Claim No: FL-2020-000018

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS
COMMERCIAL COURT (QBD)
FINANCIAL LIST
FINANCIAL MARKETS TEST CASE SCHEME

Before Lord Justice Flaux and Mr Justice Butcher

B E T W E E N:

THE FINANCIAL CONDUCT AUTHORITY

Claimant

-and-

(1) ARCH INSURANCE (UK) LIMITED
(2) ARGENTA SYNDICATE MANAGEMENT LIMITED
(3) ECCLESIASTICAL INSURANCE OFFICE PLC
(4) HISCOX INSURANCE COMPANY LIMITED
(5) MS AMLIN UNDERWRITING LIMITED
(6) QBE UK LIMITED
(7) ROYAL & SUN ALLIANCE INSURANCE PLC
(8) ZURICH INSURANCE PLC

Defendants

SKELETON ARGUMENT OF ARCH (D1)

FOR CONSEQUENTIALS HEARING: 2 OCTOBER 2020

Bundles: The Court has been provided with electronic bundles. References below are to those bundles.
Pre-reading: The Court is respectfully requested to pre-read as per any suggested reading list provided by the Claimant. It will be helpful to have to hand the latest draft declarations.

Introduction

1. This is the Skeleton Argument of the First Defendant (**"Arch")** for the hearing of matters consequential on the Judgment handed down on 15 September 2020 (**"the Judgment"**).

2. There are three issues which this Skeleton Argument addresses:
   (1) The appropriate declarations;
   (2) Arch's application for a section 12 "leapfrog" certificate;
   (3) Arch's application for permission to appeal to the Court of Appeal.

(1) The appropriate declarations

3. The Court will be provided with a set of draft declarations which have been the subject of considerable discussion (some of which remains ongoing) between the FCA and the Insurers and which are intended to reflect the findings of the Judgment. [The latest differences between the FCA and the Insurers are shown on the draft].

4. At the time of writing there is broad agreement on the declarations **[N/5/1]** to give effect to the Judgment **[N/1/1]** insofar as it relates to Arch-1. In particular:

   (1) **Declaration 9:** which sets out what constitutes public authority action is agreed between the FCA and all insurers.
   (2) **Declaration 14.2:** which sets out that from 3 March 2020 there was an emergency likely to endanger life. This was common ground between the FCA and Arch.
   (3) **Declaration 14.3:** which sets out what constituted "actions or advice of government" and reflects the common ground between the parties, set out inter alia at paragraph 310 of the Judgment.
   (4) **Declarations 14.4-14.5:** which set out in relation to different categories of business whether there was or was not respectively a prevention of access to insured premises due to the actions or advice of government due to Covid-19, reflecting what is held in the Judgment at paragraphs 324-336.

5. Where there is, at the time of writing, a difference in terms of the proposed wording of the declarations between the FCA and Arch is in respect of parts of **Declaration 11** concerning causation and trends clauses.[1]

6. **Declaration 11.1** has been agreed between the parties and reflects the finding in the Judgment that COVID-19 (and other elements of the insured peril) do not fall to be considered as part of the "counterfactual" scenario.

[1] It will be noted that Declaration 14.1 is co-extensive with Declaration 11.

Arch seeks permission to appeal this declaration although there is no dispute about its wording: see below.

7. **Declaration 11.2(a)-(c)** sets out how the counterfactual when calculating an indemnity should be constructed in a manner which reflects the Judgment. It is **declaration 11.2(b)** which is relevant to Arch-1 and reflects paragraph 347 of the Judgment **[N/1/103]**. Again, Arch seeks permission to appeal this declaration although there is no dispute about wording: see below.

8. **Declarations 11.3(a)-(c)** sets out how the applicable trends clauses should operate. It is understood that **declaration 11.3(a)** will be agreed. However, the Insurers' draft wording at **declaration 11.3(b)** is not presently accepted by the FCA.

9. The draft declaration at 11.3(b) reflects the Judgment in that it states that if there was a measurable downturn in turnover due to Covid-19 prior to the insured peril being triggered, then the counterfactual may in principle take into account the continuation of that measurable downturn as a trend/circumstance in calculating the indemnity payable in respect of the period during which the insured peril was triggered and remained operative.

10. The FCA appears to seek to include wording to the effect that the counterfactual should not take into account the continuation of that downturn as a trend in calculating the indemnity payable in respect of the period during which the insured peril was operative. Or, possibly, in the case of Arch and Ecclesiastical (it is not understood why the FCA appears to consider that different Insurers should have different declarations on this point) it is in principle appropriate to take the downturn into account but "only if the particular effect amounts to a trend or circumstances … and is sufficiently distinct from the insured peril". But neither of the FCA's formulations are an accurate reflection of the Judgment.

