The Taylor Wessing Insurance and Reinsurance Review of 2011

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The Taylor Wessing annual Insurance and Reinsurance Review summarises the key case law developments offering insurance and reinsurance throughout the year. Please note that some cases covered in this review may be subject to further appeal.

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Marine and Energy

Supreme Court rules on inherent vice Loss of jack-up rig under tow

***Global Process Systems Inc v Syarikat Takaful Malaysia Berhad* [2011][1]**
Supreme Court, 1 February 2011

As Lord Birkenhead LC noted in the famous case of *British & Foreign Marine Insurance v Gaunt* [1921][2], a policy on "all risks" terms cannot be held simply to cover all damage howsoever caused "*for such damage as is inevitable from ordinary wear and tear ... is not within the policies*". The principle is simply this: insurance covers risks, that is to say something that might or might not happen, and not certainties.

The point was developed further in *Soya GmbH v White* [1983][3], concerning a claim for heat damage to a consignment of soya beans on a voyage from Indonesia to Antwerp. The court in that case drew a distinction between cargo shipped with greater than 15% moisture content, which on the expert evidence it said was bound to suffer heat damage during the intended voyage, and cargo shipped with between 13% and 15% moisture content, which it said "*might or might not*" result in such damage. In the former case, damage would be regarded as inevitable and thus irrecoverable in principle; in the latter case the damage was fortuitous but resulted from an inherent vice, that is to say the moisture present in the cargo at the time of shipment. In that particular case the claim succeeded because the policy expressly included such loss, by way of an extension covering "*heat, sweat and spontaneous combustion*".

Commercial Court

The issue has recently come up for consideration again in the long running case of *Global Process Systems Inc v Syarikat Takaful Malaysia Berhad*. The claim concerned the loss of a jack-up rig being towed on a barge from Galveston to Malaysia. The jack-up rig design allows a working platform to be floated into position and jacked up on cylindrical legs, to suit the sea depth at the point of operation. Steel pins are engaged into the legs through pinholes spaced at six foot intervals and, to reduce stress at the corners of the pinholes, circular holes are incorporated at each corner roughly an inch and a half in diameter. For the present tow, the rig was carried on a barge with its legs in place and elevated in the air above the deck.

The tow was interrupted mid way through the voyage, near Cape Town, where some cracking was found in the way of certain of the pinhole corners. Repairs were carried out and the voyage resumed, but soon after three of the legs broke off and fell into the sea.

The rig was insured as cargo under Institute Cargo Clauses (A), containing the standard exclusion in respect of loss or damage caused by "*inherent vice or the nature of the subject matter insured*".

At the initial trial, insurers argued that the loss was inevitable and as such there was a lack of the necessary fortuity. Alternatively, they relied upon the inherent vice exclusion. They argued that the legs were not capable of withstanding the normal incidents of the tow, as demonstrated by the fact that they failed in weather conditions that could reasonably have been expected on this voyage. For their part, the assured contended that the question of inevitability had to be judged subjectively; thus, they argued, a claim for inevitable loss would be recoverable unless it could be shown that the assured knew the loss to be inevitable when taking out the insurance. As to inherent vice, the assured contended that the true proximate cause was the failure to carry out adequate repairs in Cape Town.

1 [2011] UKSC 5
2 [1921] 2 AC 41
3 [1983] 1 Lloyd's Rep 122

In the Commercial Court, the trial judge determined that the failure of the legs, though very probable, could not be said to be objectively "inevitable". Citing the *British & Foreign* case, the judge noted that the onus of proving fortuity "*represents a low hurdle for the assured*", which in this case the assured had cleared. As such, the insurers' defence of lack of fortuity failed.

However, the trial judge went on to confirm that a loss could still be caused by inherent vice though not be inevitable. On this point, the Commercial Court took account of the approach in *Mayban General Insurance v Alstom Power Plants* [2004][4], in which the trial judge put it this way:

> "If the conditions encountered by the vessel were more severe than could reasonably have been expected, it is likely that the loss will have been caused by perils of the sea (though even then there might be evidence that the goods would have suffered the same degree of damage under normal conditions). If, however, the conditions encountered by the vessel were no more severe than could reasonably have been expected, the conclusion must be that the real cause of the loss was the inherent inability of the goods to withstand the ordinary incidents of the voyage."

Adopting the above approach, the trial judge in *Syarikat* noted that the legs of the rig had broken off despite the fact that the weather experienced was within the range that could reasonably be contemplated. That was enough to lead to the conclusion that the cargo was incapable of withstanding the ordinary incidents of the voyage, and as such the proximate cause of loss was inherent vice.

Court of Appeal

The matter proceeded to the Court of Appeal, which reversed the decision of the Commercial Court, in a Judgment handed down on 17 December 2009. Having reviewed the authorities and academic texts in some detail, the Court of Appeal came to the conclusion that the test for claims on a cargo policy should in principle be no different to that for hull policies. While not formally overruling *Mayban*, the Court of Appeal said that, if the action of the sea is the immediate cause of the loss, which clearly was true here, a claim may still lie under the policy even though the conditions were within the range of "*what could reasonably be anticipated*". If, on the other hand, the cargo had been damaged by the motion of the vessel in weather that could be described as "*perfect*" or "*favourable*", then the obvious inference in most cases would be that any damage was indeed the result of inherent vice or the nature of the cargo. The *Mayban* case, said the Court of Appeal, was not creating a strict rule of evidence one way or the other, so much as a matter of inference.

In the present case, the wave conditions may well have been foreseeable but the Court of Appeal considered that they were not so benign as to create, on their own, an inference of inherent vice. On the evidence, metal fatigue was not the sole cause of the loss of the legs. Rather it was a "*leg breaking wave*" that had caused the starboard leg to break off, something that was "*not bound to occur in the way it did on any normal voyage round the Cape*". The loss of the starboard leg led to the others being at greater risk and so they, in turn, also broke off. Though with hindsight this may have been a "*highly probable*" chain of events, that was not enough to render the proximate cause something other than the perils of the sea, a risk for which the assured was covered under the policy.

Supreme Court

The matter then proceeded to the Supreme Court, which handed down judgment on 1 February 2011. The Supreme Court affirmed the decision of the Court of Appeal, but went further in formally overruling the *Mayban* decision. In so far as *Mayban* found that inability of a cargo to withstand the ordinary perils of the seas amounted to inherent vice, that case was wrongly decided, said the Supreme Court. Its effect would be to reduce much of the purpose of cargo insurance, for the cover would then only extend to loss or damage caused by perils of the sea that were exceptional, unforeseen or unforeseeable, and not otherwise. This was inconsistent

4 [2004] 2 Lloyd's Rep 609

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with the purpose of an all risks cargo policy, namely to provide an indemnity in respect of loss or damage caused by, among other things, all perils of the seas.

The court was therefore left to determine what was, in fact, the proximate cause, unconcerned by whether the sea state could be said to be exceptional or not. Applying the *Soya v White* test, the Supreme Court concluded that this could not be inherent vice, since inherent vice called for damage to the cargo as a result of its "*natural behaviour*" and "*without the intervention of any fortuitous external accident or casualty*". In this case there had indeed been an external fortuity involved, namely the rolling and pitching of the barge in the sea conditions encountered during the voyage. This had caught the first leg at just the right moment to produce stresses sufficient to cause it to break off, thereby leading to increased stresses on the remaining legs and their subsequent breakage. This process could not be anything other than an insured peril of the sea, and consequently the loss was covered.

Court of Appeal rules in Somali piracy case

Masefield AG v Amlin Corporate Member Ltd **[2011][5]**
Court of Appeal, 26 January 2011

Background

Under the provisions of the Marine Insurance Act 1906, a total loss of the insured subject matter may be actual or constructive; a marine policy will cover both, unless it expressly provides otherwise. An actual total loss (ATL) calls for the subject matter to be destroyed or for the assured to be "*irretrievably deprived thereof*". A constructive total loss (CTL), exists where the subject matter is "*reasonably abandoned on account of its actual total loss appearing to be unavoidable*". This will be so where the assured be presently "*deprived*" of the subject matter and that either (a) it is unlikely that he can recover it, or (b) the cost of doing so would exceed the value once recovered.[6]

Where a CTL exists, the assured may either treat the loss as a partial loss, or he may elect to treat it as if it were an ATL, by giving notice of abandonment to the insurer.[7] In many cases, the insurer will decline the notice of abandonment, often disputing that circumstances exist amounting to a CTL, but typically the parties will agree that proceedings are deemed to have been commenced as at the date of the relevant notice. Consequently, the question of whether a CTL existed, or not, is measured against the circumstances present at the date of the notice, rather than by reference to what happened subsequently.

The present case concerned an insured cargo of bio-diesel on board a tanker bound from Malaysia to Rotterdam, which was seized by pirates in the Gulf of Aden.

The pirates took the vessel to Somali waters, but negotiations soon ensued with the owners of the vessel, with a view to the release of the vessel, cargo and crew. While those negotiations were still ongoing, notice of abandonment was served on the insurers, who refused to accept it, but agreed to the date of notice as the deemed date of proceedings.

The negotiations with the pirates were ultimately successful. Some 10 days after the date of the notice, shipowners paid an agreed ransom to the pirates and the vessel was released. She proceeded to Rotterdam where the cargo was safely discharged. The insured cargo owners nevertheless pursued their total loss claim on the policy, in preference to taking delivery of the cargo. The court was therefore required to decide whether the seizure by the Somali pirates amounted to a total loss, notwithstanding the subsequent recovery of the cargo.

5 [2011] EWCA Civ 24
6 s. 60(2) Marine Insurance Act 1906
7 ss. 61 and 62 Marine Insurance Act 1906

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Commercial Court

The matter went to trial in the Commercial Court, upon which judgment was delivered in February 2010.

Firstly, on the question of an ATL, the Commercial Court noted that the test of whether the assured had been "*irretrievably denied*" the cargo was an objective one, to be assessed at the relevant time against the true facts then present, whether all of those facts were known to the assured or not[8]. Although the actual fact of recovery of the vessel and cargo within a short period was not directly material, let alone decisive, the court was entitled to consider what in fact happened after the relevant date in so far as that might assist in showing what the probabilities really were.[9] Moreover, the correspondence following the seizure, and the information in the public domain at that time, showed that all interested parties were fully aware that the cargoes were likely to be recovered, a view also consistent with the unchallenged expert evidence. Other vessels seized by Somali pirates had been promptly released following negotiations over a relatively short period. The vessel and cargo were safely recovered only 11 days later upon payment of a ransom, representing only a tiny proportion of the value of the ship and cargo.

The trial judge also noted that an assured could not be said to be "*irretrievably deprived*" of property if it was legally and physically possible to recover it, even though such recovery could only be achieved by disproportionate effort and expense[10]. Rather, the assured had to establish that the recovery was not possible. Mere capture by pirates did not, of itself, constitute an ATL,[11] not least since acts of pirates did not necessarily occasion any loss at all. The impact and effect of such a capture was very much dependant upon the facts, and, on the facts of the present case, the assured had lost only possession and not the property in its goods. Recovery of possession was not legally or physically impossible, and indeed was expected after the usual period of negotiation.

As to the alternative CTL claim, this also failed in the Commercial Court, for two reasons. Firstly, the cargo had not, in truth, been "*abandoned*" for the purposes of section 60, which required abandonment of any hope of recovery[12]. Although notice of abandonment had been served, the reality was that the shipowners and the cargo owners had every intention of recovering their property and were fully hopeful of doing so. Secondly, for all the reasons considered in the context of the ATL claim, it could not be said that there was a reasonable basis for regarding an actual total loss as "*unavoidable*", without which there could be no valid CTL.

Finally, the court also rejected the assured's alternative public policy argument, namely that a release of the subject-matter in response to payment of a ransom should not be treated as a relevant or appropriate consideration when deciding whether a vessel and her cargo were, in practice, irrecoverable. The court noted that payment of a ransom was not illegal, nor could it find any "*clear and urgent reason*" to categorise it as contrary to public policy. On the contrary, the courts have previously held that ransom payments are recoverable as sue and labour expenses incurred pursuant to the assured's duties under section 78(4) Marine Insurance Act 1906[13].

On this basis, the Commercial Court found in favour of insurers, against which finding the assured appealed.

Court of Appeal

The case presented by the assured in the Court of Appeal was more limited in scope. Firstly, the argument was focused purely on whether there had been an ATL. The CTL case was no longer under consideration. It was the assured's case that seizure by pirates automatically amounted to

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8 *Marstrand Fishing Co Ltd v Beer* (1936) 56 Ll L Rep 163
9 *Bank Line Ltd v Arthur Capel & Co* [1919] AC 435
10 *Fraser Shipping Ltd v Colton* [1997] 1 Lloyd's Rep 586 QBD
11 *Dean v Hornby* [1854] EngR 113
12 *Court Line Ltd v R* [1945] 78 Ll L Rep 390
13 *Royal Boskalis Westminster NV v Mountain* [1999] QB 674

an ATL, as a rule of law. What actually happened thereafter, as a matter of fact, was irrelevant, they said. Alternatively, argued the assured, seizure by pirates amounted to an act of "theft" within the English criminal law definition. Under the Theft Act 1968, a person who takes the property of another with the intention of returning it only upon terms inconsistent with the owner's rights[14] is guilty of theft. Since theft is an insured peril in its own right, said the assured, an insured loss by theft occurred at the moment of seizure.

As to public policy, the assured conceded that the payment of a ransom was neither illegal nor was it formally contrary to public policy. Nevertheless, it amounted to submission to extortion, and hence was so undesirable from the point of view of the public interest and universal principles of morality, that it could not form part of the assured's *duty* to avert or minimise the loss. If payment of a ransom could not be *required* of an assured, as part of its duty under section 78(4), then it must follow that the ATL was suffered at the point when the vessel was seized, or at any rate when notice of abandonment was given.

The Court of Appeal dismissed the assured's appeal on all grounds. Affirming the decision of the trial judge on the question of the ATL, the court held that there was no rule of law that seizure by pirates equalled an ATL. Such a seizure *may* go on to mature into an ATL, but that depended upon the facts. In this case, the facts were clear. There was not only a chance, but a strong likelihood, that payment of a ransom of a comparatively small sum, relative to the value of the vessel and her cargo, would secure the recovery of both. This was no irretrievable deprivation of property, so much as the typical "wait and see" situation. The court noted that the facts would not even have supported the CTL claim, since it could not be said that there was an "*unlikelihood*" of recovery.

As to the theft argument, this confused the concept of the "peril" with that of "loss". While theft was a peril insured against, what was required to pursue an insurance claim was the occurrence of a loss as a result of the said peril. There could be no loss without irretrievable deprivation.

Turning finally to public policy in the context of section 78(4), the Court of Appeal could find no universally recognised principle of morality to allow it to conclude that payment of a ransom was "*beyond the pale*" or "*without any legitimate recognition*". While it accepted that section 78(4) did not impose a duty on an assured to pay a ransom, it did not follow that a potential total loss which may be averted by the payment of such a ransom thereby became an ATL.

Confirmation of P&I coverage and estoppel

Micoperi SrL v The Shipowners' Mutual Protection and Indemnity Association **[2011][15]**
Commercial Court, 21 October 2011

The Claimant in this case (Micoperi) was a shipowner based in Italy. On 3 October 2005, one of its vessels was involved in an incident in the Black Sea, in consequence of which it found itself faced with claims from a third party, Toreador Turkey Ltd (Toreador), in the sum of €11.6m. Micoperi denied liability for the claim, and indeed asserted its own cross-claim against Toreador for unpaid invoices of €4.5m, for which it had contemplated arresting property belonging to Toreador, namely a consignment of steel pipes awaiting treatment at a yard in Sicily.

