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INTRODUCTION

For the first time this year, in addition to our Legal Review 2006 covering legal developments during the year affecting businesses in the UK generally, we have produced a number of industry sector supplements such as this one in some of the more bespoke areas in which we provide advice.

Here is a list of all the 2006 Legal Reviews and supplements with links to the publications. If you have received this in hard copy only, you will need to email or ring your usual contact to access these publications.

- Legal Review 2006: England
- Legal Review 2006: Scotland
- International Legal Review 2006
- Aviation
- Film Finance
- Food
- Insurance and Reinsurance
- Marine
- Media
- Sport
- Telecoms

In many cases, sources of further information have been given although partners and staff here at DLA Piper will be pleased to give advice. Details of key contacts are set out in appendix 1.

Nigel Knowles
January 2007
1. UTMOST GOOD FAITH

1.1 Law Commission review: non-disclosure ands misrepresentation


For business insurance, it proposes a new "reasonable insured" test. In order to establish the insured was in breach of its duties, the insurer would have to show (i) inducement (ie had it known the truth it would not have entered into the same contract on the same terms), and (ii) that a reasonable insured in the circumstances would understand the information to be material to the underwriter in question. For consumers, the same reasonable insured test would apply for misrepresentation, but the duty to volunteer information would disappear. Instead, it would be up to the insurer to ask clear questions about any matter it considered material.

The paper proposes that insurers should no longer be able to avoid for innocent breaches. In the case of negligent non-disclosure and misrepresentation, a proportionate remedy should apply, according to what would have happened had the true facts been known. In consumer insurance, however, if the insured had reasonable grounds for believing the truth of what he said or was otherwise not negligent, the insurer would have no remedy. Insurers would still be able to avoid the policy in cases of fraud.

The proposals outlined are only tentative at this stage. Formal proposals will be published in a consultation paper in June 2007.

1.2 Disclosure of allegations

The owners of the *North Star* claimed under a war risks policy for a constructive total loss arising from an explosion. Insurers' primary defence was that the loss had been deliberately caused by the owners but, in the alternative, they argued that they had validly avoided the policy for material non-disclosures. These included allegations of dishonesty made in court proceedings ongoing in Greece. The High Court found in favour of insurers on both complicity and non-disclosure. This appeal was limited to the question whether the non-disclosures were material.

The Court of Appeal upheld the High Court's decision that allegations of dishonesty made in the foreign court proceedings were material and should have been disclosed to insurers, even though the allegations were subsequently dismissed. The fact that an allegation can later be shown to be unfounded does not mean it was not material at placement (*The Grecia Express* [2002] 1 Lloyd's Rep IR 669), although the court can take into account any material the insured could have produced at placement to show his innocence (*Brotherton v Aseguradora Colsegueros SA* [2003] 1 Lloyd's Rep IR 746).

*North Star Shipping Ltd v Sphere Drake Insurance Plc* (Court of Appeal 07.04.06)

1.3 Materiality of allegations

The case concerned the insurance of a portfolio of properties owned by the first claimant. Insurers sought to avoid the contract for non-disclosure regarding (amongst other things) irregularities in the claimant's company's tax affairs. The Inland Revenue had issued an
estimated assessment for unpaid corporation tax and subsequently obtained judgment in default, including interest and penalties. The claimant argued there had been no real grounds for the assessment and the judgment was never enforced.

The main question was whether these non-disclosures were material, in the sense that they would influence the judgment of a prudent insurer. The High Court upheld the decision of the County court that they were not. The approach taken to the disclosure of unresolved allegations in the Grecia Express, Brotherton and the North Star (see above) left room for some proportionality, having regard to the nature of the risk and the moral hazard being considered. Some things may be too old or insufficiently serious to require disclosure, whether or not the insured had any material that proved his innocence. In this case, the allegation did not even allege criminality, let alone dishonesty, and so fell below the threshold for discloseability considered in the North Star. In any event, the County Court judge had found on the facts that, at the time of placement, the claimant had cogent and coherent evidence that neutralised the tax assessment.

