

## INSURANCE AND REINSURANCE

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### IN THIS ISSUE

*Emmanuèle Lutfalla and Simon Fitzpatrick discuss the lessons that can be learned from Covid-19 and the realities facing French insurers in its aftermath.*

## Covid-19 and Insurance: French Lessons for New Realities

### ABOUT THE AUTHORS



**Emmanuèle Lutfalla** is a founding partner of Signature Litigation's Paris office and heads the Insurance/Reinsurance practice. She is also the former International Vice President on the Board of Directors for IADC (2014-2017) and remains an active member of IADC. Emmanuèle has been recognized as a thought leader and a recommended attorney by renowned international legal publications. She can be reached at [Emmanuele.Lutfalla@signaturelitigation.com](mailto:Emmanuele.Lutfalla@signaturelitigation.com).



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### ABOUT THE COMMITTEE

The Insurance and Reinsurance Committee members, including U.S. and multinational attorneys, are lawyers who deal on a regular basis with issues of insurance availability, insurance coverage and related litigation at all levels of insurance above the primary level. The Committee offers presentations on these subjects at the Annual and Midyear Meetings. Learn more about the Committee at [www.iadclaw.org](http://www.iadclaw.org). To contribute a newsletter article, contact:



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To state the obvious, Covid-19 has completely changed the way our world operates and the effects may not fully be known until quite some time afterward. This statement could apply to many aspects of the public health crisis, but it is particularly poignant when it comes to insurance. France began to notice the effects of Covid-19 in late February to arrive at an almost complete lockdown by March 17, 2020. Unlike the United States, France's lockdown was nation-wide and enforced by fines for breaking the lockdown restrictions. But, like what we have seen in the United States, transport operators, events and other mass gatherings, and businesses were severely disrupted by the lockdown measures. As Covid-19 continues to ravage the United States and France is anticipating the second wave, now seems to be an appropriate time to take stock and see what lessons we can learn from the challenges created by the Covid-19 crisis.

**France's Approach to Business Interruption Insurance: A Lifeline under the Right Circumstances**

For many French businesses, turning towards their business interruption insurance was the next logical step, as the insurance is often sold as a lifeline to help businesses continue to operate while they reestablish themselves after a crisis. But, the vast majority of France's business interruption insurance policies only cover damage which is consecutive to a material loss. In practice, most of the time this will occur after a fire or if a machine breaks down

that causes a factory to be idled. However, French business interruption insurance policies also cover business interruptions related to natural disasters under France's natural disasters insurance scheme. Insurers pay a portion of the premiums they receive from mandatory insurance covers into a dedicated fund. In order for the insured to make a claim on this particular cover, the government must make a formal declaration declaring a natural disaster. If the payments due under the cover obtain a certain amount, the government will then step in and replenish the fund. At the beginning of the Covid-19 crisis, many businesses and entrepreneurs demanded that the government issue some sort of declaration declaring the crisis a natural disaster. The government has rebuffed these demands.

It is possible for French insurers to extend their covers to cover business interruption without material damages through coverage extensions. Very few businesses have done so in France. These particular extensions tend to revolve around outside events, such as if a specific person is unable to fulfill their duties. But subscribing to this type of cover is not a common practice for most businesses. For business that have not subscribed to a coverage extension, their Covid-19 claims will not be covered under their existing policies. For those businesses that have a coverage extension, their policies and coverage extensions were written at a time where a global pandemic of this scale was barely considered. For example, due to the imposed travel restrictions, a company is unable to obtain

the essential supplies in order to continue its operations, would this be covered under a coverage extension? What about tour operators who may suffer financial losses due to mandatory quarantine restrictions in their location or a lost season due to fears of infection? When it comes to coverage exclusions, if an epidemic is excluded, does that include a pandemic? Insurers and the insured will have to face some hard truths that will more than likely come from case-law and legislative intervention.

While not directly envisaged to include the Covid-19 crisis, the French government, in partnership with various stakeholders, has convened a working group to propose future insurance solutions in order to avoid the difficulties we have seen in regards to the current crisis. At the time of writing, the government working group has yet to make any formal announcements, but the *Fédération Française de l'Assurance*, the French insurers representative body, has made their proposals known.<sup>1</sup> French insurers are pushing for the creation of a new government backed fund that would be partially financed by an insurance premium surcharge on insurance contracts. The French government would then guarantee financing above a certain amount. The primary beneficiaries of the new scheme would be SMEs and very small businesses who would benefit from a predetermined

fixed-rate cover without the requirement of expert valuation. These new ideas are progressive from the standpoint that they are taking a proactive approach to respond for the future based upon the lessons of the past. However, some of these proposals have revealed some approximations regarding insurance coverage.

