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Policy Analysis

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Early French, German Court Rulings Raise Bar for Axa, Other Insurer Arguments Against Covering Business Interruption Losses

EXECUTIVE SUMMARY:

Capstone believes interim court judgments in France and Germany ordering Axa SA (CS on the Paris exchange) and an unnamed German insurer to cover operating losses due to COVID-19 raises the bar for insurers arguing that pandemic-related losses are not included in some of their business interruption (BI) policies. While the early rulings are only the beginning in the saga of BI legal challenges across Europe, our analysis of the judges' interpretations signals hurdles for insurers with ambiguous policies litigating to avoid paying claims from COVID-19-related operating losses. Insurers are increasingly offering voluntary cover to small and mid-sized (SME) businesses in France and Germany—a sign we believe suggests mounting legal pressure.

We believe these early judgments indicate that the risk from legal battles in insurers' future is not fully appreciated. While most insurers maintain that the vast majority of policies exclude cover for pandemics, these recent judgments may indicate that insurers underestimate the number of cases where policy coverage is due. We expect many insurers to use similar arguments that were made by both insurers in both the French and German cases. Regarding the French judgment, Axa noted that only a few hundred contracts would be affected. The precedent value of these judgments remains limited to policies with similar language.

Based on our analysis of the interim court orders in France and Germany—issued on 22nd May and 29th April, respectively—Capstone believes the following factors raise the bar for insurers litigating against COVID-19-related BI coverage:

- **State orders restricting business activities as a result of the pandemic can, in practice, be considered as closure orders.** In France, Axa argued that the government's order did not force businesses to close, that the restaurant in question could remain open, and that it was the restaurant owner's decision to close. The Paris commercial court (*Tribunal de Commerce de Paris*) concluded that the order prohibiting restaurants from allowing the public to enter should be considered as an administrative closure of the restaurant. In Germany, the insurer argued that relevant state orders did not force business closure and that certain activities—such as overnight stays for business trips and restaurant takeaway service—could continue. The Mannheim regional court, however, ruled that a government measure to restrict tourists and travel and encourage working from home has, in effect, caused a closure.

- **The legal nature of the government orders appears irrelevant in court.** Axa argued that the government's order was not an "administrative closure," so protections under the policy were not triggered. The court dismissed this claim, noting that, whether the order is executed by the prefect or health minister, orders can be considered "administrative decisions." The insurer in the German case argued that the insurance policy was not triggered as there was no "company-specific administrative act," and that the general order to limit physical contact does not trigger coverage. The court noted that, under the Infection Protection Act, an administrative order does not need to be a company-specific or individual administrative act. The court appeared to consider whether such an order forces a business to close in practice.

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- **Pandemics should be explicitly excluded from coverage, and a reference to "notifiable diseases" can be assumed to cover COVID-19.** The French court dismissed Axa's argument that general events, such as pandemics, cannot be insured, and Axa should have explicitly excluded this particular risk. Similarly, the German court noted that the insurer should have drafted an exhaustive list of diseases if it wanted to limit coverage to certain diseases. A general reference to the "notifiable diseases" in the Infection Protection Act, as was present in the case at hand, can be assumed to include COVID-19. The court considered how an average policyholder without any special knowledge of insurance law would interpret the policy. The German civil code notes that "any doubts regarding the interpretation of general terms and conditions are at the expense of the user," which, in this case, is the insurer.

- **Intention of the parties and inadequate premium calculations are irrelevant.** The German court notes that the mere fact that none of the contracting parties anticipated an event such as COVID-19, or the insurer did not recognize this risk and take it into account when determining insurance premiums, is no reason to interpret the contract in such a way that the event is not covered.

We stress that both court orders are interim judgments, handed down after expedited proceedings. Lengthy and thorough debates on the substance will take place in the main proceedings. Should the policyholders win the main proceedings, the rulings will set a precedent for cases in which insurers have highly similar policies, as many bars and restaurants do, with ambiguous language. Insurers argue that such policies account for a small percentage of their property and casualty (P&C) contracts. Additionally, each policy must be litigated separately, and the courts in different countries will consider different factors, such as national consumer protection laws.