Norwich Union Insurance Ltd v M Meisels & another (QBD 09.11.06)

2. POLICY TERMS

2.1 Law Commission review: warranties

Issues Paper 2 sets out proposals for the reform of the law on warranties in insurance contracts. The main proposal is the abolition of the automatic discharge of insurers following a breach of warranty. Instead, in consumer insurance, warranties of past or existing fact would be treated as representations only (giving the insurer a proportionate remedy as set out in Issues Paper 1). In business insurance, either the same approach would apply, or insurers would be permitted to include warranties of specific fact, provided they are set out in writing and there is a causal connection between the breach and the loss. In either case, "basis of the contract" clauses in proposal forms (which convert statements into warranties) would be ineffective.

As for warranties of future conduct, the Commission proposes that, even in cases of breach, the insured would be entitled to payment of the claim if he could show there was no causal connection between the breach and the loss. Any warranty would have to be in writing and included or referred to in the main contract document. In consumer insurance, the insurer would also have to show that it took sufficient steps to bring the requirement to the insured's attention.

Other issues raised concern the scope of the new law - whether it should cover any term that purports to exclude or limit the liability of the insurer - and the application of a fairness test to insurers' standard terms. The proposals outlined are only tentative at this stage. Formal proposals will be published in a consultation paper in June 2007.

2.2 Wilful acts exclusion

An 11 year-old boy playing in a derelict building started a fire that destroyed stock stored in adjacent premises. The issue was whether the incident was covered by his mother's householder's contents policy, which excluded any wilful, malicious or criminal acts.
The Court of Appeal concluded that the term "wilful act" meant something more than a deliberate act but less than damage deliberately caused and consciously intended. To fall within the exclusion, it was enough if the insured was reckless as to the consequences of his act. If the insured was aware that he was about to do something that risked causing damage of the kind that gave rise to the claim, or did not care whether there was such a risk or not, he would be acting recklessly if he went ahead and did it. Having regard to his age and his evidence, the Court of Appeal did not think the boy had been reckless. His conduct might be described as stupid, but that was not enough.

Christopher Patrick v The Royal London Mutual Insurance Society Ltd (Court of Appeal 30.03.06)

2.3 Deliberate acts exclusion

The claimants suffered physical and sexual abuse while resident in children's homes owned and operated by the insured company. They brought civil proceedings against the company alleging negligence. Judgment was given in their favour on the grounds that there had been extensive abuse and that the system of care operated by the company was neither adequate nor properly organised. The company was in voluntary liquidation, however, so the claimants pursued their claims directly against the company's insurers under the Third Parties (Rights against Insurers) Act 1930.

The Court of Appeal held that the claims fell within a term in the insurance excluding liability for injury arising from "a deliberate act or omission of the insured", amended in 1981 to include deliberate acts of the insured "his partners directors or managerial employees". The intention was to exclude liability for damage or injury caused by the deliberate act of a person who was to be regarded as, in effect, the company. That included the managing director, who treated the company as his own. Post 1981, the heads of individual homes fell within the description "managerial employees" and so their deliberate acts were also excluded.

KR & Others v Royal & Sun Alliance Plc (Court of Appeal 03.11.06)

2.4 Condition precedent without time limit

The insured damaged a neighbouring property while carrying out demolition work for the claimant. It notified its insurers promptly but then went into creditors' voluntary liquidation. Despite numerous requests, the insurers received no further information and declined the claim on the ground that the insured had failed to comply with the claims control clause in the policy. This obliged the insured to provide full information but did not prescribe a time limit. Observance of policy terms, however, was a condition precedent to insurers' liability.
At first instance, the judge found that it was an implied term that the information would be provided within a reasonable time. But because the insurers had not, in fact, been caused any prejudice, there had been no breach. The Court of Appeal disagreed, holding that there is no general principle that states that an insured's obligation to provide relevant information within a reasonable time will not be breached because the insurer suffers no material prejudice as a result. The insured had clearly breached the condition precedent. Different considerations might apply if the information had not yet come into existence, but to delay providing documents that were readily available for over two years was unreasonably late and obviously so.