### **Calling into Question the Fundamentals of Insurance?**

The foundation of insurance is the mutualization of risk. In its purest form, insurance only works if the pool is sufficiently large in order to cover the subscribed risks. When considering a global pandemic with mass claims and potential payouts, insurers are right to debate whether or not a pandemic is an insurable event. From a purely economic perspective, a pandemic would not be an insurable event. As we have seen, everyone is affected by the Covid-19 crisis and there cannot be an effective mutualization of risk if the entire pool files claims. There are ways to counter a loss of mutualization through investments and using the financial markets, such as the reinsurance market. However, an important distinction must be made: economic impossibility to insure does not equate to legal impossibility to insure.

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<sup>1</sup> Press Release, *Fédération Française de l'Assurance* [French Insurance Federation], *La Fédération Française de l'Assurance présente sa contribution au débat sur la création d'un régime de catastrophes exceptionnelles : le dispositif CATEX* [The French Insurance Federation Presents its Contribution to the

*Debate on the Creation of an Exceptional Catastrophes Scheme: The CATEX Mechanism*] (Jun. 12, 2020), <https://www.ffa-assurance.fr/actualites/la-federation-francaise-de-assurance-presente-sa-contribution-au-debat-sur-la-creation-un>.

As a matter of French law, insurance is manifested through contract and as such we may draw two conclusions regarding insurability. First, mutualization of risk is not a contractual mechanism in individual insurance contracts. Second, a risk may be insured so long as it is not excluded by mandatory provisions or contract. The exclusions, or inclusions as the case may be, of risks inherently resistant to mutualization could be imposed through legislation or administrative regulations. In the absence of such requirements, it falls upon insurers to exclude these risks through the insurance contracts. In France, some of the first decisions on Covid-19 insurance issues are coming down and, while still subject to appeal and decisions on the merits, the French courts have ruled that pandemics are insurable events.<sup>2</sup> As a result, some insurers are now discovering that they may have inadvertently covered pandemics due to a poorly drafted exclusion or other technical hurdles. These insurers are undoubtedly (re)discovering the fundamentals of contract law.

Another difficulty that highlights the tension between insurance and contract law is the definition of terms in insurance contracts. Most French insurance contracts cover "damages and losses" without a distinction between the two. The French Insurance Code does provide some context, but does not have a clear legislative definition:

Losses and damages created by accidents or caused by the fault of the insured are the responsibility of the insurer, except for formal and limited exclusions contained in the policy.

However, the insurer does not cover losses and damages resulting from an insured's intentional misconduct or fault.<sup>3</sup>

The insurer is the guarantor of losses and damages caused by persons of which the insured is civilly responsible for [parent/child, employer/employee, and master/apprentice], no matter that person's faults' nature or importance.<sup>4</sup>

If one were to read the terms and conditions of insurance policies, the reader would more than likely find terms such as "material damage," "immaterial damage," "direct loss," and "indirect loss." How do these terms effectively apply in the context of Covid-19 and business interruption insurance? If a business interruption insurance policy only covers material damage, French insurers have taken the position that material damage constitutes the loss of a thing or damage to the thing's structure or substance. In keeping with this definition, if a factory were to lose revenue due to physical distancing requirements and the inability to operate the machines as required, since the machines are still working properly, but they cannot be used as effectively as they once were, this would

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<sup>2</sup> Tribunal de Commerce [T. com.] [commercial court of original jurisdiction] Paris, référé, May 22, 2020, 2020017022.

<sup>3</sup> CODE DES ASSURANCES [C. ASS.] [INSURANCE CODE] art. L. 113-1.

<sup>4</sup> *Id.* at art. L. 121-2.

not be considered as material damage. While the loss of revenue certainly qualifies as a loss in layman's terms, it may not effectively fall under an insurable loss under the majority of business interruption insurance policies. Indeed, the losses would be covered if they result, directly or indirectly, from the material damages covered under the policy.