Shortly after the judgment in France was made public, Axa issued a press release noting that it would appeal the judgment on the basis that it was the result of expedited proceedings without proper debate on the substance of the argument. On 26th May, the insurer noted that it was seeking an "amicable" outcome and intended to cover the majority of claims from restaurant owners in which the policy contained ambiguous language. Axa estimates there would be a few hundred contracts that provide BI coverage when there is no physical damage involved, including that of the restaurant involved in the case. The issue should only come up regarding contracts concluded through insurance broker SATEC Group. Axa reportedly contacted insured customers and proposed paying 20% of their turnover (excluding tax) for a period of up to four months. If the restaurants accept the settlement, they cannot launch further legal proceedings against Axa.

French Regulator Takes Stock of BI Policies and Prohibits Voluntary BI Rebates

Around the same time that French insurer Crédit Mutuel began offering rebates to some of its small and mid-sized enterprise (SME) clients, the French Prudential Supervision and Resolution Authority (ACPR) issued a statement noting that insurers should be prudent, and that funds should not be used to cover events that are explicitly excluded in the contract.

Before this, the ACPR decided to draw up an inventory of the main contracts sold in the French market. The result of its findings will be sent to the ACPR's board throughout June and July. The ACPR does not provide any detail about its ultimate intentions for taking stock on the terms that occur most frequently. Its current ambitions do not appear to mirror those of the UK's Financial Conduct Authority

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(FCA), which has taken a very active role in the BI debate in the UK (see "Business Interruption Quick Take: UK Regulator to Seek Urgent Legal Clarity as Litigation Funder Joins Insurer Debate," 1 May 2020).

BaFIN and German Local Authorities Encourage Voluntary BI Coverage

In early April 2020, several Bavarian insurers joined forces with local politicians, the regional Chamber of Commerce, and relevant trade bodies, agreeing to offer payments to the hospitality industry in Bavaria. The 15% contribution made by the insurers has set a standard throughout the industry, as an increasing number of insurers offer payments of up to 15% of operating losses, even when coverage is clearly excluded.

BaFIN's executive director of insurance and pension fund supervision, Frank Grund, noted that insurers should not pay in cases where insurance coverage is clearly excluded in case of a general administrative order, echoing the French ACPR's conclusion. However, in ambiguous situations, Grund recommends that "mutually acceptable solutions" should be found to avoid expensive legal disputes, prevent loss of reputation, or even gain new customers.

A DEEPER LOOK

Background

The debate regarding business interruption (BI) insurance coverage during the COVID-19 pandemic expands across continental Europe. Court cases have been launched in several countries, which may have wide-ranging implications for insurers. At the same time, some insurers are providing voluntary rebates, a move that has received mixed reviews from various regulators. Capstone has written recently on business interruption (BI) insurance in the United States and United Kingdom (See "COVID-19 US Business Interruption Insurance Policy Day Analysis: Retroactive Coverage Unlikely; Physical Damage Arguments Central," 19 May 2020, and "COVID-19 Business Interruption Payouts Risk Builds as UK Redress Scheme Increasingly Likely, Enterprise Act Successfully Invoked," 21 May 2020).

French Commercial Court Orders Axa to Cover Losses as a Result of Business Closure

On 22 May 2020, the Paris commercial court (*Tribunal de Commerce de Paris*) issued an interim order forcing Axa to cover around two months of operating losses, worth €45,000, to the owner of four restaurants, Stéphane Manigold.[1] Manigold initially claimed that around €73,000 would be due regarding one particular restaurant (La Maison Rostang) and more than €1 million for all four of his restaurants (including Le Bistrot d'à côté Flaubert, Substance, and Contraste). In the meantime, the court has appointed an independent expert to assess the true extent of Manigold's losses.

Manigold insured himself against operating losses as a result of state-ordered closure of his restaurants. One of the clauses of his insurance contract stated that Axa would provide compensation for operating losses in the event of an "administrative closure" imposed by the policy or health services.