*Shinedean Ltd v Alldown Demolition (London) Ltd* (Court of Appeal 20.06.06)

### 2.5 Warranty as to knowledge of claims or circumstances

The insured's claims-made professional indemnity insurance included cover for breaches of regulations, including costs incurred as a result of any investigation or review. The insured warranted that specified individuals had no knowledge of circumstances which could give rise to a claim within the scope of the proposed coverage. In fact, the company had already had a supervisory visit from the FSA and, shortly after the cover incepted, received a 40-page report summarising its criticisms and requiring the insured to undertake a review of past business. Insurers denied liability, claiming that the insured was in breach of warranty.

The judge (applying Ontario law to the contract) said the question was whether a reasonable person in the position of the relevant individual with knowledge of the facts would have appreciated that those facts might give rise to a claim that not only fell within the risks covered, but also exceeded the $25m retention. On the facts, he was satisfied that the relevant individual had not appreciated that the insured might have to carry out a past business review that would cost over $25m. But a reasonable person in their shoes would have done so. There had, therefore, been a breach of warranty releasing insurers from liability.

*Travelers Casualty & Surety Co v The Sun Life Assurance Co of Canada (UK) Ltd* (QBD 01.11.06)

### 3. CO-INSURANCE

#### 3.1 The undisclosed principal

The insured's vessel was undergoing completion work at Sembawang's shipyard when it was damaged by flooding. Sembawang undertook the repairs and sought to claim from insurers as a co-insured. The contract for the works provided that the insured would obtain builder's all risks cover that would include Sembawang as a co-insured and a waiver of insurers' subrogation rights. The policy, however, made no mention of Sembawang, other than to say the cover continued while the vessel was at the shipyard. The Court of Appeal held that, as a matter of construction, this policy did not cover the shipyard as co-insured. Had the parties really intended to do so, they would have used much clearer language.

Where a party is not named as an insured and does not fall within a class or description included in the cover, it may, nevertheless, be found to be covered by the policy as an undisclosed principal. In the context of this policy, however, the absence of any reference to Sembawang had to be regarded as a positive indication that insurers were not willing to
contract with it. This was a case, therefore, in which the terms of the insurance contract by implication excluded any right on the part of Sembawang to sue as an undisclosed principal.

Even if Sembawang had been insured as an undisclosed principal, it was likely that insurers would have been entitled to avoid the policy for material non-disclosure. Sembawang's inclusion in the cover would have been material to insurers because it would affect their subrogation rights in a situation where a likely source of dispute (and therefore any claim under the insurance) would be between the insured and Sembawang. The decision significantly limits the situations in which a party not identified as insured under the policy by name or category can seek to enforce the benefit of the contract. The moral of the story is to ensure such parties are named or clearly identifiable within the categories of co-insured.

_Talbot Underwriting Ltd v Nausch Hogan & Murray Inc_ (Court of Appeal 29.06.06)

4. SETTLEMENTS

4.1 Recoverability of global settlements

The insured oil company sought indemnity from its insurers for its contribution to a settlement of litigation in Texas concerning the termination of a drilling contract. The agreement did not apportion the settlement sum to particular heads of claim. It simply referred to the fact that the drilling company had asserted "various tort claims" against the oil companies. The English court held that, had the matter gone to trial in Texas, the Texan court would not have found that there had been any tortious interference with the contract, so the claim would not have found that there had been any tortious interference with the contract, so the claim would not have been covered by the insurance in any event.

