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RISKS WITH YOUR RECEIVABLES: TRADE CREDIT INSURANCE COVERAGE AND EXCLUSIONS DURING COVID-19

02 April 2020

As COVID-19 continues to impact the global economy, risk increases that customers will be unable to pay their outstanding receivables. These risks are compounded by a number of restrictive emergency orders, regulations, and amendments that governments across the globe have recently enacted in an effort to curb the spread of COVID-19.

In Ontario, for example, the Provincial government has ordered the closure of public places and establishments, the prohibition of events and gatherings of more than five people, and the closure of all non-essential businesses. These types of emergency orders are not unique to Canada, and have been enacted in a number of countries with economic ties to Canadian businesses.

The economic uncertainty sparked by COVID-19 has raised a number of questions in the insurance realm. In the context of unpaid receivables, one important consideration for companies is whether trade credit insurance policies will provide coverage for losses arising out of the COVID-19 pandemic.

What is Trade Credit Insurance?

Trade credit insurance is a policy that protects an insured from non-payment of commercial debt. In a world where most companies' accounts receivable make up a significant percentage of their assets, trade credit insurance provides protection against the risk that a customer may default on a debt.

Aside from offering protection to businesses, trade credit insurance can also help a business to grow. With a trade credit insurance policy, a business can feel more comfortable to pursue new, larger customers that would have otherwise seemed too risky. Trade credit insurance can also enable a business to sell on an open account, rather than on a secured basis, which can offer it a competitive advantage in the marketplace.

What does trade credit insurance cover?

Trade credit insurance policies are bespoke, often being tailored to the specific needs of a particular insured. That being said, most trade credit insurance policies include coverage for similar types of losses. Typically speaking, trade credit insurance policies will cover, among other things, losses in the event that:

- Circumstances arise which could, in the reasonable opinion of a prudent insured, give grounds for the belief that a debtor may not be able to perform or comply with its obligations under a contract of sale with an insured;
- Any part of an insured debt is not paid in cash or by cheque or bill of exchange within the time period set out in the policy; and
- An event of insolvency occurs in respect of a debtor or an insolvency administrator or practitioner is appointed to the debtor.

In short, a trade credit insurance policy will typically provide coverage to an insured if a debtor cannot pay a debt, does not pay a debt, or becomes insolvent. In those circumstances, the insurer will typically cover the account receivable up to an amount as set out in the policy.

Exclusions from coverage

More important for present purposes are the types of losses that are typically excluded from coverage in a trade credit insurance policy. Again, while each policy is unique, trade credit insurance usually excludes coverage for losses arising out of, among other things, the following:

- Political risks such as war, invasion of, or acts by foreign enemies, hostilities, rebellion, revolution, confiscation, nationalisation, insurrection or military or usurped power, or **due to the order of any government, public or local authority or by any restrictions on trade transfers** ; and
- Natural disasters.

Trade credit insurance policies do not always define what constitutes an "order of any government, public or local authority" or a "natural disaster". As such, there is some uncertainty as to whether these exclusionary clauses will apply in a given case.

Questions for insureds and insurers

Given the outbreak of COVID-19 and the ubiquity of emergency orders, regulations, and amendments being made by domestic and international governments, the question looms as to whether trade credit insurance will cover certain losses arising out of the COVID-19 pandemic.

In particular, there are questions as to whether emergency orders, such as the government of Ontario's order to close all non-essential businesses, constitute an "order of any government, public or local authority" as contemplated by most policies. In other words, if a debtor business defaults on a contract of sale because it has been ordered to close its doors as a non-essential business, will coverage be excluded?

Furthermore, there are questions as to whether a pandemic such as COVID-19 constitutes a "natural disaster", such that any loss arising out of the pandemic would be excluded from coverage.

As things stand, there is no guidance in the case law regarding what constitutes an "order of any government, public or local authority" or a "natural disaster" in the context of a pandemic. Therefore, there is a degree uncertainty as to whether coverage may be excluded by an insurer as a result of losses arising out of COVID-19.

These difficult questions will require a thoughtful, in-depth analysis. Gowling WLG (Canada) LLP has extensive experience in dealing with crises, complex business losses, and contested insurance claims. Our professionals are available to meet with you or your organization to discuss any questions or concerns you may have regarding the impact of COVID-19 to your business, and the solutions that may be available.

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