In July 2006, Toreador arrested the vessel in Palermo in support of its claim against Micoperi. It offered to release the vessel in exchange for security, while at the same time offering to provide counter-security with respect to Micoperi's cross claim. In the normal way, Micoperi turned to its P&I Club (the Club), the Defendants, for assistance. The Club confirmed cover and duly provided security in the form of a standard letter of undertaking (LoU). The vessel was released. The parties then turned their attention to their substantive claims against each other, to be litigated in the English High Court. The Club appointed solicitors to act for its member, Micoperi, in those proceedings.

14 For example, against payment of a ransom
15 [2011] EWHC 2686

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At that point, however, matters took an unexpected turn. The Club's managers belatedly came to the view that the loss was not, in fact, covered after all, because the casualty resulted from "*specialist operations*" and was thus excluded from the P&I cover. Nevertheless, the Club agreed to continue the management of the English litigation on Micoperi's behalf, but under a reservation of rights. In due course, that litigation proceeded to mediation, resulting in a settlement by which Micoperi agreed to pay a net sum of €5.8m to Toreador. The Club was bound to make good the settlement sum directly to Toreador under the LoU, but it sought to recover the said payment from its member, Micoperi, alleging that there was in fact no policy coverage. That dispute was referred to arbitration under the Club rules.

In defence of the Club's claim, Micoperi argued that the Club was estopped from denying coverage, having given a clear representation of cover at the outset, upon which representation Micoperi said it had relied by not settling Toreador's claim sooner and/or not arresting Toreador's property as security for the cross-claim, and generally in accepting a settlement which it (Micoperi) thought was too high. Consequently, argued Micoperi, it would now be inequitable to permit the Club to enforce its alleged right to deny coverage.

The arbitrators found against Micoperi. Although they accepted that the Club had conveyed an unequivocal confirmation of cover, they concluded that Micoperi had not acted in reliance upon that representation in any way. Micoperi in turn appealed against that decision to the Commercial Court, alleging an error of law or serious irregularity in the tribunal's reasoning.

In a judgment handed down on 21 October 2011, the Commercial Court refused to overturn the tribunal's decision. Micoperi having asserted that the €5.8m settlement was "*much too high*", the court considered that it was quite proper for the arbitrators to reach a view as to whether that was true or not; in their assessment, a net settlement at €5.8m was in fact the best that could have been achieved, and it correctly took into account Micoperi's counterclaim for unpaid invoices. It followed that Micoperi had not relied upon confirmation of Club cover in agreeing the settlement, since it was not a deal that could have been improved upon in any case. As to Micoperi's forbearance in arresting the pipes in Sicily, Micoperi's alleged reliance was overtaken by the fact that Toreador, in fact, provided security for that claim. Consequently, nothing was lost by their failing to arrest.

War Risks
Arrest proceedings and the meaning of "ordinary judicial process"

***Melinda Holdings SA v Hellenic Mutual War Risks Association (Bermuda)* [2011][16]**
Commercial Court, 18 February 2011

While P&I Club war risk rules are intended to insure vessel owners in respect of capture, arrest and restraint, they will ordinarily exclude such losses where they arise merely in the course of the "*ordinary judicial process*". Thus, a normal judicial arrest in the context of, for example, a claim for cargo damage, or pollution liability, does not thereby give rise to a war risk loss by arrest or restraint.

The circumstances behind the present case began in 1996, with the grounding of the vessel SAFIR on coral reefs off the Egyptian coast, causing substantial environmental damage. Proceedings were brought by various Egyptian government agencies in the Port Said court against the owners of the SAFIR, Fonderance Overseas Inc (Fonderance), and the managers Seama International Shipping (Seama), leading to a judgment in December 1996.

The judgment included two elements of so-called court dues commonly imposed in Egyptian proceedings against unsuccessful defendants. The first element, in this case 5% of the amount claimed, was referred to by the court as proportional court fees, payable to the Egyptian

16 [2011] EWHC 181 (Comm)

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National Treasury. The second element, representing 2.5% of the claim, was described as a payment to the "Judges' Fund" or the "Judicial Services Fund", used to pay for the health and welfare of present and former judges, state lawyers, and their families. At the time of the present proceedings, the entire judgment against Fonderance and Seama remained unsatisfied.

Some 12 years later, in December 2008, the vessel SILVA was arrested by the Port of Suez court, purportedly in execution of the 1996 judgment, upon an application brought at the behest of the court claims office, specifically in pursuit of the court dues element of the judgment. The arrest was sought upon little more than the bald assertion that the beneficial owners of the SILVA and the SAFIR were one and the same, supported by documentation which the English court found to be forged in any event. In truth, there was no connection between the owners of the two vessels, a fact that was clear from other evidence put before the Egyptian court. Nevertheless, the arrest was ordered and maintained.

It was common ground that the vessel was a total loss. The issue between the assured and the defendant insurer was simply whether the loss took place in the course of "*ordinary judicial process*". In considering the meaning of the expression, the Commercial Court referred to the earlier decision of Mocatta J at first instance in *The Anita* [1970][17] thus:

> "In my opinion the words "ordinary judicial process" ... refer to the employment of Courts of law in civil proceedings. If a rationale be required for this, it is that in such cases the State is merely providing a service to litigants, rather than exercising its own power through the Courts for its own purposes."

As a starting point, the court noted in the present case that the purpose of the claim was to enforce and recover, amongst other things, the judges' fund for its benefit. Thus, the judges were pursuing their own purposes, and moreover hearing their own cause, which inevitably put their independence in question. The English court also found that the forged documents upon which the arrest had been sought had come from a ship chandler who had an arrangement with the Egyptian authorities and the court to assist them for reward in the collection of court dues. Far from being an "*ordinary judicial process*", this was in fact an exercise in extortion from owners of an innocent and unconnected vessel of sums owed in respect of another vessel. The exercise was pursued in the expectation that sums would be paid out, or, at the very least, secured (with judgment or compromise likely to follow), so that the court's purpose of recovering the monies could be achieved. This could not be described as an "*ordinary judicial process*", and consequently the court found for the assured.

In the alternative, the insurer contended that the assured had failed in its duty to sue and labour. Specifically, it was said that an ordinarily competent Egyptian lawyer would have advised the assured to act differently in response to the proceedings, with different results. There could have been an offer of Club security, for example, to release the vessel from arrest, or a separate claim for wrongful arrest; the assureds could have issued an application for recusal (removal of the Judge) or relied upon time bar defences. Having heard all of the evidence, the English court was satisfied that none of these steps were likely to have succeeded, and indeed in some cases they would have risked making matters far worse. At any rate, no criticism whatever could be made of the way in which the assured and its lawyers handled a "*difficult and intractable situation*". That being so, there was no breach of the duty to sue and labour.

17 [1970] 2 Lloyd's Rep 265, at 377

Offshore Energy
Meaning of "100%" and scaling for interest

Gard Marine & Energy v (1) Lloyd Tunnicliffe; (2) Glacier Re & Anor [2011][18]
Commercial Court, 30 June 2011

We have previously reported on this case in the context of a dispute about law and jurisdiction[19]. Specifically, the second reinsurer, Glacier Re, being a company based in Switzerland, sought to challenge the jurisdiction of the English court, preferring to have the matter determined in Switzerland under Swiss law. They were unsuccessful in that attempt, and the dispute between the Claimant and Glacier Re was subsequently settled.

That left the English court to address the merits of the dispute as between the Claimant (Gard) and the remaining reinsurer defendant, Lloyd's Syndicate 780 (Advent).

The background is that Gard took a 12.5% line on an operating package policy issued to Devon Energy Corporation (Devon), an independent oil exploration company with an interest of varying percentages in a number of wells in the Gulf of Mexico. The policy included cover for all risks of loss or damage to offshore and onshore property and associated business interruption, subject to a combined single limit of "*US$400,000,000 (for interest) any one accident or occurrence arising from a named windstorm in the Gulf of Mexico*".

Gard then purchased facultative reinsurance from the reinsurers, including Advent, subject to the following provision as to Sum Insured:

> "To pay up to Original Package Policy limits / amounts / sums insured excess of US$250m (100%) any one occurrence of losses to the original placement."

At the heart of the dispute was the meaning of the expression "100%", in so far as related to the claim for Devon's Hurricane Rita losses.

The gross Hurricane Rita loss from the ground up in connection with the assets insured by Gard was put at US$912.5m. Of that, Devon's interest was around 45.6% or US$416m, narrowly exceeding the original policy limit of US$400m. Accordingly, the claim was treated as a limits loss to the original policy, although in fact only US$365m was paid, reflecting a US$35m agreed discount for early settlement. Of the said amount of US$365m, Gard's 12.5% share was US$45,625,000.

The question for the court concerned the operation of the US$250m attachment point in the reinsurance, in the context of the expression "100%". Advent contended that the stated Sum Insured referred to the loss suffered by the full market of insurers subscribing to the original policy. They argued that the expression "*losses to the original placement*" meant just that. In other words, only if Devon's interest generated a claim on the original policy in excess of US$250m would this translate into a liability to indemnify Gard for the excess of this amount, as to Gard's 12.5% share.

By contrast, Gard argued that the reference to "100%" meant that the excess point was to be measured against the insured value of the original lost asset, and not merely Devon's interest in that asset. Thus, where Devon had only a percentage interest, as here, the US$250m figure was required to be scaled down. In the present case, Devon's interest was 45.6%, and so Gard argued that the attachment point in the reinsurance must be reduced from US$250m to US$114m, thereby enlarging the percentage of Gard's own losses amenable to a reinsurance recovery.

The difficulty was that none of this was spelled out expressly under the Sum Insured clause in the reinsurance. That contrasted with the original policy, which defined the term "100%"

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18 [2011] EWHC 1658 (Comm)

19 Taylor Wessing Insurance and Reinsurance Update, 20 October 2009 (Commercial Court) and Taylor Wessing Insurance and Reinsurance Review of 2010, page 13 (Court of Appeal).

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as assuming a 100% interest in the relevant well, and calling for a scaling of retentions where the assured held less than a 100% interest[20]. It was common ground that the expression "*for interest*" or "*for Assured's interest*", as it applied to the US$4m original policy limit, had the opposite effect.

Gard argued that the meaning of 100% in the reinsurance should be taken to have the same meaning as that defined under the original policy. Moreover, they contended that this was also consistent with market practice in the offshore energy market, where the 100% reference carried a specialised meaning, requiring scaling for interest.

After considering detailed expert evidence adduced by the parties, the Commercial Court found for Gard. In the judge's view, the weight of evidence did indeed establish a recognised and established meaning, as they had contended.

The court was then required to consider an alternative case of avoidance for misrepresentation. It was Advent's case that the reinsurance risk had been presented on the premise that the maximum exposure was US$135m, an assertion said to have been made by Gard's brokers at Advent's underwriting box. On the policy construction now determined by the court, that was not true, since the exposure could exceed this amount by reason of scaling for interest. Accordingly, Advent contended, the risk had been misrepresented, for which it claimed to be entitled to avoid.

Again, the court found for Gard. The alleged misrepresentation was said to have been made in an oral exchange almost six years ago, and not corroborated in any subsequent written communication. On the contrary, the underwriting notes that accompanied the broke made no mention of maximum exposure, and it was also significant that Advent raised the avoidance point only in September 2007, even though the scaling point had become an issue as early as December 2005. The implication, clearly, was that the avoidance case was in truth something of an afterthought. Perhaps more compelling still was the fact that Advent's underwriter was himself an experienced offshore energy reinsurer. He could form his own view as to the legal effect of the policy terms, and if he disagreed with the broker's interpretation he was free to challenge it and indeed to request an appropriate variation to the wording to make the position clear.

Builders' risks
Co-insurance and waiver of liability

***BMT Marine & Offshore Survey Ltd v Lloyd Werft Bremerhaven GmbH* [2011][21]**
Commercial Court, 24 January 2011

Where a Claimant (A) sues a Defendant (B) the latter may deny liability on the grounds of lack of any wrongdoing. Alternatively, B may accept liability for breach of duty but he may contend that the loss was, at least in part, also the result of wrongdoing on the part of C, either by way of breach of C's contract with A or as a joint tortfeasor. The result is that C may be held liable to contribute to the damages payable to A, under a mechanism governed in England by the Civil Liability (Contribution) Act 1978 (the 1978 Act).

The present case concerned a fire at a shipyard belonging to Lloyd Werft Bremerhaven GmbH (LWB), which occurred while repair and conversion work was being carried out on the vessel m/v 'CALA PALMA'. The vessel suffered significant damage in the fire.

The conversion works were being undertaken pursuant to a contract between Owners and LWB, which provided for German law and for the exclusive jurisdiction of the Courts of Hamburg.

20 Similar provisions appear in the *Bermuda Form* XL 004 and the Oil Casualty umbrella policy, both of which make express provision for the abatement of attachment points in the case of "joint ventures".

21 [2011] EWHC 32 (Comm)

At the time of the fire the vessel was insured under a hull policy incorporating the Institute Time Clauses - Hulls - Port Risks (20.07.87), and selected clauses of the Institute Clauses for Builders Risks (1.6.88), but with the choice of English law expressly overridden in favour of Italian law. As required under the terms of the conversion contract, the policy named both the Owners and LWB as co-assureds, though it did not refer to any express waiver of subrogation against LWB. It also required, as a condition precedent to liability, that a shipyard and/or project risk assessment survey be carried out by BMT Marine and Offshore Survey Ltd (BMT).

Following the fire, the insurers settled the claim from their assureds, the Owners, and thereby took an assignment of the attendant subrogation rights under Italian law. In pursuit of those rights, they commenced English proceedings against BMT, alleging that they had failed to exercise reasonable skill and care in the conduct of the risk assessment survey, in particular in relation to the review of hot works procedures adopted by LWB and its sub-contractors. For its part, BMT denied any lack of reasonable skill and care, and contended that the cause of the fire was in fact the negligence and/or breach of contract by LWB (or its sub-contractors) in carrying out the hot works.

Accordingly, BMT brought the present Part 20 proceedings against LWB, claiming a contribution or indemnity from LWB under the 1978 Act. In response, LWB contended that, as a matter of German law and on the proper construction of the conversion contract, Owners had agreed to waive or surrender any right to claim against LWB, whether in contract or in tort in respect of work done to the vessel. Consequently, argued LWB, they were under no liability to Owners, and hence could not be obliged to contribute.

The first question for the court to consider was whether, as a matter of German law, the conversion contract did indeed excuse LWB of liability to Owners, as alleged. LWB argued that it did, and that was why the contract required insurance to be procured for the benefit of both it and Owners. The risk of losses was to be borne by insurance, not by means of claims between the parties. BMT, on the other hand, contended that LWB remained liable to Owners, but simply that Owners were required to procure insurance of the type stipulated.

The German law experts[22] agreed that until 2000 there had been a line of cases in the German Federal Supreme Court to the effect that contracts which provided for co-insurance were generally regarded as amounting to a waiver of liability between the parties in relation to liability for losses covered by the insurance. Since then, however, BMT contended that German law had developed in a different direction, such that co-insurance no longer amounted to a waiver. While, clearly, there could be no exercise by insurers of *subrogation* rights between co-assureds, that was not the case here, since the Part 20 claim was being pursued by BMT, not by Owners' insurers.

The court accepted that, under German law, it was entitled to take into account not merely the wording of the final contract, which in this case was not entirely clear, but also the intention of the parties as revealed in the negotiations leading up to it. Having reviewed all of the evidence, it concluded that LWB were intended to benefit from a waiver of liability under the contract, save in those cases where builders' risks insurance had been withdrawn due to the fault of LWB's management.