However, the judge also made it clear that he disagreed with the finding in _Lumbermen's Mutual Casualty Co v Bovis Lend Lease Ltd_ [2005] 1 Lloyd’s Rep 494 that an insured could not recover under a liability policy if the claim was founded on a settlement agreement that did not specifically identify an amount that referred to a liability covered by an insured peril under the policy terms. It was not a precondition to recovery that the wording of the settlement should ascertain the specific cost to the insured of discharging its insured liability. Even if it did so, insurers could still challenge it. In which case, it must be permissible for the insured to rely on extrinsic evidence to support its claim. The judge was also careful not to draw any analogy with the settlement of reinsurance claims.

Further adverse judicial comment on _Lumbermen’s_ can be found in _AIG Europe (Ireland) Ltd v Faraday Capital Ltd_ (see below). Until a similar case comes before the Court of Appeal, however, the recoverability of global settlements remains unresolved.

_Enterprise Oil Ltd v Strand Insurance Co Ltd_ (QBD 26.01.06)

4.2 Mistakes in settlement agreements

The insured claimed under it business interruption policy for losses arising from a fire at nightclub premises. The issue was whether the cover was provided on a "gross profits" basis (in which case, averaging would apply) or whether it was "declaration-linked" (in which case, it would not). The insurer had not been prepared to offer cover on a declaration-linked basis, but its agent failed to inform the insured and issued a policy schedule clearly stating "Declaration Linked". The claim was settled applying average. The insured claimed that the
settlement contract was void for mistake because, on its true construction, this was a declaration-linked policy and average was inapplicable.

The court held that the policy was declaration-linked because the insurer's intention to cover on a gross profits basis was never communicated to the insured. Consequently, the settlement was concluded on the basis of a mutual mistake, both parties thinking this was a gross profits policy subject to average. But an agreement will only be void if the mistake is such that it makes the contract essentially and radically different from what the parties thought it was and so renders performance of the contract impossible (Bell v Lever Brothers Ltd [1932] AC 161, Great Peace Shipping Ltd v Tsavliris (International Ltd) Ltd [2002] 2 Lloyd's Rep 653). That was not the case here. The mistake simply made it rather a poor deal from the insured's point of view.

Kyle Bay Ltd v Underwriters subscribing under policy number 019057/08/01 (QBD 29.03.06)

5. DIRECTORS & OFFICERS ("D&O") INSURANCE

Companies' Act 2006

The Companies Act 2006 received royal assent on 8 November 2006. One of the main issues as far as D&O insurers are concerned is the codification of directors' duties. These replace the principal common law and equitable directors' duties, but are not intended to be exhaustive. The Act also confirms that a company can purchase insurance for a director against liability for negligence, default, breach of duty or breach of trust and, in certain limited circumstances, it will be able to provide indemnities in respect of liability incurred to a third party.

As now, the duties will be owed by a director to the company and so must be enforced by the company, rather than by its shareholders (unless they are able to bring a derivative action). The new Act, however, gives all shareholders a statutory right to bring derivative actions against directors for negligence, breach of duty or breach of trust and, before bringing a claim, shareholders will need to obtain the court's consent and the court will have to consider whether the claimant is acting in good faith, whether continuing the claim would promote the success of the company, whether or not the company's shareholders would be likely to ratify the matter, other available causes of action and the views of independent shareholders. Any damages awarded will be paid to the company for the benefit of all the shareholders, leaving little scope for bounty hunters.

These parts of the Act are not expected to be in force until October 2008. The government will be consulting on the timetable for implementation in February 2007.


6. EMPLOYER'S LIABILITY

6.1 Pleural plaques

In each of these test cases, the claimant had been negligently exposed by his employer to asbestos dust and, as a consequence, had (i) developed pleural plaques, (ii) was at risk of developing one or more long-term asbestos-related diseases and (iii) had suffered anxiety
about the prospect that he may suffer such a disease. None of these consequences - on its own - constituted damage sufficient to bring a claim in negligence. The issue was whether they could be aggregated to found a cause of action.