[1] A copy of the judgment is available (in French) at: https://www.leclubdesjuristes.com/wp-content/uploads/2020/05/Ordonnance-du-22-mai-2020_Rostang-AXA.pdf

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Axa raised several different grounds defending its position. First, Axa argued that events such as a pandemic could not be insured. The premiums charged to Marigold did not take into account coverage of this risk. The court dismissed Axa's arguments, noting that "Axa does not rely on any legal provision that a pandemic cannot be insured. It was up to Axa to exclude this particular risk. However, it appears that losses resulting from a pandemic are not excluded from the contract concluded between both parties."

Second, Axa France IARD claimed that preconditions (i.e., that the application of the administrative closure clause must note the prior occurrence of a guaranteed event in respect of operating loss) prevent Manigold from claiming coverage. However, the court dismissed this claim, failing to find any contractual reference to support it.

Third, Axa argued that subtle differences in language meant that the French lockdown did not result in an administrative closure, which would have been covered under Axa's policy. Axa argued that there is a distinction whether the closure was ordered by the police or health and safety authorities versus the ministry of solidarity and health. In this regard, the court noted that an order by either can be considered an administrative decision.

Finally, Axa noted that the government's closure order on 14th March did not force business to close, rather it ordered business to not "welcome the public," and that the restaurant in question could remain open and offer takeaway or delivery services. Hence, Axa claimed the restaurant was closed not as a result of the government's order, but as a result of the decision of its owner. Dismissing the claim, the court noted that:

> "Le Bistrot d'à côté Flaubert has never offered takeaway meals or delivery service [prior to the pandemic]. Assuming that this would be possible, not having resorted to this does not take away the ban on receiving the public—which is fundamental for a traditional restaurant…The prohibition on receiving public should be considered as a total or partial administrative closure of the restaurant."

Immediately after the judgment was released at 4 pm CET on 22nd May, Axa announced a press report indicating that it would appeal the decision.[2] The insurer stressed that the decision was merely a provisional ruling and that substantive arguments were not part of the summary proceedings before the court.

Should Manigold win the main proceedings, this case may have important repercussions for Axa and other insurers, as many bars and restaurants have insurance policies in place that are comparable to those of Manigold. Arguably, the Manigold case may set a precedent for the broader industry in France. However, we would highlight that the precedent value of any judgment will be limited to insurance policies that are identical or highly similar to the policy concluded between Manigold and Axa. Manigold told Reuters that he received calls from the UK, Spain, US, and South Africa asking for details of his contract and the court ruling.

Following the judgment, several well-known French chefs renewed pressure on their insurers and demanded coverage of at least 15% to 25% of losses. The hospitality industry is one of the strongest

[2] https://axalive.fr/article/axa-jugement-stephane-manigold

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advocates claiming for compensation (see "P&C Insurers: COVID-19 Business Interruption Claims, Retroactive State Bills Present Tail Risks for TRV, CB, HIG, and WRB," 17 April 2020).

In its 22nd May press release, Axa further added that there are about 200 contracts in its portfolio, across a wide variety of business sectors, that explicitly provide coverage for the current pandemic.

On 26th May, Axa confirmed that it will appeal the commercial court's ruling, but CEO Thomas Buberl added that the insurer is seeking an amicable outcome and was intending to cover the majority of claims from restaurant owners that contained ambiguous language. Attempting to limit the damage, Buberl noted that "these contracts represent less than 10% of contracts with restaurant owners." Axa's press release details that there would be a few hundred contracts that provide BI coverage when there is no physical damage involved. Axa further noted that the issue only came up regarding insurance contracts concluded through broker SATEC. Hence, the bulk of its commercial insurance policies allegedly remain unaffected. Axa noted that the vast majority of Axa France's contracts, including its standard contract, provide that a generalized event—such as the current pandemic—cannot bring into play the contractual coverage.

Axa reportedly contacted insured customers and proposed paying 20% of their turnover (excluding tax) for a period of up to four months. If the restaurants accept the settlement, they cannot launch further legal proceedings against Axa.

