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// COMMERCIAL CONTRACTS

Setting the Bar – FBD Business Interruption Case Demonstrates the Importance of Policy Wordings

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Mr Justice Denis McDonald in the Commercial Court (**Court**) recently delivered a highly anticipated judgment in the test case taken against FBD Insurance plc (**FBD**) by four plaintiff publicans, finding in favour of the plaintiffs. The test case concerned the interpretation of business interruption clauses in an insurance policy sold by FBD to the plaintiffs. The policy in question was sold to approximately 1,300 publicans in Ireland. The principal question to be considered by the Court was whether FBD was obliged to cover any losses suffered by the plaintiffs following the imposed closure of public houses by the government on 15 March 2020 as the COVID-19 pandemic began to take hold in Ireland. FBD refused cover on the basis that the imposed closure was not caused by an outbreak of COVID-19 on the plaintiffs' respective premises or within a 25-mile radius but instead because of the countrywide presence of the disease. Therefore, FBD argued there was no causative link between the closure and an outbreak of COVID-19 which occurred within the 25-mile radius surrounding the plaintiffs' respective premises.

The Court considered the FBD policy wordings in detail and applied interpretative tools in reaching its decision. The level of analysis undertaken by the Court on the meaning of individual words in the policy, and the consequences which flowed from the use of such words, provides helpful guidance for the insurance industry for future drafting of policy wordings. In addition, the findings of the Court offer some key learnings with respect to the drafting and interpreting of commercial contracts generally.

"TEXT IN CONTEXT" APPROACH

As the test case was principally concerned with the interpretation of the policy, oral evidence did not feature significantly. The Court applied the "text in context" approach, which involves approaching the question of interpretation on an objective basis in order to work out the meaning of a contractual term. The contractual language used should be construed in the context of the terms of the contract as a whole and also in the context of the relevant factual and legal background. In applying this approach, the court seeks to put itself in the position of the parties at the time the contract was made, and to interpret the contract by reference to the meaning it would convey to reasonable persons having all the background knowledge reasonably available to the parties at that time.

THE POLICY WORDING

Having outlined the relevant factual and regulatory context, McDonald J considered the wording of the policy. He noted that in cases involving standard form policies produced by an insurer, ambiguity in the language of the policy is construed against the insurer. This is known as the *contra proferentem* rule. However, McDonald J observed that this rule is usually an approach of last resort in commercial cases, applied where other rules of construction fail.

The FBD policy covered a range of risks, but the dispute between the parties related to the interpretation of section 3 of the policy, in particular the following:

"The Company will also indemnify the Insured in respect of (A), (B) or (C) above **as a result of** the business being affected by:

1. Imposed closure of the premises by order of the Local or Government Authority **following:**

a. Murder or suicide on the premises

b. Food or drink poisoning on the premises

c. Defective sanitary arrangements, vermin or pests on the premises

d. **Outbreaks of contagious or infectious diseases on the premises or within 25 miles of same…"** *(emphasis added)*

McDonald J considered the operative provisions of the policy. Referring to the dicta of O'Donnell J in *Law Society of Ireland v. Motor Insurers' Bureau of Ireland* [2017] IESC 31, he noted that it was clear that in interpreting a contract, the contract must be read as a whole and it is wrong to approach the interpretation of a contract solely through the prism of the dispute before the court.

The Court found that the policy envisaged that a public house could be the subject of an imposed closure following an outbreak of contagious or infectious disease, not only on the premises, but within 25 miles of the premises, which is a generous geographic limit in the context of pubs situated in Dublin due to population density.

THE "INSURED PERIL"

As observed by McDonald J, an insured will only recover under a policy of insurance to the extent that their losses were caused by a "peril" insured under the terms of that policy, i.e. the nature of the risk covered by the policy. The perils will either be described in the policy or cover will be provided on an all risks basis, subject to those perils which are specifically excluded.

FBD argued that the peril was the enforced/imposed closure of the pub, not the infectious or contagious disease. In such circumstances, FBD could contend that the losses would have arisen even if the pubs were open during the period in question given the existence of COVID-19 in the community and all of the attendant restrictions (other than closure) which continued to exist.

The plaintiffs argued that the peril was a composite one, consisting of

I. the imposed closure;

II. by order of a local or government authority;

III. following an outbreak of infectious disease on the premises or within a 25-mile radius.

McDonald J held that the clause had to be read as a whole, as that is how the clause would be read by a reasonable person standing in the shoes of the parties to the proceedings. He concluded that the relevant peril was not imposed closure *per se*, rather it was a composite one i.e. the imposed closure following the outbreaks of disease within 25 miles.

McDonald J then considered whether cover was limited to localised closures only. FBD argued that the government decision to close public houses was prompted, not by a localised outbreak of disease, but by reason of concern at a nationwide level. The Court did not agree. It held that the fact that the government took the view in March 2020 that it was necessary to close down public houses on a countrywide basis illustrated the widespread nature of the outbreaks. The fact that there were outbreaks within 25 miles of the premises was, at minimum, a cause of the decision to close each of the public houses.