On the basis, therefore, that LWB owed no liability to Owners for the loss, there could be no claim for contribution under the 1978 Act, since it could not be said that BMT and LWB were together "*liable in respect of the same damage*".

22 Taylor Wessing provided the German law expert evidence on behalf LWB.

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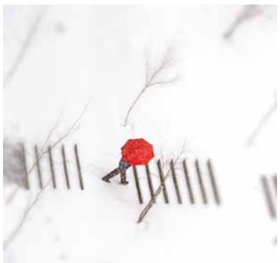
Liability Insurance

Commercial Court rules again on "series of related events"



Beazley Underwriting Ltd & Anor v The Travelers Companies Incorporated [2011][23]
Commercial Court, 17 June 2011

In May 1997 the Defendant (Travelers) sold the Minet Group of broking companies to Aon. Under the terms of the deed of sale, Travelers agreed to indemnify Aon against any loss, liability, claim or cost relating to the conduct or business of the Minet Group and arising out of any event or matter occurring on or before the date of completion.

The deed also provided that where there was a continuing series of related events, occurrences or matters which otherwise amounted to an indemnified claim then all such events etc. occurring during the period of 12 months *following* completion would be deemed to have arisen or occurred *prior* to completion.

Travelers procured PI insurance to cover the liabilities assumed by them under the deed, on a claims made basis. The particular policies issued by the Claimants (Beazley) covered the period between the sixth and seventh anniversaries of the deed, and were the last in a series of three such contracts bought by Travelers.

The Minet book of business transferred to Aon included the Standard Life Assurance account, which Minet had itself acquired with its purchase of SRS Insurance Services in 1995. In particular, Minet/SRS had for some years been responsible for broking Standard Life's own PI insurance, and each year the cover was renewed on the same terms. After the transfer in May 1997, Aon continued to renew Standard Life's PI insurance on its predecessor's expiring terms.

As it turned out, so the court found,[24] those terms were inappropriate for Standard Life's requirements, because the excess provision (referring to each "*claim and/or claimant*") meant it was impossible for Standard Life to aggregate like claims from multiple consumers. The impact was felt acutely in the 1998-2001 policy period, broked by Aon, during which time Standard Life faced 97,000 claims for endowment mortgage mis-selling, generating an aggregate liability of more than £100m. Accordingly, Aon was held liable to Standard Life in negligence for failing to procure suitable insurance cover, for which Aon in turn looked to Travelers under the indemnity.

The present litigation was concerned with Travelers' corresponding claim against its own PI insurers, Beazley. The latter denied liability on two grounds:

- that Travelers were not themselves liable to Aon under the deed; and
- that even if Travelers were liable to Aon there was no claim under the PI policy.

Beazley were successful on both counts.

Matters occurring after completion were subject to the indemnity in the deed only if they formed part of a continuing series of related events or matters existing *before* the completion date. That was not the position, on the facts of this case, so the court found. The particular instance of negligent broking that gave rise to Standard Life's claim was that committed by Aon in 1998. Even if that act of negligence took place within 12 months of the completion date (a point about which there was also a factual dispute), and even if it took an identical form to the prior acts of negligence committed by its predecessor, it was nevertheless a separate event or matter, rather than merely forming part of an earlier related series. Upon the 1998 renewal, Aon was subject to a distinct duty to Standard Life to procure a policy suitable for its needs. Accordingly, Travelers owed no liability to Aon under the deed.

23 [2011] EWHC 1520 (Comm)
24 In *Standard Life Assurance v Aon* [2008] Lloyd's Rep IR552

Moreover, even if the position were otherwise, the court held that Beazley would have no liability to indemnify Travelers under the latter's PI policy. That policy responded only to Wrongful Acts committed by the insured (Minet) and its employees, not those of Aon. While the policy did extend to cover events during the 12 months after the completion date, but which related to Wrongful Acts committed before it, it remained a requirement that the said Wrongful Acts were those of Minet. In this case, the negligence was committed by Aon, and so fell outside the policy coverage.

Breach of notice requirements and loss of a chance

Milton Keynes Borough Council v Nulty & Ors [2011][25]
Technology and Construction Court, 3 November 2011

Liability insurance policies invariably contain provisions requiring the insured to give prompt notification of a claim, or of any incident that may give rise to such a claim, and not to admit liability for the claim without the insurer's consent.

In many cases, the notice requirements will be expressed as a condition precedent to liability, such that breach will automatically relieve the insurer of all liability for the relevant claim[26]. In cases where the requirement lacks the quality of a condition precedent, however, the insurer's position is much more uncertain.

The policy in this case contained a "Claims Conditions" clause, stipulating that "*the Insured shall on the happening of any incident which could result in a claim under this Policy immediately notify and send written confirmation to the Company*".

The claim against the insured arose from a fire in 2005, at a waste disposal site operated by the Claimant. The Claimant contended that the fire was caused by a cigarette discarded by the insured Defendant (Mr Nulty), an electrical contractor. Mr Nulty had been interviewed shortly after the fire in April 2005, and again in February 2006, on the second occasion under a police caution. However, it was only nine months later, after the insured received a letter of claim from the Claimant, that the matter was first made known to his liability insurers, NIG.

NIG responded with a reservation of rights "*due to the very late reporting of this matter*" and subsequently went on to deny liability to indemnify. Initially, NIG contended that the Claims Conditions clause had the quality of a condition precedent, but they subsequently conceded that this was not so. Accordingly, NIG needed to establish that it had suffered quantifiable prejudice as a result of the late notification.

On the evidence before the court, it was concluded that the fire had indeed resulted from a cigarette discarded by Mr Nulty. In other words, on the balance of probabilities (51% or greater) this was the cause. Nevertheless, NIG contended that, if it had been notified promptly, it would have appointed fire experts to undertake a forensic investigation, which may have yielded evidence in favour of an alternative theory of causation.

The most that could be said was that NIG had suffered the loss of a chance, namely the chance of proving a cause other than Mr Nulty's discarded cigarette, However, valuing such a lost opportunity was "*fraught with difficulty*", so the court acknowledged, since there was no obvious logical way of arriving at an appropriate percentage. By definition, there was no evidence of an alternative cause, the opportunity to search for such evidence having been lost, and hence any quantification of the lost chance was required to take place in a vacuum. Nevertheless, taking into account the circumstances as a whole, the judge in this case felt able to assess NIG's lost chance at 15%. Accordingly, NIG's liability for the loss was reduced by the corresponding proportion.

25 [2011] EWHC 2847 (TCC)
26 See for example, *Kosmar Villas v Trustees of Syndicate 1243* [2008]

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This is one of the rare cases where insurers have successfully claimed damages for the lost chance of successfully defending proceedings for late notification. Such a claim is necessarily speculative and difficult for insurers to prove. It is for this reason that conditions precedent to liability are always to be preferred, from insurers' perspective.

Breach of Warranty

Loss of right by election?

Argo Systems FZE v Liberty Insurance (Pte) & Anor [2011][27]
Court of Appeal , 15 December 2011

The Claimant (Argo) was the owner of a floating casino purchased for scrap, which was to be towed as a dead ship from the US Gulf to India. They procured insurance for the tow subject to the Institute Voyage Clauses – Hulls, through their local US producing broker DeWitt Stern Imperatore (DSI). The policy contained a warranty that "*...no release, waivers or "hold harmless" given to Tug and Towers*".

On 16 March 2003, less than two weeks into the voyage, the vessel developed a list and sank in 8,000ft of water in the Caribbean Sea. The London market insurers, Liberty, were initially represented by attorneys in Houston, who in July 2003 wrote to Argo rejecting the total loss claim. They did so firstly on the ground that the insured had failed to demonstrate loss by an insured peril, but they also alleged several misrepresentations, albeit without asserting a corresponding avoidance. They said nothing about the hold harmless warranty but concluded their letter with a reservation of their clients' right to alter their position "*in light of discovery of previously undisclosed information which would materially alter the facts and circumstances presently known*".

In May 2004, Argo sued both Liberty and their brokers, DSI, in the US Court in Alabama. The negligence case against the latter was necessary, limited by reference to the defence that Liberty were running to the policy claim. Liberty asserted coverage points, but neither the breach of the hold harmless warranty nor avoidance for misrepresentation featured at that stage; at the same time Liberty also challenged jurisdiction of the court in Alabama. Ultimately, they were successful in the jurisdiction challenge and Liberty were duly removed from the US proceedings in March 2006. The litigation continued against DSI alone, who succeeded in their defence.

In February 2009, Argo commenced English proceedings against Liberty in respect of the loss. Liberty ran the same points in defence as those raised previously, but also relied in addition upon the hold harmless warranty. They noted that the towage had been agreed on the Towcon International Towage Agreement, containing the standard waiver of liability in relation to loss of or damage to the tow, and consequently alleged that the towage agreement was not compliant with the warranty. Liberty also asserted a right to avoid for the misrepresentations they had originally identified in 2003.

In a judgment handed down on 21 February 2011, the English Commercial Court held that there had indeed been a breach of the warranty. Although the Towcon form was the standard contractual form for towage contracts, and the waiver of liability therefore commonplace, the insurer could not be taken to know this. It could not be said that the insurer had agreed to subject the express warranty to the terms of the standard form.

However, the trial judge then went on to hold that Liberty had in fact lost the right to rely upon the breach of warranty, by its conduct. Although in July 2003 its lawyers had set out a general reservation of the right to assert new points in response to *fresh* information, Liberty had in fact been in possession of the towage contract since June 2003. Consequently, it already held the information to enable it to run the breach of warranty point, but had failed to do so at the time of

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27 [2011] EWCA Civ 1572

the US proceedings, or during the subsequent six years prior to the English litigation. It had thereby represented by conduct that it would not run the defence, and was estopped from now doing so.

Similarly, the trial judge found that Liberty had lost any right to avoid for the misrepresentation. While the letter of July 2003 identified the misrepresentations complained about, it neither sought to avoid the policy nor to tender return of the premium. He said it did not assist Liberty that the authors of the letter were their US attorneys; the firm had an office in London, and had asserted, without hesitation, the position of its insurer client under an English law contract.

Liberty appealed to the Court of Appeal, which handed down its judgment on 15 December 2011, reversing the decision of the trial judge. Taking the July 2003 letter in its entirety, the Court of Appeal held that it did not convey unequivocally the representation that additional points would be taken only in response to new information. The letter concluded, for example, with the rider that "*The foregoing is without prejudice to all the remaining terms and conditions of the policy*", a clear indication that Liberty were reserving the right to rely on any of the remaining terms and conditions of the policy in the future, if advised to do so, including in relation to matters already known to them. As to the fact that the breach of warranty point was not mentioned in the US proceedings, this was unremarkable since the dispute in those proceedings was primarily about jurisdiction, and hence the substantive defence to the claim was required to be raised only in general terms.

In the absence of an unequivocal representation that Liberty would not rely upon the breach of warranty point, Liberty had not lost the right to do so in the present litigation.

Utmost Good Faith

Moral hazard and the use of a "*fraudulent device*"

***Sharon's Bakery (Europe) Ltd v Axa Insurance & Anor* [2011][28]**
Commercial Court, 9 February 2011

This case represents the latest in a series of recent High Court decisions involving dishonesty in the presentation of claims[29].

The insured (Sharon) operated a wholesale bakery in North London, owned by its two directors, Mr Bension Nassim and Mr Ali Caplin. Prior to the formation of Sharon, Mr Nassim had run his own business, Sharon's Bakery (Wholesale and Retail) Ltd (SBWR) but in 2007 he had agreed to go in to business with Mr Caplin, with the formation of Sharon. Mr Caplin provided the premises for the new bakery, and Mr Nassim the equipment, which he bought from his former company, SBWR.

The new company also obtained finance for its operations from Lombard North Central Plc (Lombard), in the course of which it provided to Lombard a copy of an invoice from SBWR for the equipment that was being contributed by Mr Nassim. As SBWR and Sharon were related entities, however, Lombard demanded sight of an invoice from the ultimate supplier, so that it could verify the relevant valuation. Lombard was duly given what purported to be an invoice, made out to SBWR by a company called Bakequip (UK) Ltd (Bakequip), apparently evidencing the sale of the equipment to SBWR. It was marked "*paid in full with thanks*". In fact, so it turned out, the invoice was false. Although there was no suggestion that the equipment had come into the possession of Sharon by any illegitimate means, the fact was it had not been acquired by means of the sale from Bakequip purportedly evidenced by the invoice.

28 [2011] EWHC 210 (Comm)

29 See also *Direct Line Insurance Plc v Fox* [2009] EWHC 866 (Taylor Wessing Insurance and Reinsurance Review of 2009; page 1); *Yeganeh v Zurich Insurance Co* [2010] EWHC 1185; *Joseph Fielding Properties (Blackpool) Ltd v Aviva Insurance Ltd* [2010] EWHC 2192 (Taylor Wessing Insurance and Reinsurance Review of 2010, pages 2 and 22)

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On 8 June 2008 a serious fire took place at the bakery, for which Sharon sought to pursue a claim against the defendant all risks property insurers. In the course of presentation of the claim, the insureds also procured a second, identical, invoice from Bakequip for the same equipment, this time made out not to SBWR but to Sharon directly. The second invoice was tendered to insurers.

Upon discovering that there had been no such sale by Bakequip, whether to SBWR or Sharon, the insurers denied the claim and sought to avoid the policy on two grounds:

1. non-disclosure of the fact that a false invoice had been used in the course of securing a finance transaction with Lombard, constituting a moral hazard about which it was material for an underwriter to know; and

2. the presentation of a fraudulent device, namely the second invoice, in the pursuit of the policy claim.

For its part, Sharon contended that the invoice provided to Lombard was only ever designed to act as a valuation, and there was no criticism about the valuation *per se*. There was never any registered concern on Lombard's part as to whether, or how, Sharon had acquired title to the equipment. It simply wanted to know what it was worth. There was, therefore, no fraud as between Sharon and Lombard, and hence no fraudulent activity warranting disclosure to insurers.

As to the invoice provided in pursuit of the policy claim, it was common ground that this was not a fraudulent claim as such. The loss was genuine and the insured was not seeking to pursue a claim for a greater sum than that to which it was entitled. The only basis of the insurer's defence was the use of a "*fraudulent device*" in the pursuit of an otherwise valid claim, but such a defence could only succeed if it could be shown that the insured had used the false device to seek to improve or embellish the facts surrounding the claim.[30]

In reality, that was not the case here, argued the insured. Where they had passed on the document to insurers describing it as an "*invoice*" this was an oversight, as it was only ever intended to be tendered as a valuation. Moreover, the contrary inference made no sense. There was a perfectly valid set of documentation showing how the insured had acquired the equipment, and how Lombard had provided finance. It was wholly implausible, argued Sharon, that it would have committed a fraud in pursuit of its policy claim simply because it was more "*convenient*".

Insurers succeeded in their defence on both grounds. On moral hazard, the court concluded that the invoice provided to Lombard was designed to do more than merely evidence valuation. It purported to be evidence of a true sale and purchase agreement between Bakequip and SBWR, and in that it was a false document. It was used for a dishonest purpose, namely in furtherance of a finance application, and that would have been so even if a valuation was all that Lombard had required. On any view, the insured's conduct in furnishing the document to Lombard represented a moral hazard warranting disclosure to insurers.

As to the second invoice, the court again held that it was intended to be tendered as an invoice, and not merely as a statement of valuation. It amounted to a representation that there had been a supply of equipment from Bakequip to Sharon, when the insured knew there was no such transaction. While the policy claim might still have succeeded without it, the lie conveyed by the false invoice would have tended to "*yield a significant improvement in the insured's prospects of obtaining a settlement*". In short, it was tendered as a necessary step towards having the claim accepted, and hence the insureds were guilty of using a fraudulent means or device to obtain benefit under the policy. Consequently, all benefit under the policy was forfeited.