The Court of Appeal held by a majority that there could be no claim. Pleural plaques are not in themselves an injury or disease capable of founding a cause of action and there was no basis in law for aggregating the presence of plaques with other heads of claim, such as the increased risk of developing a disease and the anxiety this causes. There were also solid policy grounds for not imposing a general duty of care not to cause anxiety. In reaching this conclusion, the Court of Appeal was aware that it was overturning a practice that UK courts have been following for some 20 years. The House of Lords is due to hear an appeal from 25 June to 2 July 2007.

Grieves and others v F T Everard & Sons Ltd and others (Court of Appeal 26.01.06)

6.2 Apportioning liability between employers

In the test cases, Barker v Corus (UK) plc and two other cases (House of Lords 03.05.06), claimants were exposed to asbestos at different times while working for different employers and went on to develop mesothelioma. The issue was whether liability for the exposure should be apportioned between the employers.

In Fairchild v Glenhaven [2002] 3 All ER 305, the House of Lords held that such employers were jointly and severally liable, so that the claimant could recover 100% compensation from any one of them. In Barker, however, the House of Lords overturned the Fairchild approach to rule that each employer should only be held liable to the extent their breach of duty increased the risk of the claimant contracting the disease.

6.3 The Compensation Act 2006

The government reacted swiftly to Barker v Corus, introducing a new section 3 to the Compensation Act 2006 to restore the Fairchild position. Under the Act, a person who has negligently exposed the victim to asbestos ("responsible person") will be liable in respect of the whole of the damage caused to the victim by the disease, irrespective of whether the victim was additionally exposed to asbestos on other occasions.

The responsible person can seek contribution from other parties who are also liable and new rules are being introduced to amend the Financial Services Compensation Scheme to allow the responsible person (or its insurer) who has settled the victim's claim to recover a contribution from the FSCS where a mesothelioma victim or other eligible claimant could presently recover compensation from the FSCS.

7. PUBLIC LIABILITY

7.1 Trigger points

Bolton Borough Council claimed against its public liability insurers in respect of its liability to an employee who had been negligently exposed to asbestos in the 1960s. In January 1991, the employee was diagnosed as suffering from mesothelioma and he died in November that year. The policy covered liability for injury or illness "occurring within the policy period".
The Court of Appeal held that the cover was not triggered when the claimant was exposed to asbestos fibres as a result of his employer's negligence. No injury or illness occurred at that point. Liability under the policy attached when malignancy developed or when the symptoms first became apparent. It was not necessary for the purposes of this case to decide which.

*Bolton Metropolitan Borough Council v Municipal Mutual Insurance Ltd and another* (Court of Appeal 06.02.06)

8. REINSURANCE

8.1 Without prejudice settlements

The reinsured provided excess layer property cover to a US power company which suffered a series of failures in its generating units. Issues arose as to whether these constituted one or more occurrences. Settlement was eventually reached and the reinsured sought an indemnity from its reinsurers, but the reinsurers relied on the follow the settlements clause, which provided the reinsurance would "follow in all respects the settlements or other payments of whatsoever nature excluding Without Prejudice and Ex-Gratia Settlements...". The settlement agreement was stated to be without prejudice to the reinsured's position and made without the reinsured admitting liability.

The judge followed the approach taken in *Assicurazioni Generali SpA v CGU International Insurance Plc* [2003] 1 LRLR 725. Without prejudice settlements refer to settlements made on the basis of no admission of the existence of any liability under the insurance policy. Ex gratia settlements refer to payments made by insurers where there was no liability under the policy. Parties to a reinsurance contract may choose to modify the effect of a standard follow the settlements clause by specifically excluding without prejudice settlements. If the reinsured then settles an underlying claim on the basis of no admission of liability, reinsurers will not be bound by it. The reinsured will have to prove that there was actual liability to the insured.

