

INSIGHT



ISSUE 018: May 2011 **Craig Langstone, Partner**

Calculating a business interruption claim—*Synergy Health*

A recent English Commercial Court decision, *Synergy Health (UK) Ltd v. CGU Insurance plc* [2010] EWHC 2583 (Comm), sheds some light on two particular BI loss calculation issues. The lengthy judgment is largely concerned with defences raised unsuccessfully by CGU but is worth noting for its comments on BI; particularly given the lack of judgments in the area and the topical nature of BI claims following the recent earthquakes.

Synergy provided laundry and related services to the NHS. Synergy's premises, plant and equipment were insured under a Combined Commercial Policy against material damage and business interruption losses.

On 3 February 2007, during the currency of the policy, there was a fire at a laundry owned and operated by Synergy in Dunstable. This was just one of a number of sites.

The material damage losses were agreed at £4M and the business interruption losses exceeded £2M. The insurers purported to avoid the policy for non-disclosure and misrepresentation. Those defences ultimately failed.

Issues arose as to the amount of the business interruption claim. The policy was in more or less standard form, providing cover for loss of gross profit for an 18 month indemnity period; the loss being defined as reduction in turnover and increased costs of working. The case raised two important issues.

The first related to increased costs of working. Following the fire, the work of the Dunstable laundry was transferred to Derby, leading to an additional working shift at Derby which resulted in the premises operating for 24 hours a day, five days a week. Synergy claimed that this led to increased maintenance costs and the cost of additional spare parts at Derby, and that those costs continued after the work had been transferred back to Dunstable.

Perhaps surprisingly, the Judge thought that the correct construction of the policy was that it was possible to recover increased costs of working incurred after the indemnity period had come to an end, and that the indemnity period itself was relevant only to loss of turnover and not to increased costs. The Judge gave the example of an 18-month indemnity period, but the insured only being able to obtain a two-year lease for a replacement building pending repairs: the costs of the lease would be fully recoverable even though they went beyond the indemnity period (according to the Judge).

Of course any such increased costs would have to reduce the BI claim (within the indemnity period) by an amount greater than the amount of the increased costs. Ordinarily this would not happen—the increased costs past the indemnity period would exceed any BI saving. So both from a legal perspective and a practical one, it is unlikely increased costs of working would have to be paid by an insurer beyond the relevant BI indemnity period.

In any event, the facts of the Synergy case did not support a claim for additional working costs beyond the indemnity period; as the evidence showed that the machines would have incurred those costs anyway.

The second issue concerned depreciation of the machinery damaged in the fire. Ordinarily Synergy adopted the usual accounting practice of allocating depreciation of machinery across the years of its likely life, so that the value of the assets — and thus Synergy's profits — was reduced every year by an element of depreciation. Following the fire, Synergy's post-fire losses of revenue were calculated without taking into account any element of depreciation. The insurers argued that this inflated Synergy's post-fire revenue. The Judge agreed and held that Synergy had to give credit for such depreciation. This reduced the amount the insurers had to pay in respect of the BI claim.

Whilst insurers may be a little concerned about a suggestion that increased costs of working



 **JONESFEE**

INSIGHT



could be claimed for a period of time longer than the relevant indemnity period in a particular policy, in reality this is unlikely to happen. However the Judge's comments about depreciation needing to be deducted when a BI claim is calculated are of importance. So the good news for insurers is that depreciation can, and ought to be, deducted from all BI claims submitted (subject of course to what each individual policy working says).

For further information about the *Synergy Health* case or a full copy of the judgment, please contact:

Craig Langstone

Email: craig.langstone@jonesfee.com

DDI: (09) 373 0053