30 See *Agapitos v Agnew* [2002] EWCA Civ 247; [2003] QB 556

Broker Duties

Failure to advise on risk improvement requirements

Ground Gilbey Ltd v Jardine Lloyd Thompson UK Ltd [2011][31]
Commercial Court, 2 February 2011

On 9 February 2008, a serious fire occurred at Camden Market in north London, a property owned by the Claimant, GGL. The quantum of damage sustained was in the region of £6m. The cause of the fire was a liquefied petroleum gas (LPG) portable heating appliance which had ignited clothing stock in one of the stalls. While the use of LPG heaters was prohibited under the terms of the tenancy agreement with stallholders, the practice was nevertheless widespread.

The market was insured under a policy underwritten by Fusion Insurance, acting as agents for Aviva Insurance Ltd, covering property and other associated risks. The business was broked on behalf of GGL by the Defendant, Jardine Lloyd Thompson (JLT).

When Fusion originally quoted for the risk in 2005, it undertook a pre-risk survey, which identified the presence of LPG heaters, amongst other things, as a matter of concern. JLT recommended acceptance of Fusion's quotation to their principal, and reported to them on various matters identified in the pre-risk survey. They did not, however, refer to the removal of LPG heaters nor otherwise draw their principal's attention to the requirement.

Shortly before the 2006 renewal, Fusion carried out a further, pre-renewal, survey. Again, it identified LPG heaters as an issue. Once again, JLT reported to their principals on the finding of the survey, but this time they did also make reference to the removal of "*hazardous heaters and associated gas cylinders*". Two months after the 2006 renewal, a further survey took place, following which Fusion notified JLT of a number of required "*risk improvements*". It identified LPG heaters as a "*severe fire risk*" and stipulated again that they had to be removed. The insurers took the view that they could not impose the requirement as a warranty, since they recognised that GGL would not have day-to-day control over the individual stallholders, but nevertheless they asked JLT for confirmation that "*all unacceptable heating appliances have been removed*", a risk improvement that "*needs to be implemented immediately*". The stipulation was passed on to GGL.

The risk was surveyed once again at the time of the 2007 renewal, accompanied by a representative of JLT. It was observed that, while there was some attempt at enforcement by GGL, they were not keeping on top of the situation. Tenants, it was noted, were still widely flouting the rules. In response to this, Fusion escalated the obligation of compliance. Upon renewal they made cover "*conditional upon*" a further survey programme and the satisfactory completion of all its requirements "*within timescales stipulated by underwriters*". Following a subsequent site visit in September, Fusion emailed JLT in October 2007 stipulating that the timescale for removal of LPG heaters was now "*immediate*". That email was never passed on by JLT to its principals.

Following the fire, insurers denied liability for the claim, on grounds of failure to comply with the risk improvement stipulation. That claim was settled, at 70% of the claim value, upon leading counsel's advice. GGL then sought to pursue the balance of the loss from its brokers, JLT.

Initially, JLT sought to argue that it was not in breach of its duty as a broker, or, if it was, that the said breach was not causative. GGL was already aware of the existing concerns about the use of LPG heaters, and the escalation of those concerns into a formal survey condition was not something that was unusual or onerous, needing to be drawn specifically to the attention of the insureds. Even if they had passed on those requirements, argued JLT, the evidence was that

31 [2011] EWHC 124 (Comm)

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the insured would have done nothing about it, since the insured had taken no effective steps in response to the previously expressed concerns.

On breach of duty, the court rejected JLT's defence. The formal imposition of the required risk improvement measures had a "*material and potentially deleterious effect on the insurance cover*" and as such should have been drawn specifically to the attention of the insureds. As to causation, the court was satisfied on the evidence that appropriate steps would have been taken by GGL in response to the news that coverage under the policy was actually in jeopardy. While this might not have entailed immediate removal of the heaters, it could be expected that by February 2008, when the fire occurred, the LPG heaters would have been removed or at least a dialogue would have been opened with the insurers leading to a mutually satisfactory solution to the problem.

In the alternative, JLT pursued a further defence to the claim. Their breach was causative of the insured's loss, they argued, only if it could be shown that Fusion actually had a defence to the policy claim, or a reasonably arguable defence, based upon breach of the survey condition. This was not so here, they said. The policy requirement lacked the quality of a true condition precedent to coverage or warranty, and the question then arose as to whether the use of LPG heaters by tenants was with the informed acquiescence of the insured, GGL. While the policy imposed a "reasonable care" obligation upon GGL, they had been advised by their own leading counsel that this called for recklessness by GGL, which was unlikely to be proved.

The court declined to rule on the issue of policy liability, though it considered it strongly arguable that the policy claim against Fusion would ultimately have succeeded had it been pursued. Clearly, said the court, brokers should not be prejudiced where their principals had compromised the policy claim simply out of a commercial desire to reach an early settlement, or on the basis of a "*spurious construction of the cover*". In this case, however, it was at least arguable that the continued presence of LPG heaters would have afforded a defence to the policy claim. On this the judge applied the test set out in the leading academic text[32] by asking whether, as a result of the broker's breach, the insured found itself:

> "...with doubtful or uncertain rights against insurers when [they] should have had a clear and unequivocal right to indemnity for [the] loss."

In the court's view that was precisely the case here. Consequently, the settlement entered into, at 70% of the claim value, was within the range of reasonable commercial settlements of this claim[33], and GGL were entitled to recover the shortfall from their brokers, JLT.

Unicover - New Jersey Appellate Court decides

***Reliastar Life Insurance Company v Smith and Aon Re Inc* [2011][34]**
Superior Court of New Jersey, Appellate Division, 1 March 2011

The collapse of the Unicover Pool has generated more than a decade of litigation and arbitration on both sides of the Atlantic. This most recent litigation was concerned with claims by pool members against their brokers.

Background

In the mid 1990's, Unicover Managers Inc. (Unicover) brought together a group of insurance companies (the Pool) for the purpose of selling workers' compensation reinsurance. The Pool focused in particular on so-called "carve out" business, namely the accident and health portion of workers' compensation, and was heavily supported by the life insurance market, until its spectacular collapse in 1999.

32 *Jackson & Powell on Professional Liability* 6th ed.; pages 16-138
33 *BP Plc v AON Ltd* (No. 2) [2006] 1 CLC 881
34 (2011) No. A-4484-08T2, New Jersey Superior Court Appellate Division

In its role as manager of the Pool, Unicover appointed Aon Re Inc (Aon) to act as its broker. Aon was also responsible for organising retrocessional coverage to protect the Pool's underwritten obligations. Mr Roger Smith was Aon's representative in dealing with Unicover. On 1 March 1998, Reliastar Life Insurance Company (Reliastar) joined the Pool as a 5% member, following an approach from Smith. Reliastar contended that it had done so against an expectation that adequate retrocessional protection would be provided.

Over the next 12 months, the Pool experienced dramatic growth and placed reinsurance far in excess of the amounts that were originally estimated to retrocessionaires. In consequence, a number of the retrocessionaires alleged misrepresentation and non-disclosures and they initiated corresponding arbitration proceedings. The arbitral panel held that the retrocession was valid, and it denied rescission. However, for reasons that it did not express, the tribunal went on to hold that any reinsurance sold by the Pool after 31 August 1998 was not covered by the retrocession, leaving members of the Pool seriously exposed.

Reliastar action against Aon

In May 2003, Reliastar commenced proceedings against Aon and Smith, claiming damages of $40m for (1) breach of fiduciary duty (by selling too much reinsurance and thereby jeopardising the Pool's retrocessional protection); and (2) aiding and abetting Unicover's breach of fiduciary duty.

Reliastar also alleged that the defendants had failed adequately to bring to the attention of the members of the Pool that the retrocessionaires were already complaining about the account and had commenced arbitration proceedings.

In March 2009, a jury returned a verdict that Aon and Smith had neither breached their fiduciary duty owed to Reliastar nor aided and abetted Unicover in any improper activity.

Appellate Court decision

Reliastar appealed the decision on the basis that the trial judge had misdirected the jury and wrongly excluded three pieces of evidence, including the original arbitration ruling. The New Jersey Superior Court Appellate Division ruled that the trial judge had not misdirected the jury and that his decision to exclude the evidence fell within his discretion. In any event, the bare arbitral decision offered no assistance in determining whether Aon or Smith were at actionable fault, since the tribunal was not concerned with wrongdoing by either, and had expressed no conclusion on the matter. On the contrary, the Appellate Court considered Reliastar's attempt to introduce the arbitral award in evidence was "*plainly a bootstrap approach that sought to implicate Aon and Smith for causing events that they were not accused of causing*" (namely, the shortening of the retrocession's term). The court added:

> “[n]ot only was the naked arbitral award of highly suspect relevance, its capacity to mislead the trier of fact was manifest. Aon and Smith ran the unwarranted risk of having imputed to them guilt by association if the arbitration panel's actual award were made part of the trial record.”

Accordingly, the Appellate Court upheld the decision of the trial court, finding in favour of Aon and Smith.

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Procedure

Litigation privilege over survey reports The "dominant purpose" test

Axa Seguros SA v Allianz Insurance Plc & Ors [2011][35]
Commercial Court, 2 March 2011

This was a case concerning an assertion of privilege over an engineering report commissioned in the course of investigations into a claim for hurricane damage sustained to an insured highway in Mexico.

It is settled law that a party seeking to assert litigation privilege over such a document must satisfy two conditions:

1. that at the time the document in question was created, litigation was reasonably in prospect, and not a mere possibility; and
2. that the document had been made with the sole or, at least, the dominant purpose of using it to obtain advice about the actual or anticipated litigation.

The Claimant in this case (Axa) was a Mexican-based property insurer that had agreed to insure against physical loss and damage to the "Road Toll Concession", a network of 38 roads in Mexico, managed under the responsibility of the entity *Nacional de Obras y Servicios* (Banobras).

The risk was reinsured with the London market Defendants on a facultative basis, under a reinsurance contract that restricted cover to roads "*constructed to internationally acceptable standards*". The reinsurance also stipulated that:

> "within a reasonable time from inception [of the reinsurance] ... Surveys are to be carried out ... to confirm the acceptability of the quality and construction and maintenance of Roads, Bridges and Structures and to verify the valuation of the Insured Property..."

A survey report was duly provided to reinsurers some months after inception, but they considered it to be insufficiently detailed to offer any assurance about the quality of the property. Accordingly, they responded by endorsing the reinsurance policy with immediate effect "*to include a 'Reverse Burden of Proof' Clause*".

Two months later, Hurricane Juliette struck the Pacific coast of Mexico, causing considerable damage to the Don Nogales Highway, one of the 38 insured roads. Initially, loss adjusters, Cunningham Lindsey, were appointed on behalf of both Axa and reinsurers, and their reports were made available to both. Subsequently, however, reinsurers also appointed engineering surveyors, Halcrow, who undertook their first inspection of the road four months after the storm.

The underlying policy claim was pursued by Banobras by means of arbitration in Mexico, leading to a final quantified award against Axa in early 2003. Axa, in turn, sought indemnity under the reinsurance in the present English action. Reinsurers denied liability, on the grounds that the Don Nogales Highway was not of "*internationally acceptable standard*" and/or that the cause of loss was "*inherent vice and/or wear and tear and/or gradual deterioration* [etc]".

In the course of the litigation, Axa sought disclosure by reinsurers of all reports rendered to them by Halcrow, which the latter refused to provide, contending that they were privileged from production.

35 EWHC 268 (Comm)

In considering whether the tests for privilege were satisfied, the court analysed in detail the developing dispute between Axa and its reinsurers, and in particular as recorded in a succession of Cunningham Lindsey reports over the months in question. Even when Halcrow were first appointed, it was noted that their involvement was, at least in part, to comment upon whether the road was of an international standard. In subsequent reports, Cunningham observed that reinsurers had issued a reservation of rights, and that coverage under the reinsurance contract was in doubt.

Although close to the borderline, the court accepted that these documents revealed a reasonable expectation of litigation between Axa and the reinsurers, as at the time when Halcrow were appointed. The situation had already developed beyond merely a "*distinct possibility that sooner or later someone might make a claim*".[36] Since cover was only available in respect of roads constructed to internationally acceptable standards, there was a reasonable prospect that Halcrow's reports would reveal this not to be so, and that this was why Axa had failed to produce proper survey reports prior to the loss. Even if Halcrow's reports left the position unclear, this still produced a reasonable prospect of litigation because, on the reinsurers' case, the burden of proof lay with Axa.

However, the court found that reinsurers had failed to satisfy the second privilege test. While litigation between Axa and reinsurers might have been within reasonable contemplation, it could not be said that Halcrow were instructed for the "*dominant purpose*" of the said litigation. Rather, this was one of a dual purpose, the other being to determine how far the damage had been caused by the hurricane and to verify the insured's quantum figures for remedial work. The issues were of equal importance, or at least neither predominated. Moreover, the court was not satisfied that the reports could be separated into two distinct parts, each wholly or predominantly attributable to a separate purpose. Accordingly, reinsurers' claim for privilege failed.

Finally, the court also noted that reinsurers had gone on to appoint the same Halcrow as their expert witness in the litigation itself. This created an inevitable tension between the reinsurers' claim for privilege, on the one hand, and Halcrow's duties as an expert witness on the other, since an appointed expert is obliged to act independently of the party appointing it, and to offer to the court all information known to it which is inconsistent with any expression of expert opinion. Halcrow would therefore be bound to disclose its earlier reports if and in so far as they were relevant to their expert opinion, and particularly if they were unhelpful to the reinsurers' case. Consequently, even if the court had found in favour of reinsurers on their privilege claim, the substance of that finding would likely have gone on to be overridden by virtue of Halcrow's expert appointment.

Enforcement of a settlement agreement

***Starlight Shipping Company v Allianz Marine and Aviation Versicherungs AG* [2011][37]**
Commercial Court, 19 December 2011

The Claimant in this case (Starlight) were formerly owners of the vessel ALEXANDROS T, which sank off the coast of South Africa in May 2006, with the loss of many lives. In August of that year, they commenced proceedings for the loss against their Lloyd's and company market insurers, who denied the claim, alleging amongst other things that the vessel was unseaworthy with the assured's knowledge[38].

The dispute was hard fought, and particularly notable for the way in which insurers were alleged to have procured evidence in support of their unseaworthiness case. In correspondence issued by Starlight's then lawyers they alleged "serious misconduct" by at least one of the insurers, and accused insurers of "*behaving in a reckless and irresponsible fashion in making ... an allegation*

36 *USA v Philip Morris Inc* [2004] 1 CLC 811

37 [2011] EWHC 3381 (Comm)

38 Unseaworthiness with the privity of the assured, to which see s 39(5) Marine Insurance act 1906

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when they have no evidence to substantiate what they allege". At a hearing shortly before trial of the action, the allegations were developed further, in the form of a witness statement from Starlight's lawyer, in which he accused insurers of having paid members of the crew to give false evidence in support of unseaworthiness.

At the same time, Starlight sought to amend its pleaded case to claim, in addition to the insured loss, consequential losses over and beyond the measure of indemnity to which it was entitled under the policy. It was Starlight's case that, had the Defendants complied with their obligations to indemnify in accordance with the terms of the policy, it would have been possible to purchase a replacement vessel. Starlight had thus lost around US$45m by way of increased capital cost, together with chartering losses in excess of US$31m. The court declined the application to amend, noting that there can be no claim for such losses beyond the measure of the contractual indemnity, as a matter of English law.[39]

Shortly before the trial was due to start, the Lloyd's market insurers entered into a settlement of the litigation, followed soon after by the company market insurers. Upon the payment of a compromise sum, the parties agreed to resolve the dispute "*in full and final settlement of all and any claims* [the assured] *may have under Policy No … against the Underwriters in relation to the loss of Alexandros T…*" As part of the settlement, the assured also agreed "*to Indemnify each Underwriter against any claim that might be brought against it by any of the Assureds or the Claimant's associated companies or organisations … in relation to the Alexandros T…*" The agreement with the company market was expressly subject to "*exclusive*" English jurisdiction, whereas that concluded with the Lloyd's market was simply stated to be "*subject to English law and the jurisdiction of the High Court of London*".