*Faraday Capital Ltd v Copenhagen Reinsurance Company Ltd* (QBD 04.05.06)

8.2 Knowledge of loss

The reinsured provided D&O insurance to a US company that, in November 2002, announced it would be restating its accounts, causing the value of its shares to fall dramatically. Shareholders began a class action claiming they had bought shares at an artificially inflated value and had lost money as a result. The claims were settled at a mediation in March 2004 but the reinsured did not formally notify its reinsurers until 19 April 2004. The reinsurers relied on a notification clause that provided it was a condition precedent to any liability under the policy that "The Reinsured shall upon knowledge of any loss or losses which may give rise to a claim, advise the Reinsurers thereof as soon as is reasonably practicable and in any event within 30 days ..."

It was held there was no breach. The wording required actual knowledge of actual loss and there was never any actual loss known to the reinsured until settlement was reached at the mediation. Formal notification was given less than 30 days later. The wording of the clause was very similar to that in *Royal & Sun Alliance Plc v Dornoch* [2005] 1 Lloyd's Law Rep IR 544. In both cases, the parties to the reinsurance had chosen a claims cooperation clause ill-suited to liability reinsurance.
The judge also commented that the decision in *Lumbermen's Mutual Casualty Co v Bovis Lend Lease* [2005] 1 Lloyd's Law Rep 494, on the recoverability of global settlements was "unsound and should not be followed" (see also the comments made in *Enterprise Oil Ltd v Strand Insurance Company Ltd* summarised in paragraph 4.1).

*AIG Europe (Ireland) Ltd v Faraday Capital Ltd* (QBD 31.10.06)

9. BROKERS AND INTERMEDIARIES

9.1 Right of access to documents confirmed

The claimant Lloyd's Syndicates were in run-off and sought various categories of documents from the broker’s files in order to calculate the extent of their exposure. These included documents shown to the Syndicates or made available to them at placement, documents disclosed during the presentation of the claim, and documents relating to the collection, processing and accounting for premium.

At first instance, the judge found there were no grounds for finding an implied contract between broker and underwriter for the production of these documents. Practice at Lloyd's varied, so there could be no binding custom. Post-December 2000, the relationship between broker and insurer was governed by a Terms of Business Agreement ("TOBA") which, at clause 8.1 expressly entitled the Syndicates to disclosure of these documents, but this was "trumped" by clause 2.2, the broker's overriding duty to put the interests of his client first.

The Court of Appeal, however, unanimously found that there was an implied term in the insurance contract that placing and claims documents previously shown to underwriters and premium accounting documents necessary to the operation of the contract, where retained by the insured's Lloyd's broker, should be made available to underwriters in case of reasonable necessity. It was an established market practice at Lloyd's that placing and claims documentation would be retained by brokers but not by underwriters. It was, therefore, both reasonable and necessary for such documents to be made available to underwriters. Accounting documents were different, but fell within the same essential reasoning.

*Goshawk Dedicated Ltd v Tyser & Co Ltd* (Court of Appeal 07.02.06)

9.2 Establishing a duty of care

This case concerned the placement and operation of a global construction all risks open cover. Broking services were provided by Aon Risk Services of Texas ("Aon Texas") under a global Service Agreement. BP, however, established a direct relationship with Aon Ltd in London (Aon London) in respect of declarations emanating from BP's London office. Issues arose over the validity of some of the declarations. BP settled its disputes with insurers and sought to recover any shortfall from Aon London.

There was no contract between Aon London and BP, so the question was whether Aon London had assumed a responsibility to exercise reasonable skill and care in performing broking services (*Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1964] AC 465). On the evidence, the judge was satisfied that Aon London had made a sufficient assumption of responsibility to BP to give rise to a duty of care. The essential consideration was BP's reasonable perception of the conduct of Aon London. From BP's perspective, Aon London was to perform such a crucial function in effecting valid cover that Aon London was...
independently responsible for obtaining that cover. There was nothing in the Service Agreement with Aon Texas that precluded this and there was no doubt that BP had relied on Aon London's undertaking of responsibility.

