

Coronavirus - impact on insurers

February 2020

The current coronavirus outbreak (recently named COVID-19 by the World Health Organisation (WHO)) is dominating global headlines. Since it was first reported from Wuhan, China on 31 December 2019 it has spread to 25 countries, infected over 70,000 people and claimed over 2,000 lives.

While priority measures are understandably focussed on the threat to life and health, with governments around the world implementing quarantine procedures and increased health checks, global trade and business has been and will continue to be affected. We offer some initial thoughts about the wider, global impacts for insurers, areas of potential exposure and what steps firms should be taking.

Aviation

The emergence of a COVID-19 at the busiest period in the Chinese travel calendar could not have happened at a worse time. The consequential travel restrictions and flight suspensions have caused significant disruption to the travelling public and considerable financial strain to airlines and air operators which have had to adapt at very short notice to changes mandated by governments and health authorities.

Some airlines will have activated their emergency response plans to deal with a public health emergency of this nature. Those who have not done so will be consulting their advisers on the measures they need to take. Such measures call for heightened coordination between a wide-range of departments including flight operations, in-flight services, security and facilitation.



Insofar as an airline's liability for international carriage of passengers is concerned, this will likely be regulated by the Montreal Convention 1999. Under that Convention, an airline would only be liable to its passenger if it can be established that sickness resulting from COVID-19 was caused by an "accident" (defined by case law to mean an unusual or unexpected event external to the passenger) which happened on board the aircraft or in the course of embarking or disembarking. While the sickness may be unexpected, that in itself cannot be considered the accident. There has to be an external event which causes the passenger to contract the sickness.

Although airline check-in/gate agents are not medically trained to identify COVID-19 symptoms, airline companies should be exercising vigilance by keeping an eye out for passengers who may appear unwell. Most airlines' conditions of carriage would allow them to refuse carriage to passengers whose medical condition poses a danger to the health and safety of any person on the flight.

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Construction

China has been significantly involved in overseas construction projects, especially in Africa and the Gulf Cooperation Council (GCC) countries, in furtherance of its Belt and Road Initiative. The UK is forecast to be the largest European beneficiary of the Belt and Road Initiative, and any impact from COVID-19 will slow down the projected benefits on a global and European basis.

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Travel bans in affected locations could significantly hinder progress of construction projects and the introduction of additional layers of compliance with HSE policies may create a daily challenge in performing the works.

These measures may cause delay or even bring a project to a complete halt, even for a brief period of time, causing significant losses.

Whilst any delay at this stage and liability thereof can be addressed with updated schedules and re-allocation of work and resources, contractors' compliance with the policies and the implementation of any new measures put in place in response to the virus requires vigilance and caution by all concerned.

On a micro level, COVID-19 may impact the UK construction supply chain, which is reliant on a global supply chain, with many materials being imported from China. In particular, any impact that the virus may have on the supply of steel into the UK could cause delay to construction projects on a national scale.

In Thailand (one of the worst affected countries outside of China), the supply chain is already causing some concern and creating an air of pessimism. Currently, there is no great day to day effect, however we have advised client contractors about concerns relating to potential delays in the future and how these will be treated under the contracts. The concern is borne of a worry that while COVID-19 may trigger force majeure clauses, employers or project managers will argue that certain materials should have been sourced earlier, which is indicative of the ever present disputes between contractors and project managers in Thailand.

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Employment

The outbreak has already been severely disruptive for employers in affected areas, and has caused significant business interruption, in particular in the travel, hotel, hospitality, entertainment and retail sectors. This looks likely to continue for some time. Employers should adopt a common-sense approach according to the particular geographical and operational circumstances of their business.

In Hong Kong, if an employee becomes infected with COVID-19 as a result of an accident arising out of and in the course of their employment they will be able to make a claim for loss under the Employees' Compensation Ordinance. More claims against employers are likely arising out of work arrangements during the outbreak including failure to provide protective equipment.

In response, the Hong Kong Government has directed all of its civil servants to work from home until 23 February 2020, likely to be extended, and is encouraging all private sector employees to work from home “if practicable”.

In the UK, the Department of Health & Social Care and Public Health England are providing a co-ordinated response to the outbreak and a link to their advice is available via the HSE website.

During these challenging times, employers need to bear in mind their obligations to their employees under health and safety legislation and employment laws and the potentially more serious business interruption issues which may arise if they do not take immediate steps to minimise risk. Employers would be wise to draw up a specific business continuity impact analysis and consider more long-term solutions to protect their personnel.

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Financial lines

The impact of COVID-19 on the global economy is growing. Government officials have stated that China’s economy is highly resilient and have downplayed the impact of the outbreak, but it seems inevitable that both the Chinese and the wider global economy will suffer.