The settlement agreement was scheduled to a court order in a form known as a "Tomlin Order", under the provisions of which the parties agreed to stay the litigation, save for the purposes of carrying into effect the terms of the settlement. The effect is to transform the settlement agreement into an order of the court.

There matters rested until some three years later, when Starlight and it co-assureds commenced fresh proceedings against insurers in the Greek courts. In those proceedings, the Claimant pursued a claim for loss of hire and loss of opportunity, in essence consequential losses in the same or similar form to those previously declined by the English court.

Insurers responded in two ways. On the one hand, they sought to invoke the Tomlin Order in the original English proceedings. This recorded a full and final settlement of the dispute, and furthermore an indemnity from Starlight to insurers in relation to any fresh proceedings that might be brought. On the other hand, and without prejudice to their right to relief under the Tomlin Order, they initiated new English proceedings for like relief and damages for breach of the exclusive jurisdiction clause. The English court was required to consider a number of issues, including the following:

1. Starlight submitted that the Greek proceedings were not "*in relation to the loss of the Alexandros T*" or "*under*" the policies, and therefore fell outside the ambit of the previous settlement agreements; rather these were claims for bad faith brought under the Greek Criminal Code, covering perjury and the like, and should be treated as akin to "fraud". A settlement agreement that was intended to exclude such claims would, they said, have to be very clear in its intent[40].

   The court rejected this argument. The so-called "fraud exemption" in *Satyam* applied only to claims unknown at the time of the settlement, whereas in this case Starlight not only knew of the claims it was now asserting but had attempted (unsuccessfully) to introduce them to the English action three years earlier.

39 Applying the principle in *The Italia Express No 2* [1992] 2 Lloyd's Rep 281 and *Sprung v Royal Insurance UK Ltd* [1992] 1 Lloyd's I & R Rep 111 CA. The position is otherwise under the law of many other jurisdictions, including, for example, Scotland

40 Applying the principle in *Satyam Computer Services v Upaid Systems* [2008] EWCA Civ 487

The Greek claims all related to the investigations by the insurers (whether in bad faith or otherwise), and to the way in which those investigations had been carried out (whether or not maliciously). As such, they were clearly all claims "*in relation to the loss*", and in any event were covered by the release in so far as it discharged "*any claims* [the assured] *may have under*" the Policy.

2. Having determined that the subject matter of the Greek claims fell within the settlement release, the court held that it was also a breach of those agreements for Starlight to bring the said claims by way of litigation in Greece, since the parties had agreed in the settlements to exclusive *English* jurisdiction. This was expressly so in the case of the company market settlement, but also held to be so in the case of the Lloyd's market agreement even though the word "exclusive" was not used. On this, the judge's conclusions were put this way:

> “In the absence of any argument that the word exclusive was for some reason… deliberately left out, I am satisfied both by reference to the context and to the fact that the provision would otherwise be idle, that the parties did mean to and intend exclusive jurisdiction.”

3. It was not necessary for the insurers to rely upon fresh English proceedings to enforce the settlement agreement, so the court held, since the Tomlin Order in the original proceedings gave the court jurisdiction to order the relief sought by the insurers, including their claim for damages for breach of the English jurisdiction clause, and an indemnity as provided for under the settlement agreements. As to the latter, the court also ordered "fortification" of the indemnity in the form of a fund to meet future losses caused to insurers by Starlight's continued pursuit of the Greek proceedings, in breach of the settlement agreements.

Expert independence

Meat Corporation of Namibia Ltd v Dawn Meats (UK) Ltd **[2011][41]**
Chancery division, 7 March 2011

The Claimant in these proceedings sought a direction refusing the Defendant permission to call a chosen expert witness, on the grounds that the proposed expert lacked independence. In the past, both parties had approached the expert with a view to instructing her, in the course of which the expert had been in receipt of information about the dispute from the Claimant. Alternatively, the Claimant also objected on the ground that the expert acted as a consultant for the Defendant, putting her in a position of conflict.

The judge refused the application. On the first question, it was common ground that the expert had received privileged and confidential information from the Claimant when she was originally approached. In some cases this would be sufficient to disqualify. The judge cited the House of Lords decision in *Prince Jefri Bolkiah v KPMG* [1999][42] concerning accountants who provided litigation support services. It was held that they must be treated in the same way as solicitors, and therefore could not go on to act for the other side. However, in that case the accountants had actually been *engaged*, rather than merely approached by the opponent. The judge held in any case that the full rigours of the test that would apply to solicitors (and which might readily be applied to litigation support accountants providing a service akin to that of a solicitor) were inapplicable to a third party expert such as in the present case.

As to the second question, the judge applied the principles in *Armchair Passenger Transport Ltd v Helical Bar Plc* [2003],[43] namely that an expert is not disqualified from so acting merely because they have an interest, "*whether as an employee or otherwise*". It was the true nature and extent of the interest that mattered, and in this case the consultancy was an entirely separate activity.

41 [2011] EWHC 474 (Ch)
42 [1999] AC 222
43 [2003] EWHC 367

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Negligence of expert witnesses

Jones v Kaney [2011][44]
Supreme Court, 30 March 2011

This was a majority decision of the Supreme Court, reversing the previous immunity that expert witnesses enjoyed from negligence claims relating to their evidence.

The Respondent was a clinical physiologist appointed by the Appellant to assist with a claim arising from a road traffic accident. The Respondent signed a joint statement of experts that was harmful to the Appellant's case, but later admitted that she had done so only because she felt under pressure. The district judge would not allow the Appellant thereafter to change experts, leaving him with little option but to settle on terms less advantageous than otherwise would have been the case.

The Appellant brought proceedings against the Respondent expert, for damages on account of the latter's allegedly negligent performance as an expert witness. The trial judge declined to award damages, holding that he was bound by the existing principle by which experts enjoy immunity in such cases, as confirmed in *Stanton v Callaghan* [2000].[45] The reason for immunity, as confirmed by the Court of Appeal in that case, was the need to "*avoid the tension between a desire to assist the court and fear of the consequences of a departure from advice*" given by the expert. In short, the independence of experts may be impaired if they feared being sued for giving their evidence with candour.

Nevertheless, the trial judge accepted that the question of expert immunity was of sufficient importance to justify an order for direct appeal to the Supreme Court, and on 30 March 2011, the Supreme Court gave its decision. By a 5:2 majority, the Supreme Court abolished the principle of expert immunity, citing the following main reasons for doing so:

1. the previous immunity from negligence claims enjoyed by advocates had already been swept away in *Arthur Hall & Co v Simons* [2002].[46] Although that case maintained a distinction between advocates and expert witnesses, this distinction was no longer sustainable, since in reality the expert witness has much more in common with the advocate than with factual witnesses, the latter of whom remained immune; and

2. there was no real reason to suppose that a lack of immunity would discourage experts from providing their services as witnesses. The courts would be alive to the possibility of specious claims against experts by disappointed litigants, and would "*stamp vigorously*" on any practice of pressurising experts to provide the evidence preferred by those appointing them.

Late amendments to statements of case

Swain-Mason & Ors v Mills & Reeve [2011][47]
Court of Appeal, 20 January 2011

These proceedings concerned a negligence claim by the Claimant against the Defendants, its former solicitors, in particular relating to tax advice associated with a management buy-out transaction.

The proceedings were commenced in January 2009, and came to trial over a year later. At the beginning of the trial, the Claimant successfully applied for an amendment to its pleadings, materially changing the case faced by the Defendant. In allowing the application, the judge had relied upon the decision in *Cobbold v Greenwich LBC* [1999][48] to the effect that amendments

44 [2011] UKSC 13
45 [2000] QB 75
46 [2002] 1 AC 615
47 [2011] EWCA Civ 14
48 [1999] EWCA Civ 2074

generally ought to be allowed so that the real dispute between the parties can be adjudicated upon, provided that any prejudice to the other party can be compensated for in costs, and the public interest in the administration of justice is not significantly harmed.

The Defendant appealed. Allowing the appeal, the Court of Appeal held that the trial judge had misdirected himself. In recent years, and in particular since the introduction of the Civil Procedure Rules in 2000, the court noted that the emphasis had changed with regard to late amendments to statements of case. The approach in *Cobbold* had given way to one which "*paid greater regard to all the circumstances which are now summed up in the overriding objective* [in the CPR]". The Court of Appeal cited with approval the following passage in *Worldwide Corporation v GPT* [1998][49] as follows:

> “in previous years it was more readily assumed that if the amending party paid his opponent the costs of an adjournment that was sufficient compensation to that opponent. In the modern era it is more readily recognised that in truth the payment of the costs of an adjournment may well not adequately compensate someone who is desirous of being rid of a piece of litigation which has been hanging over his head for some time, and may not adequately compensate him for being totally (and we are afraid there are no better words for it) "mucked about" at the last moment…”

The Court of Appeal also added that the amendments in question were in any case unsatisfactory, being compressed, "*difficult to work out*" and "*not in proper form*". Accordingly, the matter was ordered to proceed to substantive trial on the basis of the pleaded case at it previously stood.

Law and Jurisdiction

West Tankers: The final twist

***Allianz SpA & Ors v West Tankers Inc* [2011][50]**
Commercial Court, 6 April 2011

Anti-suit injunctions are a commonly used tool in re/insurance litigation. The paradigm example sees a London re/insurer sued by an insured or reinsured in the courts of the latter’s home jurisdiction, in defiance of an exclusive English jurisdiction clause, to which the re/insurer will respond with an application for an injunction from the English court. Where foreign litigation is still pursued in defiance of such an injunction, any resulting judgment will be unenforceable in England, either because the foreign court lacked jurisdiction (in the eyes of English law) or because enforcement would be contrary to public policy, or both.

The legal effect of the anti-suit injunction is frequently misunderstood; the order is intended to injunct the litigant, not the foreign court. Nevertheless, anti-suit injunctions are often viewed with suspicion by foreign courts, who consider them an improper invasion into their domain by the English court. Some jurisdictions, most notably France, have never granted anti-suit relief.

Within Europe in particular, the anti-suit injunction has increasingly been seen as an affront to the idea that the courts of each European state are equally well-equipped to apply what have become largely harmonised rules on the allocation of jurisdiction between them. Consequently, under the terms of EU Regulation 44/2001, the courts of member states of the European Union are now prohibited from issuing injunctions to restrain proceedings already commenced in the courts of another member state. In the case of *Gasser GmbH v MISAT Srl* [2003],[51] the European Court of Justice held that this would be true even where a litigant had deliberately (i.e. in bad faith) issued proceedings in a member state court other than that stipulated in the

49 [1998] EWCA Civ 1894
50 [2011] EWHC 829 (Comm)
51 [2003] EUECJ C-116/02

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contract (*Turner v Grovit* [2004]).[52] It is up to the court first seized, alone, to decide upon the matter of jurisdiction.

What remained unclear until relatively recently was the position of arbitration clauses, because arbitration is excluded from the scope of the Regulation. Could an English court still issue an injunction restraining a party from pursuing a claim in (say) Italy, in defiance of a contractual provision referring the matter to arbitration in England?

That issue came up for consideration in *Allianz SpA & Ors v West Tankers Inc* [2007][53] concerning claims arising from an allision involving the vessel FRONT CONNOR and a jetty at an oil refinery in Syracuse, Italy, operated by Erg Petroli SpA. Erg's claim against Owners for the resulting loss and damage arose under a charterparty which provided for London arbitration, and consequently Erg duly commenced the said arbitration against Owners. In the meantime, however, Erg was indemnified by its own insurers, Allianz and others (Insurers), who launched their own recovery proceedings against Owners in the Italian courts. The result was that the same claim was being pursued in two separate venues, by Erg in the London arbitration and by its subrogated insurers in the Italian court.

In response, Owners issued an application in the English court for an injunction to restrain the Italian litigation. The English court considered itself competent to grant such an injunction, but the House of Lords referred the matter for determination by the European Court of Justice, which went on to hold otherwise. Under the ECJ's ruling handed down in February 2009,[54] it was held that only the court first seized of the matter (in this case the Italian court) could decide on the proper allocation of jurisdiction under the Regulation. The English court, therefore, could not issue an anti-suit injunction in support of an English arbitration.

The decision was not without its critics in the commercial world, and particularly in the insurance industry. To English eyes, an agreement to arbitrate is sacrosanct and it should enjoy the full protection and support of the court, including where necessary injunctive relief against any competing court proceedings. There was also a fear, articulated expressly by the House of Lords, that without the facility to protect arbitration in this way, the EU member states would become unattractive places in which to arbitrate; there was, noted Lord Steyn, no shortage of competitor jurisdictions willing to support arbitration more aggressively, notably New York, Bermuda and Singapore.

In the meantime, the *West Tankers* case itself progressed to the next stage. In the absence of an injunction, both sets of proceedings continued in parallel; Erg continued to pursue its London arbitration, while Insurers persisted with their Italian litigation, each refusing to accept the jurisdiction of the other's process.

In due course, the London arbitration tribunal issued its award, holding that Owners were not liable to Erg and its insurers for the incident. So where did that leave matters? While Owners had won in the London arbitration, the Italian litigation could yet produce a contrary judgment, which in the ordinary course would be enforceable in another EU member state (i.e. England) under the Regulation. Could the Owners use the arbitration award as a shield against enforcement of an adverse Italian judgment, despite the lack of any anti-suit injunction?

The answer was sought in the Regulation itself, which bars enforcement of a judgment of another member state court which is irreconcilable with an earlier judgment given by the court in which enforcement is sought. The problem in this case was that an English arbitration award is not the same as an English court judgment, and so the award on its own would not have that effect. In the present case, however, Owners applied to the English court to convert the arbitration award into an English court judgment pursuant to section 66 Arbitration Act 1996, an application upon which the English Commercial Court gave its decision on 6 April 2011. While the court made it clear that it would not grant such relief in all cases, it said it would do so in cases where (as here) there existed an appreciable risk of the losing party obtaining an inconsistent

52 [2004] EUECJ C-159/02

53 [2007] UKHL 4

54 [2009] EUECJ C-185/07

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judgment in a member state which it might then seek to enforce in England. Moreover, such relief was available even where (as here) the arbitration award was purely declaratory in nature. Absent such relief, so the court noted, the winning party would be deprived of the material benefit of the arbitration award.

In summary, while the Owners in this case famously lost the battle (of the anti-suit injunction) they may ultimately have won the war. Any adverse judgment of the Italian court is now unlikely to be enforceable against them in England, it being contrary to an existing English judgment. The important point in this case is that the arbitration came to a conclusion first; had the Italian proceedings been first to cross the line then the position would have been much more difficult. Nevertheless, the outcome assuages at least some of the concerns voiced following the ECJ's ruling in 2009, in that it helps to preserve the integrity of English arbitration against the threat of adverse foreign litigation, albeit only at the enforcement stage.

West Tankers in reverse
Injuncting foreign arbitrations

***Claxton Engineering Services Ltd v TXM Olaj-Es Gazkutato KFT* [2011][55]**
Commercial Court, 15 October 2011

The *West Tankers* case discussed above finally established that it is not now possible for an English court to issue an anti-suit injunction restraining court proceedings in another EU member state, in support of an agreement to refer the dispute to English arbitration. Rather, the party insisting upon the arbitration must apply to the relevant foreign court to stay or dismiss the competing litigation.

