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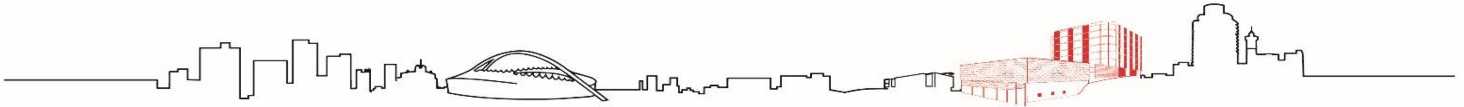

INSURANCE LAW TEAM

Legal Update

9 July 2020

Our Cox Yeats Insurance Law Team is committed to keeping you informed on developing legal issues.

BUSINESS INTERRUPTION INSURANCE –

SHOULD INSURERS BE PAYING BUSINESS INTERRUPTION CLAIMS AS A RESULT OF THE COVID-19 LOCKDOWN?

This question has vexed the insurance industry globally and has been the subject of much debate and the circulation of many legal opinions on the topic. A test case is before the English Courts at present.

Insurers' Position

Insurers contend that business interruption policies were intended to cover localised outbreaks of a notifiable disease at or near the insured premises. They have accordingly not insured a national pandemic, such as Covid-19.

They have also argued that for many businesses, the business interruption's cause was the lockdown itself – and by extension the legislative framework of the Disaster Management Act – and not the existence of the notifiable disease at or near the insured premises (as required by the wording of the Policy).

FSCA Directive

On 18 June 2020 our Financial Sector Conduct Authority issued its own regulatory response setting out its stance on business interruption insurance.

In particular it identified six common categories of Policy wordings and expressed that it was of the firm view that "*the national lockdown was not intended and cannot reasonably be interpreted to be a trigger for BI insurance cover claims".* The two main elements required for a valid claim are:

- The business was interrupted by an infectious disease either at the premises or within a specified radius;
- A competent authority has declared that an infectious disease exists within the specified radius.

It also expressed that requiring Policy holders to, for example, provide proof that people were treated at a hospital nearby, confirmation of the relevant health authority of a confirmed Covid-19 case, or submission of medical records of a person infected within the radius essentially placed too great a burden on the Policy holder and would not amount to fair treatment of financial customers.

It further concluded that insurers who did not deal with business interruption claims in accordance with the communication would be directed to do so in terms of the Financial Sector Regulation Act 9 of 2017.

Café Chameleon Decision

These and related issues came before the Cape High Court in the case of *Café Chameleon CC and Guardrisk Insurance Company Limited.* In this case, the Court was asked to issue a declaratory order that the insurer was obliged to pay the policyholder for the loss suffered as a result of interruption caused by the Covid-19 pandemic and the Regulations published under the Disaster Management Act.

The application was brought urgently before Court.

The Business Interruption section of the insured's Policy read as follows:

The insurers would indemnify the insured in respect of: …….

loss due to interruption of or interference with the business in consequence of:

(a) …(d);

(e) a notifiable Disease occurring within a radius of 50 kilometres of the Premises

Special Provisions

(a) Notifiable Disease shall mean 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, but excluding Human Immune Virus (H.I.V), Acquired Immune Deficiency Syndrome (AIDS) or an AIDS related condition.

(emphasis added)

The Insured's Case

The insured argued that, as a direct result of the regulatory framework in terms of the Disaster Management Act, the restaurant suffered business interruption and financial losses as it was unable to trade or receive customers.

The Lockdown Regulations restricted the movement of persons and confined them to their place of residence unless strictly for the purpose of *inter alia* obtaining an essential good or service. As a consequence, all businesses were required to cease operations during the lockdown, save for any business or entity involved in the manufacturing, supply or provision of an essential good or service.

A restaurant was not classified as an essential good or service and therefore remained closed. Even after the further amendments to the Lockdown Regulations in light of the Risk Adjusted Strategy which permitted the restaurant to produce and sell cooked food for home delivery and take-away, the insured's business suffered losses because it was primarily a sit-down restaurant, with only a small percentage of revenue being generated by food deliveries.