In Hong Kong, the impact will be exacerbated by the economic downturn caused by the recent anti-government protests. Shops and other retail businesses, airlines, travel operators and hotels are already suffering a significant drop in business.

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At a global level, the repercussions of a further downturn in China as the world’s second biggest economy should not be underplayed. China is a significant player in the global market and as economies are increasingly interconnected, many other countries are also at risk of an economic slowdown.

After heavy selling at the end of January, share prices have been rebounding because investors appear to have confidence that COVID-19 can be contained. However, countries in the south-east Asia region are already enacting fiscal measures in response to the outbreak. The Philippines and Thailand announced central interest rate cuts in early February and Singapore is expected to depreciate its currency. In line with the “phase one” trade deal signed with the US last month, China has announced that they will halve tariffs on some US imports on 14 February. The expectation is that this will cushion some of the economic fallout from the outbreak. However a number of businesses have already announced that their 2020 results are likely to be materially affected.

In terms of impact on insureds and their insurers in the financial lines sector, steps which are being taken by boards of companies to address COVID-19 related risk by way of contingency planning will likely be scrutinised and second-guessed in the event of loss of company value. Financial institutions and financial services firms which are regulated will be asked to explain what precautionary measures they are taking to ensure business can function as usual and to ensure regulatory compliance. The Securities and Futures Commission and Hong Kong Stock Exchange have already issued a joint announcement in relation to Results Announcements; if a listed issuer believes there is a real possibility that, as a result of COVID-19 it will be unable to publish results as required by the applicable rules, it should contact the Exchange as early as possible to discuss. The Commission is also encouraging listed issuers to consider whether they need to disclose any inside information relating to the impact of COVID-19 on their business. Regulators will be monitoring companies’ disclosures in relation to the potential impact of COVID-19 and in the event of adverse outcomes, regulatory actions or claims might be inevitable. Other regulators will be looking closely at how firms prepare for potential liquidity shortfalls and payment defaults.

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Healthcare in Hong Kong

The outbreak is of extreme concern to health professionals in Hong Kong given the land border Hong Kong shares with Mainland China and the numerous other access points with the Mainland. These links mean increased risk of transmission from people returning/visitors from affected areas.

This has led to calls from some health workers to close all land borders with Mainland China and to some taking strike action leaving public hospitals only able to maintain basic emergency services.

Many health insurers in Hong Kong have announced new measures in response to the new virus and a number of PRC insurers are providing free insurance cover to frontline medical staff, civil servants and officers and soldiers in Wuhan and, in some cases, across all China.

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Marine

The shipping industry's movement of goods and people around the world, coupled with China's position as the second biggest economy in the world, has left it more susceptible than most to the impact of the new strain of coronavirus from Wuhan.

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China's reduced demand for resources has resulted in drop in demand for oil. Sinopec, Asia's largest refiner, has reduced its operations, VLCC (very large crude carriers) rates have fallen to their lowest since mid-September and there has been a 90% drop in rates for iron ore carrying Capesize vessels.

A number of charterparty issues are also expected with delays occurring in and out of Chinese ports, at non-Chinese ports in the event of a previous call at a Chinese port and/or any suspicion that the crew may have been exposed to COVID-19. Vessels may find themselves quarantined or required to deviate. There may be delays in obtaining free pratique (clearance given to the vessel by authorities confirming that the vessel is free from contagious disease).

Issues may also arise regarding whether orders to particular ports may be orders to an unsafe port and therefore not legal under the terms of the charter. Vessel delays will inevitably lead to potential cargo losses, especially to perishable cargo, leading to bill of lading claims and insurance disputes, depending on the level of cover. Moreover, should the COVID-19 outbreak become a pandemic, it may trigger force majeure clauses commonly found in contracts.

Another side effect has been the delays in the fitting of scrubbers required for many vessels to comply with the IMO's Sulphur Regulations 2020. With many of the scrubber upgrades having been planned to take place in China, workers may not be available to return to the shipyards to complete the works commenced prior to the Lunar New Year.

In the cruise liner space, more than 5,300 people are currently quarantined on two cruise ships off Hong Kong and Japan amid concerns passengers and crew have been inadvertently exposed to the virus by infected passengers.

These incidents have raised concerns about potential spread of infectious diseases among thousands of passengers at sea and exposes the vulnerability of cruise liners to risk of outbreaks due to the close living quarters of passengers and crew.

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Product liability and life sciences

With more than 70,000 confirmed cases of COVID-19 worldwide, scientists and pharmaceutical companies are racing to develop a vaccine. Many in the life sciences industry are hopeful that a vaccine may be ready for Phase I clinical trials within months, a timescale which is unprecedented in the history of vaccines which can often take years to develop. If this can be achieved, such developments will herald a new era in vaccine development where the public will stand to benefit from solutions to worldwide health threats in much shorter timescales.