But what of the reverse situation? In this case, the parties had agreed to an exclusive English jurisdiction clause but the Defendant had nevertheless purported to commence arbitration in Hungary. The Claimant brought an application in the English court to injunct the foreign arbitration, to which the Defendant objected that this too was outside the power of the English court on the *West Tankers* reasoning. Were the English court to grant such an injunction, argued the Defendant, it would similarly be interfering with or usurping the supervisory functions of the Hungarian courts, contrary to Regulation 44/2001.

The judge rejected the Defendant's argument. While anti-suit injunctions had been found to be objectionable where they interfered with another EU court deciding on its own jurisdiction under the Regulation, that was not the case here, since all that was being injuncted was the pursuit of a foreign *arbitration*.

Having determined that he had the jurisdiction to grant the order sought, the English judge was then free to exercise his discretion in determining whether to do so. While recognising the need for caution in injuncting arbitrations outside the jurisdiction (which *could* be left to the relevant supervisory courts in the seat of the arbitration) the circumstances here were sufficiently exceptional to justify the order. The continuance of the Hungarian arbitration would be a clear breach of the Claimant's legal rights, namely the contractual right to insist upon English court jurisdiction. Moreover, there was not even an "*arguable case*" that the claimed arbitration agreement existed between the parties. As such, the Defendant's conduct in pursuing it would clearly be "*oppressive and vexatious*". The injunction was granted.

55 [2011] EWHC 345 (Comm)

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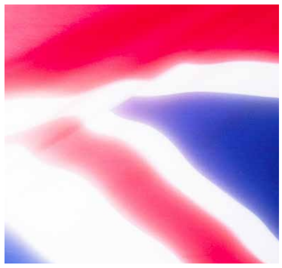
Choice of English law and the *forum conveniens* test



***Mujur Bakat BHD v Uni Asia General Insurance Berhad & Ors* [2011][56]**
Commercial Court, 18 March 2011

In launching proceedings in the English court against a party outside England, it is generally necessary for the Claimant to obtain the permission of the court to serve out of the jurisdiction. That application, by definition, must be brought before the proceedings are served on the Defendant, and hence only the Claimant is represented at that stage. However, once served, the Defendant has an opportunity to return to the court and to challenge the order for service out, seeking to have it set aside.

There are a number of alternative grounds upon which the Claimant may base an application for service out of the jurisdiction, and these are enumerated at Practice Direction 6B to Part 6 of the Civil Procedure Rules. Perhaps the most obvious ground is that the parties have expressly conferred jurisdiction upon the English court, by agreement in the policy. An English jurisdiction clause will have this effect. In some cases, however, the policy may fall short of an express choice of jurisdiction. It may, as was true in this case, identify English *law* as the governing law of the policy but fail to say anything at all about jurisdiction.

While a choice of English law constitutes one of the grounds for service out, the English courts have repeatedly made clear that a contractual choice of English law alone is not the same as a choice of English jurisdiction.[57] Consequently, an order for service out which is based purely upon a choice of English law is particularly susceptible to challenge by the Defendant. Upon hearing any such challenge, the court will need to consider whether England is clearly the most appropriate forum for the trial of the action, or whether in fact some other forum is more appropriate (the so-called "*forum conveniens*" test). This determination is a matter of the court's discretion, having considered the issues in the case, the location of the parties and other matters going to the practicality of the litigation, including for example the location of evidence and witnesses.

Where the dispute gives rise to some particularly difficult issues of English law, the court may well conclude that England is the appropriate forum. If it believes that the foreign court will fail to apply English law, or have doubts as to how it is to be interpreted, then it is clearly of benefit that the matter be heard in England. Where, however, the dispute is one about evidence, and that evidence is elsewhere than England, the argument in favour of English forum is much less compelling.

The present case concerned a claim by Malaysian shipowners under a hull and machinery policy issued by Malaysian insurers. The policy was expressed to be subject to the Institute Time Clauses Hulls 01/10/83, which contain a reference to "*English law and practice*" but say nothing about jurisdiction. Other than the English choice of law in the Institute Clauses, the contract and dispute had no connection whatsoever with England. The vessel, which was registered in Mongolia, had grounded at Maumere, Indonesia, whilst en route from East Timor to East Java. The policy was negotiated and signed in Malaysia, and premium designated in Malaysian Ringgits, while the documents and surveyor witnesses were all located in either Malaysia or Singapore.

Initially, it had been suggested that the defendant insurers might assert a right to avoid the policy for misrepresentation, namely that the vessel would be classed under Bureau Veritas within three months, which in fact was not done. The court agreed that this point raised difficult and perhaps "open" questions of English law, which alone would be enough to point to England as the most appropriate forum. However, in the course of the hearing, the Defendants confirmed that the misrepresentation point was abandoned, and they undertook not to pursue it in any foreign proceedings. Absent the misrepresentation issue, what remained were three legally straightforward points, concerning alleged breach of warranty in relation to the registration of

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56 [2011] EWHC 643 (Comm)

57 *Macsteel Commercial Holdings (Pty) Ltd v Thermasteel V (Canada) Inc* [1996] CLC 1403 (CA); *Sawyer v Atari Interactive Inc* [2005] EWHC 2351 (Ch); *Novus Aviation v Onur Air* [2009] 1 Lloyd's Rep 576

the vessel with the Mongolian registry, breach of warranty as to maintenance and management of the vessel,[58] and alleged failure to sue and labour.

Since none of these issues involved novel, complex or undecided points of English law, there was no reason to conclude that the Malaysian court would not properly apply English law to the matters in dispute. Consequently, the fact that English law was the governing law of the policy was held to be of relatively limited significance in the *forum conveniens* test.[59] Moreover, in so far as the issues in dispute called for evidence, none of that evidence was in England. The English court therefore set aside the order for service out of the jurisdiction, allowing the matter to proceed instead in the courts of Malaysia.

Finally, the Claimant also raised a discrete point going to the integrity of Malaysian justice. Although the parties could be confident that the English court would be impartial and free from suspicions of corruption, they argued that the same could not be said of the courts in Malaysia. These concerns were said to be based upon judicial comments reported in the *New Straits Times* in November 2008. The court noted, however, that the comments related to two retired judges, were not independently confirmed and, in any event, were counterbalanced by reported measures taken by the Malaysian Chief Justice that had, it was said, "*stopped corruption*". The court concluded that the article provided no justification to suggest that the parties would not receive a fair trial in Malaysia.

Dodging the triple trigger

***Faraday Reinsurance Co Ltd v Howden North America Inc & Anor* [2011][60]**
Commercial Court, 1 November 2011

Much has been written about the House of Lords' decision in *Wasa v Lexington* [2009].[61] Underlying the dispute in that case was the differing attitude between English law and that of many US states in relation to the indemnity trigger under occurrence based insurance. Under English law, insurers simply cannot be liable for loss, damage or injury actually occurring outside the period insured. In the context of mesothelioma claims, the relevant "occurrence" for these purposes is the moment when the claimant becomes fatally ill (*Bolton v Municipal Mutual* [2006][62]). By contrast, many US states look backwards through the prior period of exposure to the conditions that gave rise to the illness, and indeed forwards to the point when the relevant illness became manifest. What results is a continuous or "triple" trigger of liability, spanning multiple policy years. Moreover, many of those same states also impose a joint and several liability between the various policies impacted, with the result that the insured may sue any one of them for the full amount of the loss, even though the overall period of occurrence extends well beyond that insured.

Such an approach is entirely alien to English law, and naturally London market insurers and reinsurers will wish to do all they can to ensure that they do not fall victim to it. In *Wasa*, the solution was to be found at the reinsurance level; the reinsurance being an English law contract, London market reinsurers were held not liable to follow the decision of the US state court on the underlying claim, notwithstanding the existence of a follow clause.

More recently, the issue has arisen again, in the context of direct excess liability insurance in *Faraday Reinsurance v Howden North America* [2011]. In this case, the predecessor company of the Defendant (HNA) was a manufacturer of asbestos products, sued in the US under a mass tort claim by mesothelioma sufferers in 1999. By 2003, those claims had become the subject of coverage litigation in the Pennsylvania state court between HNA and its primary and first excess

58 Specifically, lack of compliance with the SOLAS (Safety of Life at Sea) Regulations and the MARPOL Convention (International Convention for the Prevention of Pollution from Ships)

59 *Navigators Insurance Co v Atlantic Methanol Production Co LLC* [2004] Lloyd's Rep IR 418 considered

60 [2011] EWHC 2837 (Comm)

61 [2009] UKHL 40

62 [2006] 1 WLR 1492

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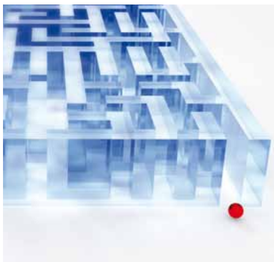

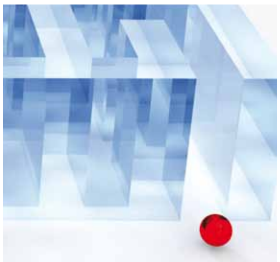

layer insurers for the 1998-1999 policy year (Year 1). The Claimant, Faraday, was one of the higher excess layer insurers in the Year 1 tower, and not among those sued at the time by HNA. Faraday also participated at a similar excess layer for the following years 1999-2000 (Year 2) and 2000-2001 (Year 3).

In 2005 the proceedings against the primary and first excess layers were settled, following which HNA turned its attention to higher excess layers. In 2009, it sued insurers subscribing to each of the excess layers in Year 1, up to but not including Faraday's layer. Some, but not all, of the defendant insurers to the 2009 action also went on to settle.

Finally, in August 2010, Faraday received from HNA a "*precautionary notice*", issued to all higher level excess insurers, advising them of an occurrence which "*may give rise to a claim*", such notice being intended to apply to each of Years 1-3. In response, Faraday issued English proceedings seeking a declaration that its policies were subject to English law and asking the court to determine how policy cover would operate, including as to the proper meaning of "injury" under English law.

Governing Law

The policies for Years 2 and 3 provided expressly for English law, whereas Year 1 was silent on applicable law. Applying the principles in the Rome Convention[63], the court needed to consider whether, in the absence of express choice in Year 1, the parties had nevertheless conveyed an implied choice of English law "*with reasonable certainty*". It held that they had. The mere fact that a policy was placed in the London market might not be sufficient of itself. In this case, however, the policy was on a London market underwriting slip, bearing London market clauses and abbreviations, and referring to London market institutions and features. All of this was consistent with an implied choice of English law.

Jurisdiction

Next, the court had to decide whether it should retain jurisdiction over the dispute. HNA argued that the court should stay the English proceedings because:

1. in relation to Year 1, coverage proceedings already existed in Pennsylvania, which litigation was long running and wide ranging. Pennsylvania was clearly the more appropriate forum; and

2. in relation to Years 2 and 3, Faraday's claim was purely hypothetical and should be dismissed, as no claim had in fact materialised under these years.

On Year 1, the court found for Faraday. The first major consideration was that the policy was (so the court had found) subject to English law, a factor weighing heavily in favour of its determination in the English court. Moreover, this was not a case where Faraday had been asked to participate in an overall programme covering multiple layers and multiple years; there was no joint underwriting decision taken by Faraday and its co-insurers, and hence no necessary commonality between Faraday and the insurers sued in Pennsylvania. Rather, Faraday's subscription was a matter of distinct contract between it and the insured, suitable for determination by the English court, independently of the wider proceedings going on elsewhere. While the Pennsylvania litigation may have been concerned with the underlying facts, what the English court was being asked to do was simply to determine matters of law and construction of the English law policy. There was no reason to suppose that the two sets of proceedings would yield inconsistent results.

As to Years 2 and 3, the English proceedings were not hypothetical at the time they were issued, so the court found. At that stage, Faraday was in receipt of notification of a circumstance which, it was said, "*may give rise to a claim*". In those circumstances, it was clearly legitimate for them to commence these proceedings for declaratory relief as to the basis upon which they could (or could not) be liable for such a claim, should it materialise. However, once the English proceedings had been served, HNA's solicitors wrote to Faraday confirming, in terms, that their client would *not* pursue a claim under Years 2 and 3. That, the court held, was enough to render the present

63 The Convention on the Law Applicable to Contractual Obligations, 1980. Now superseded by the Rome 1 Regulation

proceedings unnecessary, and accordingly the court set aside the order permitting service of the English proceedings on HNA in so far as concerns Years 2 and 3 only.

This case highlights the importance that insurers attach to the jurisdictional battle, particularly when presented with claims from jurisdictions that may take a starkly different coverage attitude to that under English law. In such cases, the pre-emptive strike for declaratory relief in the England court can be a valuable weapon.

Arbitration

Challenge to an arbitral award

***Ispat Industries Ltd v Western Bulk Pte Ltd* [2011][64]**
Commercial Court, 31 January 2011

This case concerned an application in the English Commercial Court brought by the Claimant charterers, challenging an arbitral award on the ground of "*serious irregularities*" and/or error of law.

As to irregularity, the main complaint was that the tribunal had failed to address the concerns raised by the one dissenting arbitrator regarding the reliability of the evidence of one of the Defendant's witnesses. That challenge was rejected. While it was true that the majority did not refer to the concerns, and while it might have assuaged the charterers' concerns had they done so, they were under no such obligation. A serious irregularity would arise upon the tribunal's failure to deal with an "*essential issue*", but this was not one of them. In particular, failure to set out a reason for rejecting an argument was not the same as the failure to deal with an issue at all.

As to alleged error of law, the Claimant's main complaint was concerned with "Rule B" attachment orders that had been obtained by the Owners against the charterers in the New York courts. The charterers contended that by pursuing such proceedings the Owners had put themselves in breach of the arbitration clause in the charterparty, requiring all disputes to be referred to London arbitration. Again, the complaint was rejected. The "Rule B" procedure available in certain US jurisdictions was simply a conservatory remedy for the preservation of assets, and was regularly invoked to support a substantive dispute by way of arbitration in London or elsewhere. Where the foreign proceedings went beyond the mere preservation of assets and strayed into a dispute on the merits of the claim[65] then they may well constitute a breach of the arbitration clause, but that was not the case here.

Arbitration time bar

***X v Y* [2011][66]**
Commercial Court, 9 February 2011

This case concerned a claim on a charterparty containing an arbitration clause requiring that that the arbitrator be appointed "*within 12 months of final discharge or termination of this Charterparty*".

The charterparty was for three consecutive voyages. In respect of the first, discharge was on 8 February 2008; discharge for the third and final voyage completed on 18 May 2008.

Applying the decision of the Court of Appeal in *The Simonburn* [1973],[67] the arbitrator concluded that "final discharge" in a consecutive voyage meant final discharge of the cargo

64 [2011] EWHC 93 (Comm)
65 As in *The Kallang No.2* [2009] 1 Lloyd's Reports 124
66 [2011] EWHC 152 (Comm)
67 [1973] 1 Lloyd's Law Rep 392

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on the particular voyage in respect of which the claim arose (in this case, the first voyage). As for "*termination of the charter party*", however, he held that this meant termination of the charterparty at the end of the third voyage. On that latter basis, the present arbitration, commenced on 23 February 2009, was within time.

The Commercial Court agreed with this approach. There was no "*black hole*", as the Claimant contended; there was no need to insert the words "*whichever is the sooner*" or indeed "*whichever the later*", but rather either date could be used as the relevant start point. Consequently, the reference to arbitration, on 23 February 2009, was valid.

