



In this week's Insurance Bulletin:

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## 1. REGULATION AND LEGISLATION

### **UK: third country EU equivalence for financial services in doubt – but does it matter?**

**The UK’s chances of obtaining regulatory equivalence with the EU for financial services are in doubt, as the UK and EU have missed their self-imposed deadline of 30 June 2020 to complete the UK’s equivalence assessment. However, much of the (re)insurance industry is already prepared for equivalence not being obtained.**

In the context of (re)insurance, the European Commission can grant regulatory “equivalence” to a third country (e.g. the UK) in three ways:

1. where (re)insurance contracts entered into in the third country are to be treated the same as if they were entered into with EU (re) insurers;
2. where EU groups have subsidiaries in equivalent third countries, those subsidiaries can follow local capital requirements instead of Solvency II; and
3. where equivalent third country firms have activities in the EU, the EU supervisors can rely on the group supervision conducted by the equivalent third country regulator.

On 23 June 2020, the Chancellor, Rishi Sunak, announced<sup>1</sup> that the UK intended to divert from parts of Solvency II, including the operation of internal models and reporting requirements for insurers, expecting to publish a Call for Evidence in Autumn 2020. This statement, combined with the continued uncertainty of the UK-EU post-Brexit relationship, have cast doubt over the outcome of the equivalence assessment process.

However, the impact of a “non-equivalence” finding might be limited. Several UK (re)insurers have contingency plans in place, with subsidiaries established in Dublin, Luxembourg and Belgium. Those without such plans may still be able to write certain classes of business,

such as MAT, across the UK-EU border on a services basis. In addition, equivalence would not be necessary if the UK and the EU agree a deal on their future relationship contains an equivalent to passporting rights, which will cease to apply to UK (re) insurers after 31 December 2020.

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### **Footnotes**

- 1 <https://www.parliament.uk/business/publications/written-questions-answers-statements/written-statement/Commons/2020-06-23/HCWS309/>

## 2. COURT CASES AND ARBITRATION

### **England & Wales: Update on the FCA test case on the validity of COVID-19 business interruption claims**

**Last month, we reported on the progress of the FCA test case<sup>1</sup>, after the FCA had filed its claim and the first Case Management Conference had taken place.**

Since then, the eight defendants have filed their Defences to the claim (on 23 June), the FCA has served its Reply and the FCA has lodged its skeleton argument for the trial. There has also been a further CMC, at which directions were given for the trial. As a result, there are now many hundreds of pages of pleadings and argument so the following is simply an attempt to encapsulate some of the important points in issue.

Some of the key arguments arising from the Defences are as follows:

1. There is no basis for the FCA’s assumption that, where a policy does not expressly define and exclude epidemics and pandemics from its cover, the policy was intended to cover them.
2. In relation to those policies which require an occurrence to take place at or within a defined area of the insured premises, an insured would need to prove the

occurrence of a specific cases of COVID-19 within the relevant area, rather than relying on statistical analyses.

3. Insureds would also need to prove that the specific case or cases identified gave rise to the interruption to business, and not restrictions imposed on a wider basis to suppress the spread of COVID-19 generally.
4. Generally, the FCA's case that all measures and guidance put in place by the Government constitutes closure, or prevention or hindrance of access to insured premises is denied. For example, it is denied that social distancing measures give rise to closure or any such hindrance of access.
5. Any business interruption loss must be caused by an insured peril, i.e. that the loss would have occurred 'but for' the local occurrence of COVID-19. The Government measures were not put in place as a result of any local occurrence(s) of COVID-19, but to prevent the spread of COVID-19 across the nation. As such, in the absence of local occurrences of COVID-19, the businesses would have been in exactly the same position in any event.

The second Case Management Conference took place on 26 June. At this hearing, Flaux LJ and Butcher J directed that the Hospitality Insurance Group Action and the Hiscox Group Action are permitted to intervene and make both written and oral submissions at the hearing. The judges also decided the procedural timetable and directed that:

1. the seventh defendant, Royal & Sun Alliance Insurance Plc, is not permitted to rely on factual evidence regarding a policy wording outside the representative sample as evidence of the cover available in the market generally;
2. the FCA is not permitted to rely on expert evidence relating to two policy wordings of the third defendant, Ecclesiastical Insurance Office Plc as to the nature of local outbreaks of COVID-19; and

3. the FCA is permitted to amend its Particulars of Claim in respect of the prevalence of COVID-19 in the UK. On this latter point, the court mooted the possibility of a second shorter hearing in the Autumn dealing with factual points (as opposed to points on principle) on the prevalence of COVID-19 in the UK.