Axa further noted that it would contribute c. €500 million to support French SMEs, in addition to plans already announced by French insurers to invest €1.7 billion in French companies. This is separate from ongoing discussions at the national level by the Ministry of the Economy and Finance and the insurance industry to set up a global solidarity fund to compensate for firms' operating losses.

In the meantime, on 6th May, the French Prudential Supervision and Resolution Authority (*autorité de contrôle prudentiel et de résolution* or ACPR) decided to follow the UK Financial Conduct Authority's (FCA) footsteps and get involved in the BI debate (see "Business Interruption Quick Take: UK Regulator to Seek Urgent Legal Clarity as Litigation Funder Joins Insurer Debate," 1 May 2020).[3] The French insurance supervisor notes that, typically, such insurance policies only cover a specific physical damage caused to the property (e.g., as a result of fire, theft, machine breakdown) that results in lost revenues. The ACPR decided to draw up an inventory of the main contracts that are sold in the French market. The result of its findings will be sent to the ACPR's board in June and July. The ACPR does not provide any other detail about its ultimate intentions with the information.

French Regulator Prohibits Insurers from Providing Voluntary BI Coverage

Following the trend of motor insurers offering voluntary rebates, including French mutual insurers MAIF and Matmut, rebates have also been given regarding BI policies (see "Rebates, Suspended Premium Payments on the Horizon for General Insurers as FCA Focuses on Product Value, Customers," 6 May 2020, and "UK Motor Insurers Resist Pressure to Provide Rebates as Drivers Stay Home; Limits to Renewal Price Increases Delayed," 14 April 2020).

[3] https://acpr.banque-france.fr/sites/default/files/medias/documents/20200506_communique_presse_garantie_pertes_exploitation.pdf

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French bancassurance firm Crédit Mutuel (and its CIC subsidiary) deemed it a "moral duty" to reimburse several SME policyholders holding BI policies. Crédit Mutual is the second-largest P&C insurer in France. The rebate—called the mutual recovery stimulus premium (*prime de relance mutualiste*) and varies between €1,500 and € 20,000—costs the firm €200 million in total and is intended to cover operating losses caused by the COVID-19 pandemic.

Crédit Mutuel's action triggered Crédit Agricole to refund €200 million to its SME policyholders.

Notably, these reimbursements have triggered interest from the French National Federation of General Insurance Agents (*agent generale d'assurance* or AGEA), which stated in a letter to the French government and the ACPR that the action of Crédit Mutuel should not be interpreted as meaning that business interruption insurance covers losses that result from the COVID-19 pandemic.[4]

Moreover, the chair of AGEA argued that the insurance policy in question (the Acajou contract) appears to cover operational losses that result from COVID-19. Article 17.1—titled Basic Cover—details that the insurer covers, "pecuniary losses that you may suffer due to the interruption or reduction of your activity," and also from, "a measure prohibiting access by administrative or judicial authorities, following an event external to your activity and the premises in which you exercise it." Based on our analysis, neither the exclusions from the cover in article 17.4 or the general exclusions in article 29 explicitly exclude pandemics, epidemics, or situations of health risks. Should this be the case, the insurer would have to pay out closer to €1 billion than €200 million. This is one of the issues the ACPR is currently examining.

However, Crédit Mutuel states that article 29 of its terms and conditions excludes damage caused by microorganisms. According to Crédit Mutuel, around 27,000 customers would be insured for operating loss by the Acajou contract.

In offering the discount, the insurer wrote letters to its clients. While it was rumored that if recipients wanted to accept the discount, a precondition was to waive their right to bring legal proceedings, the official letter sent to clients does not appear to contain a clause where the insured sign away some of their rights. Instead, the insurer stressed that, "the general conditions of its contracts provide for an exclusion for damage caused by microorganisms, such as the coronavirus." Hence, article 29 overwrites the general principle stated in article 17.1.

AGEA noted that if COVID-19 losses would be covered by the Acajou contract, Crédit Mutuel's action would be "morally shocking," and its behaviour would qualify as false advertising and have to be taken extremely serious from a legal point of view.