Time bar to the claim, not merely the remedy

***Nanjing Tianshun Ltd v Orchard Tankers* [2011][68]**
Commercial Court, 11 February 2011

This case concerned a dispute under a shipbuilding contract, persuant to which the buyer enjoyed certain prescribed rights to terminate or cancel the contract. Under paragraph 2 of the contract, the seller was, however, entitled to dispute the buyer's cancellation by way of arbitration "*if such institution of arbitration is made within thirty (30) days of the Buyer's cancellation…*".

The contract also contained a residual law and jurisdiction provision as follows:

> "In the event that any dispute shall arise out of this CONTRACT between the SELLER and the BUYER, which dispute is not otherwise governed by Paragraph 1 or 2 of this Article, such dispute shall be resolved in and subject to the jurisdiction of England and the courts in London, England…"

The seller sought to dispute the buyer's cancellation, but outside the 30 day period, in response to which the buyer contended that the seller's right to bring such a claim was time barred.

The seller agued that the 30 day period applied only to proceedings brought by way of *arbitration*. Upon expiry of the 30 day period, so the seller contended, the right to an arbitration procedure was lost but the claim could still be pursued by way of court proceedings in the normal way, at any time up to expiry of the six year statutory limitation period.

The court rejected that argument. It said there would be no commercial purpose in granting the seller an option either to institute a private arbitration within 30 days or, alternatively, "*whether by choice or indolence, to be able to institute public litigation after 30 days but within 6 years*". The court referred to a passage in the leading academic text, Mustill & Boyd, *The Law and Practice of Commercial Arbitration*, to the effect that the court should lean in favour of construing such clauses as "claim barring" rather than merely "remedy barring", and held that this was precisely the effect in the present case. Consequently, the expiry of the 30 day period extinguished the seller's right to pursue a claim in respect of cancellation, rather than merely the remedy of pursuing such a claim by way of arbitration.

68 [2011] EWHC 164 (Comm)

Application to remove arbitrator - English Commercial Court

A & Ors v B & Anor [2011][69]
Commercial Court, 15 September 2011

The underlying dispute in this case was subject to LCIA arbitration, in which the parties had jointly agreed to the appointment of a Queen's Counsel to sit as sole arbitrator. Two years later, the arbitrator informed the Claimant that he was in fact acting as an advocate for the Defendant's solicitors (but not for the Defendant) in a separate matter proceeding by way of Commercial Court litigation. Those proceedings had predated the arbitration by many years, and had for some time been in abeyance subject to a stay, but latterly came to be resurrected, prompting the arbitrator to bring the position to the attention of the parties.

The Claimant applied under section 24 of the Arbitration Act 1996 for removal of the arbitrator on the grounds of "*justifiable doubts as to his impartiality*". The challenge was unsuccessful. Where an arbitrator had an "*actual predisposition*" towards a particular firm of solicitors, and was wishing to foster a relationship with it then the court confirmed that this would constitute actual bias. In other cases, an arbitrator/barrister might receive a substantial proportion (perhaps 60%) of his instructions from one of the firms involved. In such cases there might be a "*real possibility of apparent bias*", even though no actual bias.

However, the present scenario fell into neither of these categories. In fact, the Commercial Court litigation was only the second set of instructions that the arbitrator had received from the Defendant's solicitors. For the same reason, the judge also rejected the alternative argument that the arbitrator's delay in disclosing his involvement in the litigation was itself a "serious irregularity" within the meaning of section 68 of the Arbitration Act 1996.

Application to remove counsel – US Federal Court

Northwestern National Insurance Company v Insco Ltd (2011)[70]
United States District Court, SDNY, 3 October 2011

This much discussed case considered what is and what is not appropriate when dealing with evidence in support of alleged arbitrator bias in a US reinsurance arbitration. The key issues that the New York federal court had to consider were: (1) whether it is proper for the *courts* rather than the tribunal to deal with disqualification of a party's law firm; and (2) whether disqualification is the appropriate remedy in circumstances where a law firm obtains copies of communications between panel members that relate to the alleged bias.

Dealing with these questions in turn, the Court of the Southern District of New York found that:

1. lawyer disqualification is a matter for the courts and not arbitrators. Arbitrators are selected for their expertise in a particular industry and "*cannot be expected to be familiar with the standards of conduct applicable in the legal profession*"; and

2. lawyer disqualification is appropriate in circumstances where private emails between members of an arbitration panel are obtained by lawyers representing a party in an ongoing arbitration and the lawyer fails to disclose those emails. This was considered to be a serious breach of the New York rules of Professional Conduct and, in particular, a serious breach of ethical conduct.

69 [2011] EWHC 2345
70 No. 11 Civ. 1124 (SAS) 2011 WL 4552997 (S.D.N.Y. Oct. 3, 2011)

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The Plaintiff reinsured (NNIC) commenced arbitration against the Defendant reinsurer (Insco) for amounts owed under a contract of reinsurance. Pursuant to the arbitration agreement, a panel was appointed consisting of two party appointed arbitrators and a neutral umpire. Following suggestions made to Insco by its own arbitrator, Insco became concerned that his counterpart was biased, and accordingly they challenged the impartiality of NNIC's appointed arbitrator, alleging an improperly close relationship between the arbitrator and NNIC's lawyers.

Insco wrote to the panel and to NNIC demanding that all of the arbitrators resign immediately because of "*evident impartiality*". Insco's own arbitrator promptly resigned (although the other panel members did not) and shortly afterwards he disclosed some 130 private intra-panel emails to Insco's lawyers. That he had done so became clear to all parties when Insco's lawyers went on to refer to some of those emails in the course of a court application for disqualification of NNIC's arbitrator.

This prompted NNIC to demand production of all disclosed emails, which were then passed directly for review to outside counsel appointed by NNIC, so that NNIC's lawyers did not personally review them.

NNIC and their outside lawyers were most concerned by what they found in that review. They contended that many of the emails disclosed to Insco by their arbitrator related to issues that were still pending in the arbitration and, moreover, that when they came to be exhibited in the court application, Insco's lawyers had deliberately changed their appearance. The tribunal ordered that while the "*release...of intra-panel communications was highly inappropriate...this panel will continue to decide the case on the facts and evidence presented*". It ordered that all copies of confidential communications be destroyed within ten days, but otherwise refused to consider further the matter of the leaked documents.

In light of this decision, NNIC brought a motion before the court to disqualify Insco's lawyers from representing them in the arbitration proceedings, due to their conduct in obtaining the private panel emails and, in part, failing to disclose that fact. Insco's lawyers opposed the motion by asserting that the emails obtained by the Defendant did not bear upon the merits of the arbitration.

The court granted the Plaintiff's motion and made the following observations:

1. The possible disqualification of a lawyer is an issue for the court to determine and is not within the capabilities of arbitrators, who are selected for an arbitration primarily based on their expertise in a particular industry. Arbitrators cannot be expected to be familiar with the standards of conduct applicable to the legal profession. In any event, so the court noted, the panel had explicitly refused to deal with this issue, leaving it for the court to do so. It would therefore have been manifestly unfair for the court to refuse to at least consider NNIC's motion to disqualify Insco's lawyers.

2. The conduct of the Defendant's lawyers "*constituted a serious violation of arbitral guidelines, as well as ethical rules*", and was an abuse of the New York State Rules of Professional Conduct.

The court entirely rejected Insco's attempt to justify its actions by arguing that the emails were obtained legitimately as they were for the purpose of proving arbitrator impartiality. The court stated that "*a party is never allowed to probe the decision-making process of an arbitration panel to prove bias, except in the most egregious of cases*" and that it was "*inappropriate for Insco to obtain panel deliberations before the close of the arbitration, and in violation of the arbitration guidelines*". Allowing parties to obtain confidential panel deliberations would, so the court concluded, "*provide an unfair advantage in the legal proceedings and have a chilling effect on the ability of arbitrators to communicate freely*".

This decision makes it clear that, in a US arbitration, the disqualification of a law firm is not within the jurisdiction of the arbitration panel. It also clearly demonstrates the court's view on intra-panel communications, which should remain confidential in order to uphold the integrity of the arbitral process.

As a final note, Insco sought a motion for reconsideration of the court's decision on 9 November 2011, based on evidence given by their arbitrator. This was flatly refused by the court, citing the lack of any new arguments or facts. All points raised by Insco in the motion for reconsideration had already been fully and properly considered. In response, Insco then sought a stay of the disqualification order pending the pursuit of an appeal to the Second Circuit US Court of Appeal. That motion was also declined, in a decision given on 5 December 2011. While recognising that the case presented an unusual set of facts, Insco had nevertheless failed to show a strong likelihood of reversal on appeal and the judge considered that the court could not stay the disqualification order without effectively nullifying the relief it had granted. While acknowledging that Insco would suffer harm without a stay, it was also the case that granting such a stay would punish NNIC.

Other Developments

Lead underwriter clause

PT Buana Samudra Pratama v Marine Mutual Insurance [2011][71]
Court of Appeal, 29 September 2011

This case concerned a summary judgment application on a marine hull and machinery claim arising from the grounding of a tug. The policy contained a lead underwriter claims settlement clause in the following terms:

> It is agreed to follow [the Lead Underwriter] in respect of all decisions, surveys and settlements regarding claims within the terms and conditions of the policy, unless these settlements are to be made on an ex gratia or without prejudice basis.

Some seven months after the loss, the lead underwriter, Axa, agreed to pay its 40% share. However, the Defendant, a following underwriter, considered that there were grounds to deny liability for breach of warranty, and accordingly it wrote to Axa, asking it to ensure that any settlement was on a without prejudice basis. The leader declined to do so, replying instead in the following terms:

> We have agreed to the CTL of the vessel and this settlement was not made on a "without prejudice" basis pending further investigation on the circumstances of the incident.

The central issue was whether the follower had become bound to follow the settlement concluded by the lead insurer. The Defendant argued that the breach of warranty rendered the claim otherwise than one "*within the terms of the policy*" and so there was no obligation to follow. In other words, the lead's authority to bind was limited to the adjustment and settlement of a claim which otherwise fell within the policy terms, essentially confining the leader to matters of quantum.

The Claimant, on the other hand, submitted that the leader's decision in this case constituted a settlement "*regarding claims within the terms of the policy*" and so the Defendant was obliged to follow, whether or not there had been a breach of warranty. To find otherwise, they said, would "*drive a coach and horses through the clear commercial purpose of the clause*".

71 [2011] EWHC 2413

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The Commercial Court judge found for the Claimant, giving the following grounds for doing so:

1. the wording of the clause referred to *all* settlements, suggesting that there were no exceptions to those which must be followed, save for those expressly stated, namely settlements on an ex gratia or without prejudice basis;
2. the clause referred to *all decisions, surveys and settlements*, suggesting that the authority to manage the whole process of claims investigation and settlement was conferred on the leader. That process necessarily included issues both of liability and quantum;
3. in the above context, the words *regarding claims within the terms of the policy* would reasonably be understood as encompassing decisions or settlements as to whether claims were within the terms of the policy;
4. to allow the following underwriters to dispute liability, but not quantum, might well give rise to difficulty where both have been considered by the lead underwriter in reaching a settlement and would mean that the costs of investigation and assessment of a claim (which would include issues both of liability and quantum) might be incurred by the following underwriters in addition to such investigation and assessment by the lead underwriter; and
5. underwriters were all well aware of the commercial purposes of a "follow" clause such as this. In those circumstances, if the intention of the present clause had been as contended by the Defendant, it would need to have been stated in much clearer language than that used in this case.

Iranian sanctions clause and policy renewal

Arash Shipping Enterprises Company Ltd v Groupama Transport **[2011][72]**
Court of Appeal, 25 May 2011

In October 2010, EU Council Regulation No 961/2010 (the Regulation) came into force. Amongst other things, the Regulation prohibited the insurance or reinsurance of an Iranian entity or body. The Claimant (Arash) was a Cypriot shipowning company, but controlled by an Iranian entity. It was common ground that Arash was subject to the Regulation.

The Regulation contained transitional provisions with regard to policies already in force at the time of its commencement. Specifically, Art 26(4) prohibited "*the extension or renewal of insurance and re-insurance agreements concluded before the entry into force of the Regulation*", but did not prohibit *"compliance with agreements concluded before that date*".

The dispute concerned Arash's hull and machinery policy with the Defendant, Groupama, which had incepted in May 2010. The policy contained an Iran sanctions clause as follows:

> "Insurers hereon may, on such notice in writing as the Insurer may decide, cancel the Insurer's participation under this Policy in circumstances where the Assured has exposed or may, in the opinion of the Insurer, expose the Insurer to the risk of being or becoming subject to any sanction, prohibition or adverse action in any form whatsoever against Iran..."

There was also a renewal clause in the policy, by which cover automatically extended for a further 12 months upon its anniversary, albeit subject to a proviso that renewal would not take place automatically if the claims experience had exceeded a certain prescribed level.

Two months after the commencement of the Regulation, Groupama purported to give notice of cancellation pursuant to the sanctions clause, which notice was challenged by Arash. The Commercial Court found in favour of Groupama in relation to that challenge, a decision against which Arash appealed.

72 [2011] EWCA Civ 620

Arash argued that the sanctions clause required a specific act or omission on the part of the assured such as to "expose" the insurer to the risk of sanction. There had been no such act in this case. They also argued that the notice of cancellation was not given in good faith, and was unreasonable. On this question, Arash relied primarily upon the renewal provisions in the policy. Since the policy extended automatically, they argued, the extension would in fact be in "*compliance with agreements concluded before*" the Regulation, pursuant to Article 26(4). Moreover, Arash contended that this was so obviously the correct application of Article 26(4) that the continuation of the policy could not possibly expose insurers to sanction, and hence it was unreasonable of them to conclude that it would do so.

The Court of Appeal rejected both arguments. On the first point, it was enough that a regulation had been introduced such as to expose insurers to sanction. It was not necessary that the assured should first have committed some specific act or omission to bring that situation about.

As to the second point, it could not be said to be unreasonable of insurers to form the opinion that an extension would expose them to the risk of sanction under the Regulation. This was particularly so in circumstances where the view of HM Treasury had been sought and they had specifically refused to endorse the assured's interpretation of the Regulation.

Municipal insurance and the creation of insurance mutuals
The requirement of open tender

Harrow London Borough Council v Risk Management Partners Ltd [2011][73]
Supreme Court, 9 February 2011

Until it ceased trading in 1992, most insurance provided to local authorities in the UK was underwritten by Municipal Mutual Insurance Ltd (MMI). As the name suggests, MMI was a mutual insurance company, created by and for its member authorities.

Following the demise of MMI, local authorities were required to look to the private insurance market for coverage, until 2006 when several London authorities resolved to create and participate in a new mutual, to be known as London Authorities Mutual Ltd (LAML).[74] By then, however, matters had been complicated by the introduction of the Public Contracts Regulations 2006 (the 2006 Regulations), giving effect to EU Council Directive 2004/18/EC (the Directive). In short, it is a requirement under the Directive and the 2006 Regulations that, where an authority seeks offers to undertake a public contract, it must put the contract out to tender and award it to the lowest price, or to the tender "*most economically advantageous*" from the point of view of the authority.

The parties to this Supreme Court appeal were the London Borough of Harrow (Harrow), being one of those participating in LAML, and a private insurer, Risk Management Partners Ltd (RMP) as underwriting agents on behalf of Chartis Insurance. RMP contended that, by placing its insurance risk with LAML, Harrow was in breach of its obligations under the 2006 Regulations, in that it had failed to put the insurance contract out to competitive tender. Accordingly, RMP pursued a claim for damages.