The FCA filed both its Amended Particulars of Claim and its Reply and Defence to Counterclaims on 3 July. In its Reply and Defence to Counterclaims, the FCA rejected the Defences as being dependant *"upon adopting unduly restrictive meanings of particular words (such as 'prevention' and 'occurrence') and approaches to proof as to the presence of COVID-19, and causal tests prescribing unrealistic, impractical counterfactuals, depriving the cover clause of much of its apparent and intended scope"*. The FCA argues that this does not accurately reflect the understanding of the reasonable person in the parties' position. The FCA filed its skeleton argument for the trial on 13 July.

The substantive hearing is due to take place over eight days from 20 July before Flaux LJ and Butcher J.

If you would like any more detail on the FCA test case and associated issues please contact **Christopher Foster** (christopher.foster@hfw.com), **Jonathan Bruce** (jonathan.bruce@hfw.com), **Rupert Warren** (rupert.warren@hfw.com) or your usual HFW contact.

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#### **Footnotes**

- 1 <https://www.hfw.com/insurance-bulletin-june-2020>



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**“Lloyd’s proposals highlight the need for the insurance industry to collaborate with governments to protect customers during their recovery from COVID-19, and to strengthen the resilience of businesses and society to future systemic risks.”**

### 3. MARKET DEVELOPMENTS

#### **UK: Lloyd’s proposals on protection against a future wave of COVID-19**

**Lloyd’s has recently published a white paper on supporting global recovery and resilience for customers, and outlining how the global insurance industry could respond to COVID-19. The paper sets out solutions to offer greater protection against another wave of COVID-19 and future systemic risks.**

Lloyd’s proposes three frameworks, focusing on economic recovery and building greater resilience.

##### **1. ReStart**

The Lloyd’s ReStart framework is a potential solution for non-damage business interruption resulting from further waves of COVID-19. ReStart is aimed in particular at supporting SMEs by providing business coverage and supporting re-opening through the pooled capacity of various Lloyd’s market participants. This framework should support businesses in their recovery and provide them with greater certainty of business interruption coverage, whilst protecting insurers by pooling risks.

Lloyd’s hopes that the framework could be applied, not only in the Lloyd’s market, but also globally. Lloyd’s also intends for this framework to work alongside their second framework, Recover Re.

##### **2. Recover Re**

The Recover Re framework is ‘after the event’ insurance, aimed at insuring Covid-19 and future pandemic risks. It provides immediate and long-term relief and recovery in respect of non-damage business interruption arising out of COVID-19. The framework envisages collaboration between the insurance industry and the government to inject capital into the economy in order to support customers who are unable to support themselves easily with individual cash injections.

The insurance industry possesses the necessary risk management expertise and infrastructure to aid SMEs directly, thereby facilitating capital injection into the economy, whilst the government would guarantee premiums and provide the cash flow needed to pay claims in the early part of policy periods.

##### **3. Black Swan Re**

Black Swan Re is a government-backed reinsurance framework designed to insure against the risk of “Black Swan” events (i.e. systemic catastrophic events, such as pandemic-related major public health emergencies, global cyber-attacks, or critical supply chain failures). It would enable insurers to provide cover for non-damage business interruption and it provides better protection from the long-term detrimental effects of such events.

The insurance industry would pool capital to provide the reinsurance in case of Black Swan events, with the capital guaranteed by the government, should it become inadequate.

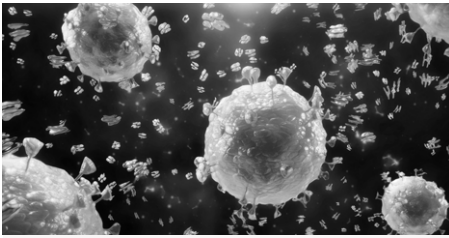
Lloyd’s proposals highlight the need for the insurance industry to collaborate with governments to protect customers during their recovery from COVID-19, and to strengthen the resilience of businesses and society to future systemic risks. This national and global collaboration would help to mitigate risk for both insurers and government while protecting consumers from Black Swan events.

We have seen the catastrophic impact that COVID-19 has had on the insurance industry and the economy as a whole. By refining and implementing the frameworks suggested by Lloyd’s, the hope is that society will be better prepared to handle the next pandemic and resist an economic downturn.

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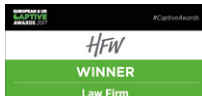
Additional research by Samantha Cash (Trainee Solicitor, London)



We are working with clients across our international network to help them minimise the impact of COVID-19 on their business and to prepare for what's next. To find out more, visit our dedicated Covid-19 hub: [www.hfw.com/covid-19](http://www.hfw.com/covid-19) or speak to your usual HFW contact.

We are aware that this is a challenging time for our clients, and we have a number of legal training sessions that we can deliver remotely to our clients. We have a flexible approach so we can provide appropriate content in a format that works for your team. Please get in touch with your usual HFW contact or with our Client Training Partner, **Adam Strong** ([adam.strong@hfw.com](mailto:adam.strong@hfw.com)), if you would like to see a list of topics or discuss a tailored session to look at issues relevant to your team.

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