We feel that the best course of action for insurers, be they French or foreign, is to better define losses and damages in their insurance policies. Fundamentally, insurance is a contract and insurers are in the business of contracting. The Covid-19 crisis has shown the flaws in being complacent about general exclusions relating to public health crises. On June 23, 2020, France's Prudential and Resolution Control Authority released its study of business interruption insurance contracts in the French market and found that 4.1% of French business interruption insurance contracts are not sufficiently clear to determine whether or not Covid-19 is an insurable event.<sup>5</sup> We hope that one of the main lessons-learned from the Covid-19 crisis is that insurance policies will be better drafted and that there is more articulation between the clauses.

### **Better Drafting, Improved Clarity, and Peace of Mind for All**

Naturally, drafting insurance policy exclusions is a delicate task that will have real consequences once the event occurs. Sadly, the Covid-19 crisis has shown us the importance of taking care in drafting exclusion clauses. The French Insurance Code imposes two conditions for exclusions to be valid: that the exclusion clauses be formal and limited, and be written in "apparent" characters.<sup>6</sup> French case-law has determined that for exclusions to be formal and limited, there should be no need to interpret the exclusion clauses.<sup>7</sup> Bearing in mind this high standard, some policy exclusions do not seem to pass muster. For example, after the SARS and H1N1 epidemics, many insurers began to insert exclusions specifically excluding these illnesses and other "atypical respiratory inflammation." For France, insurance case-law regarding illness and other medical ailments is not fully developed, but French courts are reluctant to allow exclusions that rely on symptoms rather than medical definitions. For the rare policies that cover business interruptions without material damage, difficulties have arisen under the meaning of "closure ordered by an

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<sup>5</sup> Press Release, Autorité de contrôle prudentiel et de résolution [ACPR] [Prudential and Resolution Control Authority], *Garantie « pertes d'exploitation » : l'état des lieux de l'ACPR ["Business Interruption" Covers: the ACPR's Situational Analysis]* (Jun. 23, 2020) [https://acpr.banque-france.fr/sites/default/files/medias/documents/2020](https://acpr.banque-france.fr/sites/default/files/medias/documents/20200623_communique_presse_pertes_exploitation.pdf)

[00623\\_communique\\_presse\\_pertes\\_exploitation.pdf](https://acpr.banque-france.fr/sites/default/files/medias/documents/20200623_communique_presse_pertes_exploitation.pdf).

<sup>6</sup> CODE DES ASSURANCES [C. ASS.] [INSURANCE CODE] arts L. 113-1 and L. 112-3.

<sup>7</sup> Cour de cassation [Cass.] [supreme court for judicial matters] 3e civ., Oct. 27, 2016, Bull. civ. III, No. 140.

administrative authority,"<sup>8</sup> "loss of clientele," etc. Despite the forthcoming amount of litigation on these issues, we feel that it is imperative to provide clearer and more comprehensible definitions for future insurance policies.

Clarity should also extend not only to the individual clauses within the policy, but between the policy terms and the insurer's general terms and conditions. In some policies, the lack of clarity and organization can lead to confusion and serious consequences. This development is of a particular concern regarding coverage extensions where the underlying cover is not easily identifiable. The French conception of a coverage extension is a contractual mechanism where in consideration of a supplemental premium, the insurer will agree to cover specific events that are not covered under their standard insurance policies. In practice, a coverage extension often equates to a separate cover. For example, a business interruption insurance policy that covers consecutive losses resulting from the material damage has an coverage extension to include non-consecutive losses. In these circumstances, subjugating the non-consecutive losses to a material damage effectively vitiates the coverage extension. The true difficulty arises when the coverage extension refers only to the policy's purpose or conflicts with an exclusion clause. While it is clear that a specific policy's special terms and conditions

override the insurer's general terms and conditions, when an extension and an exclusion are in the special terms and conditions, making a distinction becomes much more difficult. One could argue that a special coverage extension should be superior to a standard exclusion clause so that the extension is not vitiated. However, the best practice for the future could be to simply insert a clause that provides a hierarchy taking into account the order of interpretation and application.

