

Changes in the Irish business interruption insurance market



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It is a time of significant change for the Irish insurance market. Business interruption insurance has, in particular, become a focal point of the challenges presented by the Covid-19 pandemic. On 5 February 2021, Justice Denis McDonald of the Irish High Court held that the pub owners were entitled to be compensated by FBD Insurance for financial losses associated with the closure of their businesses due to the Covid-19 pandemic. It is understood that the FBD decision is not being appealed.

The decision of the court in the FBD case (which is consistent with the position adopted by the UK Supreme Court on 21 January 2021 in the FCA's test case) clearly favours the position of the customer. The decision represents a classic example of the application of the doctrine of contextualism in contractual interpretation: not only is the written text of a business interruption insurance policy contract relevant, so too is the legal and factual context in which it was arranged.

The response of the regulator: the Central Bank of Ireland

It is noteworthy that the decision of the Irish High Court in the FBD insurance case arises within the context of the Central Bank's (CBI) 'Covid-19 and Business Interruption Insurance Supervisory Framework' in August 2020 (the Supervisory Framework), which sets out the CBI's expectations of the insurance industry for adopting a 'customer first' approach to resolving issues relating to business interruption insurance.

The Consumer Protection Code 2012 and the Insurance Distribution Regulations 2018 are fundamental and pervasive principles underlying the Supervisory Framework, which emphasises that regulated financial service providers must take immediate remedial action in line with CBI's expectations where concerns are identified in relation to customer treatment and interpretation of business interruption insurance policies.

In keeping with its previous industry letter of 27 March 2020 (the Dear CEO Letter), the CBI indicated that the full co-operation of the senior management and boards of directors of regulated financial service providers is expected when implementing the Supervisory Framework. Key

talking points in the Supervisory Framework can be summarised as follows:

- 1) **Interpretation of Irish government's order to close** – the CBI's view is that the government's communication in March 2020 that businesses should close should be treated as a direction or mandate for the purpose of determining whether business interruption cover exists.
- 2) **Unclear policy wordings** – the CBI reiterates its view expressed in the Dear CEO Letter that unclear business interruption policy wording should be afforded the interpretation which is most favourable to customers and the CBI sets out the steps which regulated financial service providers should undertake when assessing if the wording of a policy is unclear.
- 3) **Litigation costs** – in circumstances where litigation proceedings are agreed to be a 'test case', such as in the FBD case, the CBI expects the relevant defendant regulated financial service providers to be cognisant of the significant costs burden on plaintiffs in those proceedings. Furthermore, regulated financial service providers should consider how the scope of the issues in dispute can be narrowed to reduce costs. Where a regulated financial service provider obtains a favourable court interpretation of a business interruption insurance policy wording, the CBI expects the regulated financial services provider not to seek costs against the plaintiff in recognition of the significant litigation costs involved. Finally, the CBI also states that regulated financial services providers should pay the reasonable costs of plaintiffs in 'agreed test case' litigation.
- 4) **Coverage assessment and escalation strategy** – the Supervisory Framework sets out in detail how the CBI will monitor and analyse the approach taken by relevant regulated financial service providers in the areas of (i) cover (ii) causation and (iii) quantum and claims handling. It also explains the CBI's expectations and outlines how matters will be escalated where its expectations are not met.

For example, in circumstances where the issues of cover and causation are clear but the regulated financial service provider does not accept this, the CBI will inform the regulated financial service provider of its view that it should accept that the issues are established. Where cover and causation are disputed, and regulated financial service provider is denying cover and/or causation or both, the CBI may intervene by communicating its view. In these situations, if the regulated financial service provider does not respond in line with the Central Bank's expectations, it may then take 'such further measures as may be appropriate to the circumstances.' Once a resolution is reached, the CBI then expects the regulated financial service provider to carry out an impact assessment to identify if there are any beneficial impacts that could be applied to other customers with similar policies. The wider impact assessment is a recurring theme in the Supervisory Framework and applies equally to regulated financial service providers on the conclusion of any litigation proceedings.