11. Addressing the FCA's argument that the whole emergency had to be removed from the counterfactual, not just that part of the emergency which occurred

after the date on which the disease became notifiable, the Court held at paragraph 351 **[N/1/104]** (addressing the Arch-1 trends clause with emphasis supplied):

> "…Upon analysis, if it were correct, once an insured peril occurred, here the prevention of access due to government actions or advice due to the pandemic, the policyholder would in fact recover for its losses both before and after the occurrence of that insured peril, despite Mr Edelman QC's attempts to contend that this was not the effect of his argument. In any event, in the case of the Arch policy wording, whatever the merits of the argument it is precluded by the express words of the trends provision. **Any downturn in turnover before the date(s) when businesses closed pursuant to government advice or the Regulations was a trend or circumstance which affected the business before the Damage,** i.e. as manipulated before "the Prevention of access to The Premises due to the actions or advice of government due to an emergency which is likely to endanger life" within the meaning of (i) of the trends provision"

See also paragraph 389 of the Judgment **[N/1/113]** which gives the example of the church collection; and also paragraph 283 of the Judgment **[N/1/87]** which holds that "the counterfactual can only assume that the insured peril applies from the time that the restrictions are imposed, and only for as long as they are imposed".

12. The examples given by the Court, in particular at paragraph 351 of the Judgment **[N/1/104]**, make it clear that the Judgment finds that parts of the insured peril do fall to be taken into account (at least as a trend or circumstance) if they have resulted in a downturn before the full insured peril occurs.

13. To the extent that the FCA seek to argue (as suggested in correspondence) that the Court "did not rule specifically" on what amounted to a trend or circumstance within the meaning of the details of the quantification machinery for each policy and did not rule, for example, on whether a closure before the full trigger (or closure when instructed to do so but before the 21 and 26 March Regulations took effect) would fall within such a trend or

circumstance, Arch submits that the FCA did not ever argue that it would not do so. Indeed, the FCA did not descend to this level of detail.

14. The Insurers' proposed declaration is further consistent with the finding in the Judgment as regards causation as well as trends clauses: see, for example, paragraph 99 of the Judgment **[N/1/37]** (subsequent government measures, accepted at 111-112), 102 **[N/1/38]**, 113 **[N/1/40]**, 155 **[N/1/54]** and paragraph 296 **[N/1/89]** which provides as follows (emphasis supplied):

> "…Notifiable human diseases may manifest themselves in areas which are not constrained by boundaries such as a 25-mile radius, and the response of the authorities is likely to be to the whole of whatever outbreak there is, rather than parts. In the same way as for a number of the "disease clauses", we consider that there will be satisfaction of this requirement of the clause, **if and from the time that there has been a case of the disease within the 25 mile radius**, **and this can be regarded as having led to (resulted in) the closure or restrictions placed on such premises on 26 March because it was part of one cause of those restrictions,** which were imposed by the government as a response to a national picture which was made up of the individual local parts."

15. The FCA's approach implies that an occurrence of disease on, say, 1 April, can cause a government response on 26 March.

(2) Application for a section 12(1) "leapfrog" certificate

16. By an application notice dated 28 September 2020 **[O/4/1]**, Arch seeks a certificate pursuant to section 12(1) of the Administration of Justice Act 1969 **[S/1/1] (a "Leapfrog Certificate")** certifying that Arch's grounds of appeal are suitable for an appeal directly to the Supreme Court. In short, Arch seeks a Leapfrog Certificate on the basis of the exceptional public importance and urgency of this test case.

17. Arch seeks permission to appeal declaration 14.1 (and therefore declaration 11.1) and declaration 11.2(b). For the avoidance of doubt Arch does not seek to appeal any of the other declarations, including declaration 11.3 as per the Insurers' latest draft or declarations 14.2-14.5 as per the draft.

18. Arch's proposed grounds of appeal are as follows:

(1) **Appeal from declaration 11.2(b) as drafted:** The Court erred in holding that the insured peril under Arch-1 was a "composite peril" which included (1) the prevention of access; (2) the action of government and (3) the emergency or incident. The Court accordingly erred in holding that the comparison required for the assessment of the business interruption loss is between the performance of the business as a consequence of the prevention of access to the premises due to the actions or advice of the government due to the emergency and what the performance would have been had there been no emergency and thus no government actions or advice and no prevention of access to the premises.

(2) Having held (correctly) that the emergency was not an insured peril under Arch-1 and that social distancing advice and Regulation 6 of the 26 March 2020 Regulations **[J/16/4]** did not prevent access to insured premises, the Court was wrong to hold that where insured premises were required to be closed, the losses which could be recovered would include losses which the policyholder would have suffered in any event by reason of the emergency and by the social distancing advice and Regulation 6.

