

Business

Courtroom wrangling leaves insurance industry in crisis

A new wave of lawsuits triggered by the pandemic has damaged insurers' standing, says *Simon Foy*

In the early hours of April 18 1906, an earthquake decimated San Francisco, killing thousands and triggering fires that raged for days.

At the time, governments tended not to provide relief funds to regions affected by natural disasters as they do today, meaning much of the responsibility for recovery fell on insurers.

Despite the huge costs associated with paying out claims, Cuthbert Heath, an underwriter at Lloyd's of London, demanded that his San Francisco agent "pay all of our policyholders in full, irrespective of

the terms of their policies". The decision cost Lloyd's \$50m (£44.6m) – more than \$1bn in today's money – but this show of goodwill resulted in it dominating the US insurance market for nearly half a century.

The 1906 earthquake is now known in the industry as the "San Francisco moment", but observers fear insurers today have forgotten the lessons learnt. A recent report from insurance adviser Mactavish reveals that British companies are now three times more likely to sue their insurers to get their claims paid than they were in 2017.

The research, which looks at every legal insurance claim filed at the High Court over the past decade, shows that legal cases against the top 20 in the UK have increased from an average of 19 from 2012 to 2017 to 69 in 2020, and 71 last year. Mactavish says this is just the

tip of the iceberg as an unknown number of cases will have been settled privately without going to court.

While legal claims were already rising steadily before 2020, the pandemic acted as a trigger for a new wave of litigation. Business interruption insurance became a huge source of controversy after Covid lockdowns began in March 2020, with many companies accusing providers of unfairly refusing to pay out claims.

The list of companies denied a payout was vast and ranged from restaurants to nurseries.

"The market missed its 'San Francisco moment' with business interruption claims," says David Hertzell, chairman of Mactavish.

"Many insurers looked to challenge all Covid claims arguing that in effect, they never intended to insure such a loss. The decision generated terrible publicity and near-unanimous unfavourable decisions in the High Court and the Supreme Court yet, even then, despite some large total payout sums, a relatively small proportion of all affected policyholders got paid."



Lloyd's of London's top reputation was built on its 'San Francisco moment', paying out over the 1906 earthquake

LEON NEAL/AFP VIA GETTY

Earlier this month, the Financial Conduct Authority, which had launched and won a legal test case against insurers over pandemic claims, warned that insurers face a crackdown after it found "significant issues" in their handling of Covid-era claims and said it would use "all regulatory tools" to address the problems uncovered.

Yet the Mactavish report shows legal battles are not restricted to Covid claims and stem from all parts of the

market, including marine, technology, property, finance, manufacturing, as well as claims related to road traffic accidents and asbestos.

The report says the rise in legal cases has occurred because of a prolonged "hard market" for the industry – a sustained period of rising insurance prices. Bruce Hepburn, chief executive of Mactavish, says:

"Insurers don't care about market share, they care about protecting their

balance sheets. This is why premiums go up and insurers start to look for ways to reject claims."

Mactavish cites a breach of policy conditions, lack of coverage, misrepresentation, non-disclosure of facts and claims alleged to be outside the scope of cover as the main reasons why insurers are rejecting claims.

It adds that companies are giving multiple reasons for rejecting claims, or drastically cutting the payout level. However, Mactavish also found that it was not uncommon for many of those reasons to "fade away as the case approached judicial scrutiny, perhaps indicating they were not reasonable objections in the first place".

Mactavish warns that not only is the industry further damaging its reputation and eroding its relationship with customers, but the jump in legal battles could harm the wider economy.

"If businesses do not have confidence in the insurance market, they are less likely to take the kind of business risks that are required to maintain economic growth," the report says.