The ACPR issued a statement on 21 April 2020, noting that insurers should be prudent in these unprecedented times and that funds should not be used to cover events that are explicitly excluded in the contract.[5] The statement continued by noting that coverage relating to business interruption as a result of a pandemic cannot be adequately valued without a compulsory state guarantee scheme. Total losses in the industry in France are estimated to be around € 60 billion.

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[4] http://www.agea.fr/actualites/27-04-2020/alerte-mesures-du-credit-mutuel-cic
[5] https://acpr.banque-france.fr/sites/default/files/medias/documents/20200421_cp_engagements_fonds_propres.pdf

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BaFIN and Germany Local Authorities Encourage Voluntary BI Coverage by Insurers, Mutuals

In Germany, voluntary rebates are becoming more common after several Bavarian insurers joined forces with local politicians, the regional Chamber of Commerce, and relevant trade bodies to reach an agreement to offer payments to the hospitality industry in Bavaria. State subsidies cover around three-quarters of hoteliers' and restaurateurs' losses. Initially, three underwriters—including Allianz SE, die Haftpflichtkasse, and Versicherungskammer Bayern (the latter two being mutual insurers)—offered to cover half of the rest, or 15% of the total cost. Nuernberger Versicherung and Zurich Insurance Group Ltd. are reportedly preparing to join the voluntary commitment. Other insurer—including Barmenia Versicherungen AG, HDI Global SE, and Signal Iduna—were considering joining the effort, but requested several preconditions before joining.

The consortia of insurers would make up around 10% to 15% of the damage that would normally be covered by an insurance policy.[6] Payments were made to policyholders with BI insurance policies (*betriebsschließungsversicherung*) totaling around €500 million, according to the German trade association of German insurers (*Gesamtverband der Deutschen Versicherungswirtschaft* or GDV).

According to insurers and the GDV, the relevant BI policies in Germany very clearly exclude coverage as a result of pandemics. They noted that policies cover business closure resulting from an infectious disease/virus that emerges within a business. Regarding COVID-19, they argue the closure was not a result of an outbreak of a virus within the business premises, so coverage does not apply.

BaFIN's executive director of insurance and pension fund supervision, Frank Grund, noted that insurers should not pay in cases where insurance coverage is clearly excluded in case of a general administrative order. This statement is identical to the ACPR's conclusion and deciding otherwise, in Grund's eyes, would harm the "insured collective." In ambiguous situations, Grund recommends that "mutually acceptable solutions" should be found. This should be done to avoid expensive legal disputes, prevent losing reputation, or even gain new customers.

It seems the Bavarian deal has set an example for the industry. Zurich, for example, offers to cover 15% of the loss of sales when a policy allegedly does not cover damages that result from business closure due to the pandemic. A case of preventive closures to contain a pandemic is not insured or cannot be insured at all, according to a Zurich spokesman. The majority of the losses are covered by the state by emergency aid or state loans. Allianz is offering similar settlements to Bavarian firms that face bankruptcy in the short term.

However, a member of the Federal Association of German Insurance Brokers estimates a 50/50 chance of success for many insurance contracts and discourages policyholders from settling too easily. One of the reasons why several German insurers want to be perceived as being "generous" and "doing the right thing" is that the claims they could have to pay out are significantly larger than 15% of insured businesses' operating losses.

Mannheim Regional Court Confirms BI Coverage

[6] https://www.vbw-bayern.de/vbw/Pressemitteilungen/Betriebsschlie%C3%9Fungsversicherungen-Bayerische-L%C3%B6sung-f%C3%BCr-Hotels-und-Gaststt%C3%A4tten.jsp

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In what appears to be the first German court order regarding BI coverage for COVID-19-related losses, the insurer's arguments were dismissed, and the policyholder—a hotel operator who also owns several restaurants—is entitled to BI coverage. On 29 April 2020, the 11th civil chamber of the Mannheim regional court (*Landesgerich Mannheim*) refused all defenses put forward by the insurer (who remains unnamed) and contradicts the statement of many insurers that losses as a result of COVID-19 are not insured per se.[7] Whereas the court clearly acknowledged that coverage should be provided by the insurer, it did not grant an injunction based on procedural reasons.