It is clear from the Supervisory Framework that the CBI intends to adopt a robust supervisory approach in its engagement with regulated financial service providers relating to their handling of Covid-19 related business interruption insurance claims. Indeed, the concluding paragraph of the Supervisory Framework fires a clear warning shot:

'The Central Bank will continue to examine all possible options within the full suite of our powers and we will intervene where appropriate, as we take this work forward.'

The market implications of the Supervisory Framework are significant. The CBI is likely to be encouraged by the recent judicial decision in the *FBD Insurance* case. The CBI published a statement on 5 February 2021 in response to the *FBD* decision, reiterating the expectations set out in the Supervisory Framework. In addition, the emphasis on prioritisation of business interruption issues in the CBI's Conduct Priorities for 2021 featured in the

speech delivered by the CBI's director general, financial conduct to the BPFJ Membership Forum on 16 March 2021. It stands to reason that a regulatory investigation by the CBI into an insurer's handling of its business interruption insurance is a genuine possibility in 2021.

The expected impact on the Irish insurance market

The market response to the Supervisory Framework is likely to precipitate action on the part several key stakeholders in the insurance industry: the regulator, the insurer and the customer.

On the part of the regulator, it is clear that the CBI will intervene in appropriate cases where regulatory breaches are identified. The CBI has an extensive record in bringing successful enforcement proceedings against regulated entities that are in breach of regulatory frameworks. Recent enforcement actions have been taken against leading financial institutions, and, most recently, an enforcement action against Davy Stockbrokers leading to a multimillion euro sanction being imposed against Davy for breaches arising from personal account dealing. At the time of writing, Davy is listed for sale in light of the controversy.

Insurers exercising proactive, prudent management will likely undertake a comprehensive review of their internal practices and procedures relating to business interruption insurance, internal governance, as well as the insurer's communications strategy vis-à-vis its customers. This internal review will likely assess the insurer's rate of compliance with the four pillars of the Supervisory Framework. Early action to identify potential gaps will provide an opportunity to the insurer to 'put right' any deficiencies in its practices and procedures, and, if carefully managed, should afford the insurer maximum protection in any regulatory investigation conducted by the CBI, or any legal proceedings that may arise from its business interruption insurance policies. A comprehensive internal review process will also identify key learnings, allowing the insurer's business to evolve going forward.

One must also consider the position of the customer: the Supervisory Framework, together the decision in the *FBD Insurance*

case, clearly places the customer on the higher ground in any dispute with an insurer over the interpretation of a business interruption insurance policy. Where there is any element of doubt in relation to an interpretation of an insurance policy, the courts, and, indeed, the regulator, will most likely favour the customer. In light of the *FBD* decision, there is likely to be an increase in legal proceedings initiated by customers against insurers and brokers in relation to the interpretation of business insurance policies. An increase in litigation may have significant cost implications for the insurance industry and the potential for reputational damage is apparent, particularly where there is a lack of action to 'put matters right' on the part of the insurer. Behind the scenes, it is possible that lawyers representing customers may seek to capitalise on the Supervisory Framework to give further leverage to a customer's position in seeking compensation under their business interruption insurance policy.

Conclusion

It is apparent that there is significant exposure for Irish insurers as a result of recent developments. The Supervisory Framework is a clear statement by the CBI that it will not accept customer detriment in matters relating to business interruption insurance policies, and that it will take steps to protect consumers. In essence, the Court's decision in the *FBD Insurance* case confirms the position adopted by the regulator in the Supervisory Framework: if there is any doubt as regards the interpretation of business interruption insurance policy, the Court too will favour the customer.

While it remains to be seen what the longer term implications of this new market dynamic may hold for business interruption insurance more generally, it would appear that in the short to medium term, insurers are charged with the task of regularising matters relating to business interruption insurance so that the customer is appropriately accommodated. Early action on the part of the insurer to identify gaps in its policies, procedures and communication strategy would be a prudent move, and would offer the insurer maximum regulatory protection as the industry moves forward from the many challenges presented by the Covid-19 pandemic. ■