THE MEANING OF "FOLLOWING"

McDonald J considered the meaning of the word "following" in the section of the policy wording which stated that FBD would provide cover to the insured for *"(1)Imposed closure of the premises by order of the Local or Government Authority* **following:....**"

FBD argued that the word "following" should be interpreted in the same way as the words "as a result of", meaning that closure should be proximately caused by the outbreaks within 25 miles. The Court distinguished the use of the word "following" in the relevant section of the policy with the wording used elsewhere which indisputably connoted proximate cause, namely "resulting from", "as a result of", and "caused by". McDonald J also made reference to wording used in analogous policies available in the Irish market such as "in consequence of" and "arising directly from".

McDonald J rejected FBD's argument and found that the word "following" was deliberately intended to signify something other than proximate cause. He found that the word "following" in this context should be construed as requiring that the matter described in paragraph (d) (i.e. *(d)Outbreaks of contagious or infectious diseases on the premises or within 25 miles of same...")* should be *a cause,* but not necessarily **the dominant cause** of the imposed closure.

CAUSATION

Under contract and tort law, a plaintiff may only recover damages for those losses which were *caused* by the defendant's wrong. The general test in contract cases is the *"but for"'* test, i.e. the plaintiff must show that the loss would not have occurred *"but for"* the defendant's breach. In an insurance context, the losses insured under the policy will be those which would not have been suffered *"but for"* the occurrence of the relevant peril covered under the policy. FBD argued that a strict interpretation of the *"but for"* test should be applied and that the public houses should be indemnified by the insurer in respect of those losses which it can prove would not have arisen *"but for"* the eventuation of the insured peril. Based on this approach, FBD argued many of the losses claimed by the plaintiffs would have arisen in any event by reason of societal reaction to the COVID-19 pandemic, rather than as a result of the government-imposed closure.

However, McDonald J found that a fair and reasonable modification of the *"but for"* test should be applied. In doing so, he held that where loss is sustained as a result of two or more interrelated events which are each capable of causing the loss, such as the government imposed closure and the changes in societal behaviours, but where it is not possible to say that, *"but for"* any one of them, the loss would not have been incurred, the insured peril is regarded as a sufficient cause to satisfy the *"but for"* test.

THE COUNTERFACTUAL POSITION

The Court then moved on to consider whether losses had been sustained as a consequence of the insured peril. The Court had to construct a picture as to what would have been the position of each of the plaintiffs' businesses in the absence of the occurrence of the peril which was insured under the FBD policy. This is known as the "counterfactual". This approach would assist in establishing the base point against which the plaintiffs' losses could be calculated.

FBD argued that the counterfactual should be a scenario where there was no imposed closure, but where COVID-19 restrictions were still in place. An application of this position to the plaintiffs' policies would reduce the level of profits they would have made in that counterfactual scenario thereby reducing the losses they could recover under their policies.

In contrast, the plaintiffs argued that the relevant scenario should be one which involved no closure and no COVID-19 restrictions, such as the trading position for pubs before the outbreak. In agreeing with that position, McDonald J held that the *"...correct counterfactual is a world in which there is no imposed closure and no outbreaks within 25 miles of the plaintiffs' premises"*.

INDEMNITY

The Court also considered the definition of "Indemnity Period", which was defined in the policy as *"[t]he period beginning with the occurrence of the loss or damage and ending not later than the twelve months thereafter during which the results of the business shall be effected (sic) in consequence of the loss or damage"*.

The plaintiffs argued that this definition envisaged that the indemnity period would continue so long as the business was affected by the loss or damage. The Court noted that the plaintiffs were essentially saying that they were entitled to be compensated, post the period of imposed closure, for the losses that arise from changes in societal behaviour arising from the continuing presence of COVID-19 in the community. McDonald J stated that this seemed to go beyond the scope of the indemnity available under the policy. The definition of the indemnity period should be read in the context of the policy as whole, and the specific context of the words which immediately precede the relevant section, which stated that *"the company shall* **indemnify** *the Insured in respect of ... the loss of gross profit during the indemnity period..."* (emphasis added). The Court held that it is clear that FBD committed to indemnify the insured in relation to the loss of gross profit until the period of imposed closure came to an end or the indemnity period of 12 months came to an end (whichever is the earlier), which is entirely consistent with the principle that a policy of insurance is a contract of indemnity.

THE IMPORTANCE OF CONSIDERED DRAFTING

A key takeaway from this decision is the importance of considered drafting in policy wordings, in particular due to the Court's focus on the meaning of certain words used. This was demonstrated in the Court's approach to the interpretation of the word "following". The Court quoted caselaw which found that "after" is a more usual meaning of the word "following" rather than causative words such as "because of" or "as a result of". McDonald J also noted that the policy used language in other sections such as "resulting from" and "as a result of" which suggested that a different meaning was intended by the use of the word "following", and quoted from similar policies on the market which used wording like "in consequence of" and "arising directly from" rather than "following".

As the COVID-19 pandemic and nationwide lockdowns continue, this decision is sure to create some food for thought for the insurance industry, particularly for those involved in drafting policy wordings. There are a number of lessons to be learned from the approach of the Court in the test case, in particular the interpretation applied to policy wordings. Our dedicated Insurance & Reinsurance Department is available to advise (re)insurers and (re)insurance intermediaries in relation to policy interpretation.

In addition, our Commercial Contracts Group can assist in drafting and reviewing commercial contracts generally to ensure that the intended meaning of provisions is clear and unambiguous to the parties involved.

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