Similar to the Paris commercial court's ruling, the Mannheim court handed down an interim judgment concerning a preliminary legal protection proceeding. The most relevant clause in the insurance agreement reads as follows (Capstone translation):

> "1. The insurer provides compensation if, on the basis of the Infection Protection Act (Infektionsschutzgesetzes or IfSG), the competent authority…closes the insured company or insured permanent establishment to prevent the spread of notifiable diseases or pathogens in humans. Prohibition of any activity by employees of a company or a permanent establishment is equivalent to the closure of a company."
>
> "2. Notifiable diseases and pathogens within the meaning of the terms and conditions are those mentioned in §6 and 7 IfSG."

The Mannheim court ruled the following:

- **A general reference in the policy to sections 6 and 7 of the IfSG constitutes COVID-19 coverage.** The insurer argued that COVID-19 is not covered by the insurance policy, as it is a disease that is only temporarily notifiable and is not mentioned by name. The court noted that the insurer should have drafted a conclusive catalog of diseases if it wanted to limit coverage to certain diseases. However, a general reference to sections 6 and 7 of the IfSG, as was present in the case at hand, can be assumed to include COVID-19. The court stated that a policyholder can reasonably assume that all diseases mentioned in sections 6 and 7 of the IfSG trigger the insurance protection. Notably, the court considered how an average policyholder without any special knowledge of insurance law would interpret the policy. The court relied on article 305c (2) of the civil code (*Burgerliches Gesetzbuch* or BGB) concerning ambiguous clauses, which states that, "any doubts regarding the interpretation of general terms and conditions are at the expense of the user," which, in this case, is the insurer. A reasonable policyholder may assume that changes to the IfSG will apply to the insurance contract. This is also in the interest of the insurer, in the event certain illnesses are removed from the list in the future.

- **Coverage applies even if a closure order is not company-specific or the result of an individual administrative act.** The insurer argued that there is no closure due to a "company-specific administrative act." Rather, there is a general order seeking to limit physical contact, which would not trigger insurance coverage. The Mannheim court noted that an administrative order under the IfSG does not necessarily have to be a "company-specific or individual administrative act." The court appears to consider whether such orders force a business to close

[7] A copy of the judgment (in German) is available at: https://www.juris.de/jportal/prev/JURE200005793

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in practice. Moreover, the contract does not indicate that such a specific individual administrative act is required.

- **The restrictions, taken together, effectively caused a complete closure of the business.** The insurer argued that the relevant state orders do not force a business to close. Hence, the business' activities could have continued. Providing accommodation was only prohibited for tourists, but not overnight business stays. The insurer also claimed that the restaurants could offer takeaway service.[8] The judge ruled that a restriction that prevents tourists from staying overnight combined with other measures that encourage people to work from home and not travel has the effect, in practice, of complete closure, which is covered by the insurance policy.

- **Failing to anticipate COVID-19 or its risks is not a just reason for interpreting coverage to exclude it.** The court notes that the mere fact that none of the contracting parties anticipated an event such as COVID-19, or the insurer did not recognize this risk and did not take it into account when determining insurance premiums, is no reason to interpret the contract in such a way that the event is not covered.

- **Coverage requested by a business must accurately reflect operating profit.** The insurer argued that the level of damages cannot simply be compared to the same months of the previous year, adding that the spread of COVID-19 had significant effects in the first three months of 2020, which should be taken into account when calculating the operating profit. Here the court did note that the amount of the claim could not be adequately justified and because of this, an injunction (and ultimately protection under the insurance cover) was not granted. The court referred the applicant to the main proceedings to enforce the claims.

[8] The City of Hamburg, on 16 March 2020, issued a general decree stating "*Accommodation providers in the industry may not be provided to tourists. […]"* The Covid-19 containment measures regulation in Berlin, issued on 17 March 2020, state, among others, that *"Hotels and other accommodation establishments may not offer tourist accommodation"*

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