(3) **Appeal from declaration 11.1 as drafted:** The Court further erred in its construction of the Arch-1 'trends' clause, in particular that the clause required word "Damage" should be replaced with the "composite peril", thereby reversing-out both the Damage and whatever had caused the Damage, such that the 'trends' clause should operate as if the whole Covid-19 pandemic and all its consequences was part of the peril insured against.

(4) The Court was further wrong to hold that the decision in Orient-Express Hotels Ltd v Assicurazioni Generali SpA [2010] Lloyd's Rep. I.R. 531 **[J/106/1]** was distinguishable from the present case and/or should not be followed in that it was wrongly decided. It was correctly decided.

19. By way of background to this application:

(1) The Framework Agreement concluded by the FCA and the Insurers, dated 31 May 2020 **[R/1/1]**, provides that the parties shall act at all times constructively and in good faith to promote the mutual objective (clause 6.1), namely "to achieve the maximum clarity possible for the maximum number of policyholders (especially, although not solely SMEs) and their insurers consistent with the need for expedition and proportionality" (recital I).

(2) Clause 8.3 of the Framework Agreement **[R/1/11]** states as follows: "In particular, and without prejudice to their obligations to seek expedition above, the Parties agree to explore the possibility and appropriateness of seeking a leapfrog appeal to the Supreme Court under PD 1.2.17 and 3.6 of the Practice Direction of the Supreme Court."

(3) The FCA put the Supreme Court on notice of this agreement and Herbert Smith Freehills told the defendants by email on 28 July 2020 **[Q/1/1]** that the Registrar of the Supreme Court had told them that:

> "in principle the Supreme Court could accommodate a hearing on an expedited basis during Michaelmas term 2020, subject to the point that the final decision would be for the President, Lord Reed, at the time. The Registrar also noted that Lord Reed was already aware of this matter and that in appropriate urgent previous cases the Supreme Court has sat out of term time in September."

20. The Court should grant the Leapfrog Certificate because Arch's grounds of appeal satisfy the statutory conditions for a Leapfrog Certificate in section 12(3A) of the Administration of Justice Act 1969 Act **[S/1/1]**, in that each of those grounds of appeal involves a point of law of general public importance, and:

a. this test case "entail[s] a decision relating to a matter of national importance or consideration of such a matter" (s.12(3A)(a) of the 1969 Act);

b. the result of this test case is "so significant", whether considered on its own or together with claims by policyholders that are likely to follow from it, "that … a hearing by the Supreme Court is justified" (s.12(3A)(b)); and

c. "the benefits of earlier consideration by the Supreme Court outweigh the benefits of consideration by the Court of Appeal" (s.12(3A)(c)).

21. As this Court knows, this test case concerns 21 lead policy wordings and, as noted in paragraph 7 of the Judgment **[N/1/4]**, may potentially affect around 700 types of policies across 60 different insurers and around 370,000 policyholders. The Arch-1 wording was selected by the FCA to represent a form of "prevention of access" wording which will be relevant to large numbers of policyholders in the UK.

22. Ultimate legal certainty is required in circumstances where neither individual policyholders nor reinsurers are party to the test case or bound by its outcome as a matter of res judicata. It is common ground that very large numbers of policyholders have suffered significant losses as a result of the Covid-19 pandemic and the UK Government's response to it. The issues therefore need to be authoritatively determined as a matter of urgency as reflected in the terms of the Framework Agreement **[R/1/1]**.

23. The grounds of appeal set out above concern the extent to which policyholders' losses fall within the scope of the Arch-1 wording. The proposed grounds of appeal have a realistic prospect of success. If an appeal is required to proceed via the Court of Appeal, that will significantly prolong the length of these proceedings (especially bearing in mind the risk that an appeal to the Supreme Court ultimately occurs in any event).

24. The application was made within 14 days of the Judgment, i.e. the period specified by section 12(4) of the 1969 Act **[S/1/1]**, and prior to the deadline stated in paragraph 4 of the order made by Flaux LJ and Butcher J dated 15 September 2020 **[N/2/1]**. If the Court grants a Leapfrog Certificate as requested, Arch will promptly apply to the Supreme Court for permission to appeal pursuant to section 13(1) of the 1969 Act **[S/1/1]**.

25. It is to be noted that the FCA has made its own leapfrog application, as have the other Insurers (barring Zurich whose policies were held not to respond). It is therefore common ground that this Court should grant a Leapfrog Certificate. Whilst it is of course for the Court to decide whether a Leapfrog Certificate is applicable, the fact that the FCA and the Insurers are agreed that this is the appropriate way forward for an appeal is a strong indication that the Court should accede to the application.