#### **Insuring and Ensuring Employee Safety: France and the U.S. on Different Paths?**

At the time of writing, France has lifted most of the restrictive lockdown measures and some signs of daily life have returned. However, Covid-19 is still actively circulating, albeit to a lower degree than what we see in the United States. One of the challenges of keeping a business operating during the lockdown and the reopening period is assuring the safety of the business's employees and evaluating the potential implications of a business's civil liability policy. Under French law, employers owe a duty of result in regards to employee and workplace safety. This particular duty extends to employees' commutes, so that employees may feel safe coming in or leaving the workplace. During the lockdown period, most businesses that could switch to working from home arrangements probably did so, but those who were deemed

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<sup>8</sup> Tribunal de Commerce [T. com.] [commercial court of original jurisdiction] Paris, référé, May 22, 2020, 2020017022.

essential workers were asked to continue to come into work. Specifically regarding workplace safety requirements in the Covid-19 context, employers would have to ensure physical distancing requirements and provide their employees with masks, hand sanitizer, and gloves.

For an employee to claim damages under civil liability for alleged failings, the employee would have to prove that they effectively became ill with Covid-19 at the workplace or on their way to and from work. The courts would more than likely take a practical approach, taking into consideration that it is difficult to pinpoint the exact time of infection and its location. Moreover, if an employer can demonstrate that it has followed the relevant health guidelines and recommendations, an employer should have a reasonably sound defense. Two cases were brought against Amazon<sup>9</sup> and Renault,<sup>10</sup> a French car manufacturer, for allegedly failing to meet workplace safety standards. In both cases, the courts ruled against the employers and ordered them to undertake specific measures. For Amazon, it was required to deliver only essential goods, such as food products and housekeeping items. In response, Amazon decided to close all of its French distribution centers. Insurers were not involved in these cases and no damages were awarded, however these

cases demonstrate that workplace safety issues are a concern for employers and their insurers. Whether or not the U.S. Senate Republican's liability shield is adopted or rejected,<sup>11</sup> both employers and insurers should read their policies carefully to determine their rights and responsibilities, especially when facing litigation. At present, France is not currently contemplating a liability shield like the American proposal.

### **Is My Tangible Good a Vector for Transmission?**

Considering insurance policies that are designed to cover property damage, there could be an interesting debate regarding if a good that has been exposed to Covid-19, leaving traces of the virus on the object, and if that could constitute damage. Another example could be to consider if the good could be damaged by taking measures to prevent the spread of Covid-19, such as being required to leave a good unattended for a certain time to kill the virus. For French insurance policies, epidemics are more than likely excluded, but if the policy is silent about a pandemic, is a pandemic included? Moreover, what does it exactly mean for a good to be damaged or contaminated? If the good is perfectly fine and could be sufficiently treated to kill the virus is it permanently contaminated? There are still

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<sup>9</sup> Cour d'appel [CA] [regional court of appeal] Versailles, 14th chamber, Apr. 24, 2020, 20/01993.

<sup>10</sup> Tribunal judiciaire [TJ] [ordinary court of original jurisdiction] Le Havre, référé, May 7, 2020, 20/00143.

<sup>11</sup> Richard Cowan & David Morgan, *U.S. Republicans seek liability protections as coronavirus aid battle*

*looms*, Reuters (Jul. 17, 2020), <https://www.reuters.com/article/us-health-coronavirus-usa-congress/u-s-republicans-see-liability-protections-as-coronavirus-aid-battle-looms-idUSKCN24I18H>.

many unknowns about Covid-19, but it does seem that most virus transmission occurs through aerosols rather than surfaces. This issue could be open to debate and, therefore, it is imperative to verify the individual policy's definitions and exclusions.

### **French Lessons for the World**

So much has happened in 2020 that at times it seems like we are spinning out of control. Our economies, health systems, and our daily lives have been pushed to the limit. Insurance is marketed as a safety net in uncertain times and in many ways it is. But, like most things these days, the insurance system may soon be pushed to the limit. Many insurers are facing massive amounts of claims and their refusals may lead to litigation. Clarity of what was agreed to will be key. Almost no one has a recollection of the last pandemic and those who ignore history are doomed to repeat it. Now seems like an appropriate time to remember going forward, and to improve the terms and conditions of insurance policies and provide clarity to insurance subscribers. This may also include creating dedicated funding sources in order to keep the foundations of insurance intact. If insurance is to remain the important safety net it is designed to be, it seems we collectively need to repair the net to be ready for the next tumble.



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