The Insurer's Case

The insurer argued that:

- the matter was not urgent;
- declaratory relief would be premature because the insurer was still waiting for more information from the insured;

- the loss was not insured under the Infectious Diseases Extension ("Extension") clause in the Policy because:

  (a) the extension was to cover only localised infections or outbreaks at or near the premises;
  (b) there was no causal link between the Lockdown Regulations and the Policy extension.

Courts Findings

Urgency

The Court found that the matter was sufficiently urgent because of the insured's financial distress and the fact that the business would fail if it was not afforded redress now.

Declaratory Relief

The Court determined that it could issue a declaratory order and that it was not premature to do so as the insurer had appointed a loss adjuster to assess the claim and it was clear since 27 March to the date of the application, that the restaurant had generated no business at all.

The Court found therefore that the loss of income which the insured had already suffered was manifest.

The Court also noted that the insured only sought declaratory relief regarding the insurer's liability, but not the final quantification of the insured's claim.

Did the Claim fall within the Insuring Clause?

The Court accepted that in interpreting contracts, it is necessary to "navigate away from a narrow peering at words in an agreement". The Court must have regard to the context and purpose of the provision in order to interpret the words sensibly and ensure that the result is not unbusinesslike.

The insurer provided conceptual information to the interpretation argument including that:

(a) prior to the Coivd-19 pandemic and the imposition of the national lockdown there were several types of insurance cover available in the South African insurance market that would have offered cover to the Applicant for losses it may have suffered as a result of the national lockdown, however the Applicant did not purchase such other policies;

(b) the insurance industry view the losses suffered as a result of the national lockdown to not fall under a Notifiable Disease type insuring clause; and

(c) if the insured are simply to be indemnified within their policies for the Covid-19 losses they may have suffered, without applying the terms of the policies, it may have the potential to destabilise the global and the South African insurance market.

The law requires that insurance policies should be construed in accordance with sound commercial principles and good business sense, so that their provisions receive fair and sensible application. Nevertheless, the Court reasoned that "it cannot be that the Policy under consideration must be interpreted with reference to other policies or on the basis of generalised concerns about the impact of Covid-19 on the insurance industry at large, of which the Applicant had no knowledge of*".*

The Court further analysed the legislative framework in respect of notifiable diseases and concluded under the provisions of the National Health Act, read with the Regulations relating to the Surveillance and the Control of Notifiable Medical Conditions ("Surveillance Regulations") that Covid-19 was a notifiable medical condition which must be reported by the most rapid means available to the focal person at the health sub-district level.

The insurers argued that the Surveillance Regulations were made by the Minister of Health, being an officer of the National Government, and not an officer of any "competent local authority". Therefore, no local authority itself stipulated that the outbreak of any human infectious disease must be notified to it, but it was the National Government acting through the World Health Organisation, and the Minister who did so. Although the Lockdown Regulations were promulgated under the Disaster Management Act with countrywide effect, it was the Head National Disaster Management Centre that initially classified the pandemic as a National Disaster in terms of the Disaster Management Act.

The Court held that, having regard to the legislative framework, it was evident that once Covid-19 was by law reportable to a competent local authority, “it surely cannot matter that the source of that obligation is national legislation, rather than an ordinance, bylaw or other subordinate legislation enacted by a local authority”.

Based on an interpretative approach, the Court held that the principal reason why the notification requirement was introduced to the Extension, was to “ensure that cover thereunder would be triggered only by outbreaks of the most serious diseases, and not whether the source of that obligation to report the gravity of the threat was national legislation, rather than subordinate legislation enacted by a local authority".

In terms of the wording of the Extension, the Court held that it simply required the triggering of an obligation to report the disease to a local authority. “In the absence of such an obligation in any by-law, common sense dictates it must have been contemplated that the obligation would be applied by National Legislation, provided that it imposed an obligation to report to a local authority”. In the Court’s view, that is what the National Disaster Management Centre did on 15 March 2020 in GN 312 when it declared a National Disaster.