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If a potential vaccine does successfully reach an early stage clinical trial within the next few months, it will still need to undergo extensive testing to ensure its efficacy and safety and then obtain regulatory approval - a sentiment aligned with recent reports from the WHO. Even in the best case scenario, a vaccine could still take at least one year to be brought to market.

Whilst it is possible in some countries to fast track a vaccine through regulatory channels, this would only occur in exceptional circumstances. For example, in the US, the declaration of a public health emergency could allow for emergency use authorisation of medical products from the Food and Drug Administration. In the EU and UK, the urgent release of a vaccine would likely require a special resolution to be passed.

Caution should however be exercised in ‘fast-tracking’ any vaccine (or indeed any other medicinal products) to market as the medium-to-long term effects of such vaccines will not have been extensively studied, even if limited clinical trials have taken place. As such there is a potential for future liabilities to occur if, for example, vaccine recipients suffer known or potential side effects which are inadequately warned about by manufacturers. The challenge for manufacturers (and regulators) will therefore be to balance such risks against the benefits that the rapid release of vaccines convey where the circumstances urgently warrant it.

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Supply chain/business interruption

Based on our experience advising insurers on SARS, it is anticipated that some of the risk and losses will be transferred to insurers; the COVID-19 outbreak is expected to give rise to policy coverage, exclusion and aggregation issues.

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Many carriers (Cathay Pacific, UPS) have reduced or cancelled their flights to China. This relates not just to the movement of people, and the corresponding impact on tourism, but also to cargo. The electronics, technology and pharmaceutical industries rely heavily on Chinese suppliers.

They can therefore anticipate significant disruption to their supply chains and if the inventory pipeline is held up, this may prevent completion of finished goods.

It will therefore be important for businesses, as part of their risk assessment approach, to ensure that they have alternative suppliers available. It may not be as simple as cancelling the order with the original supplier as much will depend on the contractual terms agreed.

Will the supply chain disruption prevent the business from honouring its own contracts? If so, what can be done? Contracts should be checked to see if they contain a ‘force majeure’ clause and if so, what protections the clause provides. It will then be a case of assessing each case on whether or not the outbreak of the virus falls within the contract terms.

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Travel

The WHO has issued (and updated) advice for international travel and trade in relation to the outbreak of pneumonia caused by COVID-19 and has advised countries to follow the International Health Regulations.

The Hong Kong Government has implemented a number of travel restrictions: it has shut down two railways, suspended the issue of new visas to tourists from the Mainland, cut flight and cross-border bus services, suspended through-train services and ferry services between Hong Kong and the Mainland, and closed all but three border checkpoints.

In the UK, we have advised our tour operator clients to follow the advice published by the Foreign & Commonwealth Office (FCO), namely not to travel to China altogether or to transit through China.

For those operators selling packages as defined by the new European Package Travel Directive of 2018, there are obligations on operators to offer cancellations or alternative trips for passengers affected.

Travel insurance products vary greatly so the policyholder will need to check their policy/with their broker if they wish to make a claim as a result of having to cancel their travel plans due to travel restrictions imposed to combat the spread of the virus. They may also be eligible for a refund from the travel operator.

If an insured contracts COVID-19 whilst travelling they may, depending on the terms of their travel insurance, be able to claim for their medical/hospitalisation bills. They may also be able to claim for other costs such as additional accommodation and travel costs incurred as a result of their condition/medical treatment.

It is possible those travelling against advice may not be covered by their travel insurers if anything untoward happens.

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View from the US

The US has declared the outbreak a public health emergency, put travel restrictions in place, and has denied entry to foreign nationals who visited China within 14 days of arrival to the US. Citizens are also subject to a mandatory quarantine when traveling to the US from China's Hubei province. Multiple airlines temporarily suspended all flights to China.

US companies that employ Chinese nationals on H1-B visas face special challenges as employees return to the US after visiting family over the Lunar New Year holiday and it is anticipated that insurance carriers

in the US will see a broad range of claims including under business interruption (CBI) and supply-chain policies.

The outbreak of a contagious disease may also expose policyholders to liability claims for failing to protect others from exposure to infection on their premises. The policyholders, in turn, may make claims under their general liability policies, which provide broad coverage for bodily injury and property damages.

Moreover, with increasing travel bans and restrictions, travel insurance is another type of insurance that will undoubtedly be affected.

With at least 13 confirmed COVID-19 cases in the US and no specific treatment or preventative vaccine identified, it is important to recognize these risks and stay abreast of the developments and the impacts.

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To find out more about our services and expertise, and key contacts, go to: kennedyslaw.com

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