(3) Permission to appeal to the Court of Appeal

26. Arch applies for permission to appeal to the Court of Appeal on the same grounds as set out above, in the event that the Leapfrog Certificate is not granted and/or the Supreme Court otherwise refuses permission to appeal.

27. In accordance with CPR 52.6, permission to appeal may be given where (a) the court considers that the appeal would have a real prospect of success; or (b) there is some other compelling reason for the appeal to be heard.

28. The first basis on which permission to appeal may be given ("real prospect of success") is precisely the same test as that which the courts apply when considering summary judgment: see r.24.2. The rationale is the same. In Swain v Hillman [2001] 1 All E.R. 91, CA, Lord Woolf MR famously explained that under r.24.2 the court had to consider whether there was a "realistic, as opposed to a fanciful, prospect of success".

29. Arch submits that it can clearly satisfy this hurdle.

    (1) At the heart of the Judgment (see in particular paragraph 347 as affects Arch **[N/1/103]**) is the characterisation by the Court of what is insured as a "composite peril", i.e. in the case of Arch-1 an insured peril which includes the prevention of access and the cause(s) of the prevention of access, namely the government regulations and the emergency.

(2) This characterisation is, with respect, a novel approach to identifying the insured peril with which the Court of Appeal may well disagree. In Arch's most respectful submission, there is no rule of law or fact that requires the counterfactual to pass a test of realism or non-artificiality (see paragraph 348 of the Judgment **[N/1/103]**) and the correct approach is to apply the contract in accordance with the parties' intentions. This would lead to the correct determination that what was insured against under Arch-1 was only prevention of access in certain circumstances and therefore that it is only prevention of access (and not the emergency or the regulations – which merely set out the circumstances in which a prevention of access will constitute an insured peril) which is "stripped out" of the counterfactual.

(3) There is a realistic possibility that the Court of Appeal will find that having held that the emergency was not an insured peril under Arch-1 (Judgment, paragraph 309 **[N/1/93]**) and that social distancing advice and Regulation 6 of the 26 March 2020 Regulations **[J/16/4]** did not prevent access to insured premises (see Judgment, paragraphs 328-329 **[N/1/98]**), this Court should have held that where insured premises were required to be closed, the losses which could be recovered should not include losses which the policyholder would have suffered in any event (i.e. if not closed) by reason of the emergency and by the social distancing advice and Regulation 6.

(4) It is further submitted that the Court of Appeal may well come to a different view than this Court on the Arch-1 trends clauses. In the Judgment (see paragraph 349 **[N/1/103]**) the Court has inserted what it regarded as the composite peril in place of the word "Damage". However this, with respect, is not correct. It would mean that for the purposes of calculating an indemnity on orthodox principles, policyholders under Arch-1 become entitled to reverse-out both the Damage and whatever had caused the Damage.

(5) Finally, there is a real prospect of the Court of Appeal finding that Orient Express Hotels Ltd v Assicurazioni Generali SpA [2010] Lloyd's Rep. I.R. 531 **[J/106/1]** is not distinguishable from the present case and/or should in any event be followed. It was correctly decided both at the Tribunal stage (before, inter alios, George Leggatt QC as he then was) and at the Commercial Court on appeal before Mr Justice Hamblen (as he then was).

30. The second basis on which permission to appeal may be given ("some other compelling reason") would, it is submitted, include the public importance of this case for insurance claims and particularly in the context of the ongoing pandemic. Arch will say that for the same reasons as set out above in respect of the s.12 applications, this is such a case.

31. In particular, ultimate legal certainty is required in circumstances where neither individual policyholders nor reinsurers are party to the test case or bound by its outcome as a matter of res judicata and where there are enormous potential losses. The reasons set out above constitute compelling reasons that these matters should be determined authoritatively and as a matter of urgency as reflected in the terms of the Framework Agreement.

Extension of time

32. If the Court grants permission to appeal to the Court of Appeal, Arch respectfully requests the Court to grant a further extension of time for Arch to file an Appellant's Notice at the Court of Appeal (pursuant to CPR 52.12(2)), until 14 days after the date on which the Supreme Court determines any application for permission to appeal.

33. To the extent that the Supreme Court grants permission, then this further extension of time will become redundant. Even if the Court refuses to grant permission for Arch to appeal to the Court of Appeal, if it grants the Leapfrog Certificate, then it would still be appropriate for the Court to grant an extension of time to file an Appellant's Notice at the Court of Appeal, until 14

days after the date on which Supreme Court determines any application for permission.

34. If the Court grants a Leapfrog Certificate but refuses to grant such an extension, time for seeking permission from the Court of Appeal would expire prior to any decision by the Supreme Court concerning Arch's permission application.

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30 September 2020

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