The Court concluded that, on a proper interpretation of the indemnity, insofar as it is conditioned upon a "human infectious or human contagious disease, an outbreak of which the competent local authority has stipulated shall be notified to them”; Covid-19 falls within the ambit of the Policy Extension, and the fact that the Surveillance Regulations were made by the National Government, rather than by any local authority, does not offend against the provisions of the Policy.

Causation

The insurer’s argument was that the Applicant had failed to demonstrate that its business was interrupted due to the Covid-19 outbreak, but rather that its business was interrupted by the regulatory regime which fell outside of the ambit of the Applicant’s insurance Policy.

The Court affirmed that the general approach to questions of causation are equally applicable to insurance law, although its application will be subject to the provisions of the Policy.

Nevertheless, the Court held that the initial inquiry, being one of factual causation, will seldomly be affected by provisions of the Policy in question. Once factual causation is established, the secondary inquiry is one of legal causation and the existence of a sufficiently close connection.

It is in terms of this inquiry where regard must be had to the provisions of the Policy in question which may limit the consequences covered. The Court affirmed that the specific provisions, the type of the Policy, the nature of the risk insured against and the conditions of the Policy may assist the Court in deciding whether the factual cause should be regarded as the cause in law.

The Court adopted the common sense “but for test”[1] and asked whether, but for the Covid-19 outbreak, the interruption or interference to the Applicant's business would have occurred when the Lockdown Regulations were promulgated.

Having regard to the classification of Covid-19 as a national disaster, the subsequent declaration of a National State of Disaster by the Minister of Cooperative Governance on the same day after considering the magnitude and severity of the Covid-19 outbreak, the resultant regulations promulgated in terms of the Disaster Management Act, and the fact that it was common cause that Covid-19 occurred within 50kms of the Applicant’s premises, the Court held that there was a clear nexus between the Covid-19 outbreak and the regulatory regime which caused the interruption to the Applicant’s business.

Accordingly, the insured was successful in establishing factual causation, and the insurer’s arguments that the regulatory regime was only introduced to “flatten the curve” were found to be misplaced.

Notably, the Court held that the magnitude of potential business interruption losses caused by Covid-19 and the significant demand upon the resources of insurers in this respect would not form a Policy consideration in determining legal causation in the context of the Policy Extension.

Furthermore, the Court disregarded the insurer’s predictions of “industry collapse” as “nothing more than speculation” and remarked that it cannot be a defence for an insurer to say that it must be excused from

[1] As set out in *Minister of Finance v Gore* [2007] 1 All SA 309.

honouring its contractual obligations on the basis that its business has unexpectedly incurred greater debt than had been expected.

Accordingly, the Court held that the insured had successfully established causation and that therefore the Respondent was liable to indemnify the insured in terms of the Business Interruption section of the Policy for loss suffered as a result of the Covid-19 outbreak which resulted in the regulatory framework.

Conclusion

In conclusion, the Court held that the insured had successfully established that the insurer was liable to indemnify it in terms of the Business Interruption section of the Policy for the loss suffered.

Although this is the first decision in the Cape Town High Court and given the impact of the judgment, it is likely to be taken on appeal, the decision may be followed in other jurisdictions of the High Court. It establishes important principles for consideration which would impact across the common business interruption extensions in the insurance market.

There are further matters pending before the Courts, which will now have to take into account the reasoning of the Court in this decision, which will be persuasive but not binding on other Provincial Courts until such time as there is a decision of an Appeal Court.

Should you require any assistance in this regard, Richard Hoal can be contacted on :

RICHARD HOAL
Partner
Direct Tel: 031 536 8511
Cell: 079 496 1799
Email: rhoal@coxyeats.co.za

Visit us at: www.coxyeats.co.za

DURBAN OFFICE:
Tel: 031 536 8500 | **Fax:** 031 536 8088
Address: Ncondo Chambers, Vuna Close, Umhlanga Ridge, Durban, 4320

JOHANNESBURG OFFICE:
Tel: 010 0155 800
Address: 4 Sandown Valley Crescent, Sandton, 2196

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