendered a decision. Given the importance of the London market to the global insurance industry, the High Court's conclusions could also affect other countries. The opportunity to hear arguments from both sides about the interpretation of BI policy wording in an independent and objective forum could resolve the uncertainty that many SME owners and insurance companies involved in this matter are facing. Alternatively, protracted and lengthy examinations in multiple courts of law could further aggravate the image cost of insurance companies and increase litigation and claims administration expenses, which could also burden the industry's credit strength. We expect that a fair and objective decision from the High Court will provide the clarity needed in this market, which is a far better outcome than more arbitrary resolutions in other jurisdictions. DBRS Morningstar will continue to closely monitor this process and its potential impact on insurance claims across the British insurance industry.

#### **Related Research**

- [\*P&C Insurance: The Conundrum of Business Interruption Coverage during the Coronavirus Pandemic\*](#), April 8, 2020.
- [\*Assessing Financial Strength Ratings of P&C Insurance Companies Amid the Global Coronavirus Pandemic\*](#), April 2, 2020.
- [\*Coronavirus: Likely Increases in P&C Insurance Claims in Certain Business Lines; Financial Markets' Volatility Will Affect Investment Portfolios\*](#), March 12, 2020.

### About DBRS Morningstar

DBRS Morningstar is a global credit ratings business with approximately 700 employees in eight offices globally.

On July 2, 2019, Morningstar, Inc. completed its acquisition of DBRS. Combining DBRS' strong market presence in Canada, the U.S., and Europe with Morningstar Credit Ratings' U.S. footprint has expanded global asset class coverage and provided investors with an enhanced platform featuring thought leadership, analysis, and research. DBRS and Morningstar Credit Ratings are committed to empowering investor success, serving the market through leading-edge technology and raising the bar for the industry.

Together as DBRS Morningstar, we are the world's fourth-largest credit ratings agency and a market leader in Canada, the U.S., and Europe in multiple asset classes. We rate more than 2,600 issuers and 54,000 securities worldwide and are driven to bring more clarity, diversity, and responsiveness to the ratings process. Our approach and size provide the agility to respond to customers' needs, while being large enough to provide the necessary expertise and resources.



The DBRS group of companies consists of DBRS, Inc. (Delaware, U.S.)(NRSRO, DRO affiliate); DBRS Limited (Ontario, Canada)(DRO, NRSRO affiliate); DBRS Ratings GmbH (Frankfurt, Germany)(CRA, NRSRO affiliate, DRO affiliate); and DBRS Ratings Limited (England and Wales)(CRA, NRSRO affiliate, DRO affiliate). Morningstar Credit Ratings, LLC is a NRSRO affiliate of DBRS, Inc.

For more information on regulatory registrations, recognitions and approvals of the DBRS group of companies and Morningstar Credit Ratings, LLC, please see: <http://www.dbrsmorningstar.com/research/highlights.pdf>.

The DBRS group and Morningstar Credit Ratings, LLC are wholly-owned subsidiaries of Morningstar, Inc.

© 2020 Morningstar. All rights reserved. The information upon which DBRS ratings and other types of credit opinions and reports are based is obtained by DBRS from sources DBRS believes to be reliable. DBRS does not audit the information it receives in connection with the analytical process, and it does not and cannot independently verify that information in every instance. The extent of any factual investigation or independent verification depends on facts and circumstances. DBRS ratings, other types of credit opinions, reports and any other information provided by DBRS are provided "as is" and without representation or warranty of any kind. DBRS hereby disclaims any representation or warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability, fitness for any particular purpose or non-infringement of any of such information. In no event shall DBRS or its directors, officers, employees, independent contractors, agents and representatives (collectively, DBRS Representatives) be liable (1) for any inaccuracy, delay, loss of data, interruption in service, error or omission or for any damages resulting therefrom, or (2) for any direct, indirect, incidental, special, compensatory or consequential damages arising from any use of ratings and rating reports or arising from any error (negligent or otherwise) or other circumstance or contingency within or outside the control of DBRS or any DBRS Representative, in connection with or related to obtaining, collecting, compiling, analyzing, interpreting, communicating, publishing or delivering any such information. No DBRS entity is an investment advisor. DBRS does not provide investment, financial or other advice. Ratings, other types of credit opinions, other analysis and research issued or published by DBRS are, and must be construed solely as, statements of opinion and not statements of fact as to credit worthiness, investment, financial or other advice or recommendations to purchase, sell or hold any securities. A report with respect to a DBRS rating or other credit opinion is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. DBRS may receive compensation for its ratings and other credit opinions from, among others, issuers, insurers, guarantors and/or underwriters of debt securities. DBRS is not responsible for the content or operation of third party websites accessed through hypertext or other computer links and DBRS shall have no liability to any person or entity for the use of such third party websites. This publication may not be reproduced, retransmitted or distributed in any form without the prior written consent of DBRS. ALL DBRS RATINGS AND OTHER TYPES OF CREDIT OPINIONS ARE SUBJECT TO DISCLAIMERS AND CERTAIN LIMITATIONS. PLEASE READ THESE DISCLAIMERS AND LIMITATIONS AT <http://www.dbrsmorningstar.com/about/disclaimer>. ADDITIONAL INFORMATION REGARDING DBRS RATINGS AND OTHER TYPES OF CREDIT OPINIONS, INCLUDING DEFINITIONS, POLICIES AND METHODOLOGIES, ARE AVAILABLE ON <http://www.dbrsmorningstar.com>.