For its part, Harrow relied upon the exemption considered in the case of *Teckal Srl v Comune di Viano* (Case C-107/98) [1999].[75] That case pre-dated the current rules as set out in the Directive, but it considered the definition of a "public contract" under the prior regime. The case concerned a consortium of Italian municipalities that had collectively established a company

73 [2011] UKSC 7

74 Under separate proceedings in the Administrative Court it was subsequently determined (under the law then in force) that the authorities lacked the power to create the company. See *Brent London Borough Council v Risk Management Partners* [2009] EWCA Civ 490. LAML was placed in provisional liquidation on 8 October 2009.

75 [1999] ECR I-8121

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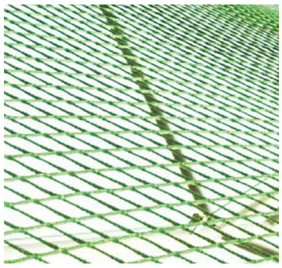
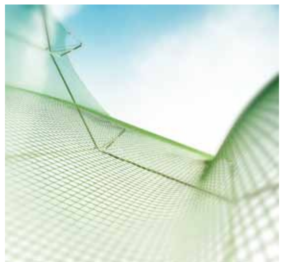
to provide them with environmental and energy services, without inviting tenders from private bidders. The court concluded that a "public contract" meant one between a public authority "*and an entity formally distinct from it and independent of it in regard to decision-making*". Conversely, relationships with an entity over which the authority exercised control would be viewed in the same way as internal relationships within its own departments, and hence not subject to the tender regime.



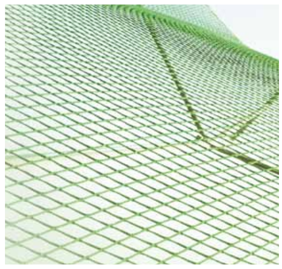
Among the issues that the Supreme Court was required to consider on Harrow's appeal were the following:

1. Did the *Teckal* decision apply to the 2006 Regulations?
2. If so, was the exemption applicable to contracts of insurance?
3. If so, to satisfy the *Teckal* "control" test, was it necessary that the authority exercised the same degree of control over LAML as that over its own departments, or was it sufficient that it did so collectively with other authorities?
4. If collective control was sufficient, was that requirement satisfied in the present case?



The Supreme Court found as follows:

1. The *Teckal* exemption applied to the 2006 Regulations. The broad object of both the Directive and the 2006 Regulations was to ensure that public bodies awarded certain contracts above a minimum value only after fair competition and to the person offering the lowest price or making the most economically advantageous offer. The *Teckal* exemption was to be read into the Directive because it would be undesirable for contracts of that kind to be open to public procurement. The absence of any reference to the *Teckal* exemption in the 2006 Regulations was of no more significance than the absence of any reference to it in the Directive that was being transposed.
2. The *Teckal* exemption was capable of applying to insurance.
3. Individual control was not necessary for the *Teckal* exemption to apply. No injury would be caused to the policy objective of the Directive if public authorities were allowed to participate in the collective procurement of goods and services, so long as no private interests were involved and they were acting solely in the public interest in the carrying out of their public service tasks. The decisive influence that a public authority must exercise over the contractor could be present even if it were exercisable only in conjunction with other public authorities.[76] Therefore, collective control by the local authorities was enough.
4. On the facts of the present case, the required collective control over strategic objectives and significant decisions was with the participating authorities at all times. This satisfied the *Teckal* control test.



Objections to a Part VII Transfer

***In the Matter of Sompo Japan Insurance Inc* [2011][77]**
Companies Court, 16 February 2011

In July 2002, Nissan Fire and Marine Insurance Co merged with Yasuda Fire and Marine Insurance Co to form Sompo Japan Insurance Plc. A large part of Nissan's legacy business comprised aviation and cat reinsurance contracts formerly underwritten on their behalf by Fortress Re. The book had suffered heavy losses, mainly due the events of 9/11 and to the air crash over Queens in New York later that same year.

76 *Carbotermo SpA v Comune di Busto Arsizio* (C-340/04) [2006] ECR I-4137 ECJ (1st Chamber), *Asociacion Nacional de Empresas Forestales (ASEMFO) v Transformacion Agraria SA (TRAGSA)* (C-295/05) [2007] ECR I-2999 ECJ and *Coditel Brabant SA v Commune d'Uccle (C-324/07)* [2008] ECR I-8457 ECJ (3rd Chamber) considered

77 [2011] EWHC 260 (Ch)

In March 2010, an application was presented to the English court, pursuant to Part VII of the Financial Services and Markets Act 2000, to transfer the Nissan book from Sompo to a subsidiary of Berkshire Hathaway Inc, Transfercom. The application faced objections by certain affected policyholders, as follows:

1. The policyholders contended that the proposed transfer would adversely affect their security. In the event of an insolvency of Transfercom, its resources would be pooled, with the result that the policyholders' prospects of payment in full could be affected by adverse experience in the run-off of Transfercom's prior existing business. The court rejected this objection. The independent expert relied upon by the applicants had in fact given an (unchallenged) opinion that, since the transferring policies would run off substantially earlier (being shorter tail business) than those of Transfercom's existing policyholders, it was the transferring business that would have first access to Transfercom's free capital.

2. The risk of lack of recognition under foreign law. The objectors contended that the majority of the contracts being transferred would likely be subject to a governing law other than that of England, perhaps with no equivalent to the Part VII regime, and which may refuse to recognise the substitution of Transfercom for Sompo as reinsurer. The scheme could therefore be in vain. Again, the objection was rejected. Provided the evidence showed that a sufficient proportion of transferring policies were subject to English law, then the risk of difficulty of recognition in relation to at least some of the balance was not a persuasive reason to refuse to sanction the scheme.

Rent-a-captive agreements struck down

American Patriot Insurance Agency et al v Mutual Holdings (Bermuda) Ltd et al [2011][78]
Court of Appeal for Bermuda, 5 August 2011

This case concerns the rent-a-captive industry, specifically the contractual structures used by it, and is a case with implications for the industry both in Bermuda and other captive centres. At first instance, the judge in the Supreme Court of Bermuda found for the Defendants, the operators of a rent-a-captive programme, and against the Plaintiffs. However, on 5 August 2011 the decision was in part overturned by the Court of Appeal for Bermuda, finding that the Appellants had been, as they alleged, victims of "*fraudulent misrepresentation and fraudulent conspiracy*".

The Defendant Respondent companies were members of the insurance group 'Mutual'. The group included both onshore subsidiaries, including Legion Insurance Company (Legion) and certain offshore entities domiciled in Bermuda, including the Defendants, Mutual Risk Management Ltd (MRM), Mutual Holdings (Bermuda) Ltd (MHB) and Mutual Indemnity (Bermuda) Ltd (MIB).

MRM widely advertised its ability to provide "rent-a-captive" insurance programmes in the United States, through its subsidiaries. Essentially, the rent-a-captive structure offers a means of tax efficient self-insurance through an offshore captive, but without the start-up costs associated with establishing a new wholly owned entity.

The Plaintiff and First Appellant in this litigation was American Patriot Insurance Agency Inc (AMPAT), an insurance brokerage incorporated in Wisconsin, USA. AMPAT had established an insurance programme called "Roofers' Advantage", to offer workers' compensation and various forms of liability coverage to roofing contractors, as an alternative to commercial insurance products.

AMPAT entered into an agreement with Mutual to make use of the rent-a-captive facility marketed by MRM. In its essential structure, it was like many other such programmes. AMPAT would propose insurance contracts which, if approved, would be underwritten by Legion, a

78 [2011] Bda L.R. 47

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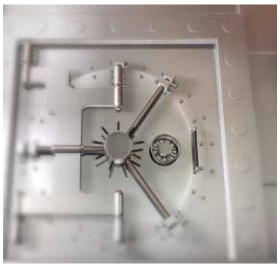

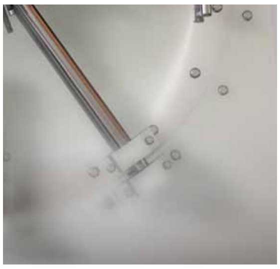

regulated onshore company within the Mutual group. For regulatory reasons, Legion was obliged to retain a small part of the risk, corresponding to 10% of gross written premiums. As to the balance, Legion's risk was reinsured with an offshore subsidiary of Mutual, in this case MIB, up to a maximum stated amount of 70% of gross written premium (referred to as the Aggregate Attachment Point, or AAP). The net total of premiums written and ceded, after deduction of agreed commissions and expenses, would be insufficient to meet the total exposure, leaving a potential shortfall, or "gap", between net premiums and total ceded liabilities up to the AAP. AMPAT, as the captive client, undertook to meet this gap by agreeing to indemnify MIB against the amount of any shortfall, in exchange for which AMPAT received the corresponding premium earned and investment returns.

As regards losses exceeding the AAP, it was agreed that Legion would take out stop loss reinsurance with open market reinsurers for an amount of US$5m in excess of the AAP. The main risk/reward for AMPAT therefore resided in the "gap".

In response to regulatory developments, it became necessary to amend the structure, with the result of extending AMPAT's exposure to losses sustained. At the same time, AMPAT paid some US$1m to MIB for additional reinsurance coverage, but this coverage was never actually purchased.

The dispute came about following questions raised by representatives of AMPAT regarding the actual extent of their potential liability. AMPAT contended that the Mutual group Respondents had falsely represented the extent of AMPAT's potential liability under the original agreement, and fraudulently (or negligently) induced them both to renew the scheme, based on the new terms, and to pay US$ 1m as a purported reinsurance premium.

Delivering the judgment of the Court of Appeal, Mr Justice Evans allowed the appeals in respect of AMPAT's claims against certain Respondents (including MIB), concluding as follows:

1. that the renewal of the AMPAT programme for the fourth year (2000/2001) and the amendment to the agreement were procured by the fraud or fraudulent misrepresentation of Legion and/or MIB, and accordingly the renewal and/or amendment could be rescinded and/or set aside; and

2. that AMPAT and its proprietors had no liability to indemnify MIB and/or MHB against any losses arising under the programme in respect of the above underwriting year.

The court made a number of provisional comments on the ineffective nature of the contractual structure of the scheme in this instance, and while it stressed that the decision was based upon the particular programme under review, and not a comment upon the rent-a-captive concept generally, the decision nevertheless throws into question the legal stability of the rent-a-captive industry. Given the importance of the decision, both in Bermuda and more widely, Mutual has indicated that it intends to appeal to the Privy Council.

The insolvency clause and reinsurers' rights to interpose

Everest Reinsurance Co v Wrynn (In re Liquidation of Midland Insurance Co) **[2011][79]**
New York Appellate Division, 25 August 2011

First Instance

Everest Reinsurance Company (Everest) entered into various excess of loss reinsurance treaties and facultative reinsurance contracts with Midland Insurance Company (Midland) for policy periods in the 1970s and 1980s.

79 No. 4195, 2011 New York Appellate Division (25 August 2011)

In 1986, the New York Supreme Court placed Midland in liquidation, and, by way of injunction, it thereafter enjoined (stayed) the commencement and prosecution of claims against Midland.

Claiming that its contractual rights were not being honoured, Everest sought from the court of first instance an order modifying the injunction so as to permit it to pursue an action under the reinsurance contracts. In particular, Everest sought leave to seek a declaration that the liquidator, in his handling of inward claims, had breached the reinsurance contracts in failing to provide Everest with: (a) proper information regarding the relevant claims; (b) an opportunity to participate in settlement negotiations with the relevant Midland policyholders; and (c) an opportunity to participate in the claim allowance process. Everest also sought a declaration regarding its statutory right, as reinsurer, to interpose defences to inward claims, specifically under New York Insurance Law § 1308(a)(3). This provides that a reinsurance agreement:

> "... may provide that the liquidator, receiver or statutory successor of an insolvent ceding insurer shall give written notice of the pendency of a claim against such insurer on the contract reinsured within a reasonable time after such claim is filed in the insolvency proceeding and that during the pendency of such claim any assuming insurer may investigate such claim and interpose, at its own expense, in the proceeding where such claim is to be adjudicated any defenses which it deems available to the ceding company, its liquidator, receiver or statutory successor. Such expense shall be chargeable subject to court approval against the insolvent ceding insurer as part of the expense of liquidation to the extent of a proportionate share of the benefit which may accrue to the ceding insurer solely as a result of the defense undertaken by the assuming insurer."

The present contracts contained an "Insolvency Clause" in a standard form, designed to give effect to § 1308(a)(3). It required that:

> "... the Liquidator ... shall give written notice to the Reinsurer of the pendency of a claim against the Company... which claim would involve a possible liability on the part of the Reinsurer within a reasonable time after the claim is filed in the liquidation proceeding... and that during the pendency of such... claim the Reinsurer may investigate such claims and interpose... in the proceeding where such claim is to be adjudicated any defense or defenses that it may deem available to the Company..."

The liquidator took the view that it was enough to provide Everest with 60 days' notice *after* it had decided to allow a claim in the liquidation but *before* submitting it to the court for approval, whereas Everest argued that it was entitled to participate in the handling and settlement of claims from the outset, and so to take part in the initial decision-making whether to allow or disallow a claim in the liquidation. The court of first instance found for the liquidator. Everest had failed to establish a likelihood of success in proving that the liquidator had violated its contractual rights, and the court considered that the liquidator's approach to Everest's interposition rights was compliant with § 1308(a)(3).

Appellate Court

Everest appealed, but without success. The Appellate Court confirmed that insurance law provides a liquidation court with broad authority to issue injunctions as it deems necessary to prevent interference with the liquidator or waste of the insurer's assets. A party wishing to claim error in the exercise of that discretion had the burden of showing an abuse of such discretionary power. In the present case, it was held that the lower court had given due consideration to the interests of justice in denying Everest's motion, and Everest had failed to show there had been an abuse of power.

The appellate court also affirmed the decision as regards the statutory imposition rights under § 1308(a)(3). While the Insurance Law permitted a reinsurance agreement to allow a reinsurer some involvement in the adjudication of claims of insolvent insurance companies, this did not imply a right to negotiate or settle claims with a policyholder. In an insolvency, claims were adjudicated *after* they had been allowed and filed at court. It was only then that Everest was permitted to be involved under the Insolvency Clause.

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The court also added that Everest's claim of a right to interpose defences at the commencement of a liquidation was at odds with the very nature of reinsurance. Even where reinsurance existed, the primary insurers remained solely responsible for the investigation and defence of inward claims, it said. The reinsurer did not assume liability for losses paid, but rather its obligation was to indemnify the primary insurer.

Moreover, the reinsurance contracts involved in the present case also contained typical "follow the settlements" or "follow the fortunes" provisions, leaving reinsurers little room to dispute the primary insurer's claims under New York law. The result, said the court, was that the reinsurer was bound by the settlement of a claim agreed by the cedent, unless it could show impropriety in arriving at the settlement.[80] The reinsured's determinations about liability were, therefore, immune from challenge by the reinsurer "*unless they are fraudulent, in bad faith, or the payments are clearly beyond the scope of the original policy or in excess of* [the reinsurer's] *agreed-to exposure*".[81]

Finally, the appeal court also rejected Everest's claim that the court lacked the authority to order the appointment of a referee to consider any defences that may be put forward by the reinsurer. On the contrary, it considered that the liquidation court's procedure for appointing referees offered a useful mechanism for dealing with a reinsurer's defences during the liquidation of an insurance company.

80 *Excess Ins. Co. Ltd. v Factory Mut. Ins. Co* 3 NY3d 577, 583 n3 [2004].

81 *Allstate Ins Co v American Home Assurance Co,* 43 AD3d 113 121 [2007], quoting *North Riv. Ins. Co. v Ace America. Reinsurance. Co.*, 361 F3d 134, 140 [2d Cir 2004]