**BP plc v Aon Ltd and another (QBD 13.03.06)**

### 9.3 Post-placement duties

HIH insured a company funding film projects against the risk that revenues from the finished films would be insufficient to repay the loan. The insurance and HIH's back-to-back reinsurance were placed by the same broker. The films flopped and the insured claimed under the policies. HIH paid the claims and sought to recover from its reinsurers. In 2001, the Court of Appeal confirmed that there had been breaches of warranty as to the number of films to be made. HIH now sought damages from the broker for breaches of its post-placement duty of care.

The court held that the scope of an insurance broker's duties to its client post-placement would depend on the circumstances. Here, the broker was required to disseminate information about the films in the form of risk management reports and the judge could not accept that, in doing so, it was merely acting as a post-box. The broker had a duty to alert HIH to the fact that the number of films had been reduced, even though HIH had this information from the risk management reports.

The broker's breach, however, did not cause HIH's loss. Even if the broker had explicitly drawn the reduction in the number of films to HIH's and reinsurers' attention, HIH had failed to prove that reinsurers would have agreed to the reduction or that they would have waived their rights to rely on the breaches of warranty. The judge found on the evidence that HIH would have paid the underlying claims in any event.

**HIH Casualty and General Insurance Ltd v JLT Risks Solutions Ltd (QBD 15.03.06)**

### 9.4 Continuing duty

This claim arose from a train derailment that caused substantial disruption to GNER's business. GNER claimed under its breakdown and business interruption cover but the insurers said the claim fell within a faulty workmanship exclusion. In July 2000, the High Court agreed, finding that the brokers on renewal had failed to alert the insurers to the difference between the (wider) exclusion in the expiring policy and the narrower one being requested. GNER claimed damages from the brokers but the brokers argued that the claim was time-barred because the renewal was placed over 6 years before proceedings were issued. GNER, however, claimed that the brokers owed a continuing, post placement duty of care.

The judge commented that whether or not a broker owes its client a continuing duty of care will depend on the facts of each case. Here, there was a strongly arguable case for a continuing duty and this was enough to defeat the summary judgment application. But even if GNER established that the brokers owed continuing duties, difficult issues as to causation might arise. Such issues were not suitable for summary judgment.

**Great North Eastern Railway Ltd v JLT Corporate Risks Ltd (QBD 10.05.06)**
9.5 Ostensible authority

In November 2004, two binding authorities granted by R+V to Risk to write reinsurance on its behalf were held to be the result of a dishonest conspiracy between two individuals. This case concerned a third binder and whether R+V was bound by a reinsurance contract signed by Risk on the grounds of ostensible authority.

Risk had approached a potential reinsured (ING) with documents that appeared to confirm that Risk had authority to bind R+V. Where a principal represents to a third party that an agent has authority and the third party deals with the agent on that basis, the principal will be bound by the agent's actions because the agent has ostensible authority. But the third party must be reasonably justified in regarding a communication from the principal as amounting to such a representation. On the evidence, the court found that the documents gave ING cause to ask further questions which would have shown that the proposed quota share treaty was outside its scope.

The case also raised the question whether an agent with ostensible authority is able to hold out that another person has ostensible authority to bind the principal. The judge, however, found on the evidence that the underwriter at ING knew that the document in question had not been addressed to him and did not think it was something he was meant to have seen, so it could not amount to a representation by Risk to ING.

ING Re (UK) Ltd v R+V Versicherung AG (QBD 29.06.06)

10. JURISDICTION

10.1 Service of suit clause

A number of Lloyd's syndicates participated in a US surplus lines insurance of a Nebraskan company. Disputes arose concerning the scope of the cover, but the first issue was that of jurisdiction. The policy, written on Lloyd's form NMA 2072, included a non-exclusive jurisdiction clause in favour of the English court and (as required by Lloyd's regulations) a service of suit clause giving the insured an option to request insurers to submit to the jurisdiction of courts in the US. Underwriters issued proceedings in England and the insured subsequently issued proceedings in Nebraska. Both parties were acting within their contractual rights, but which prevailed?

The court considered which of the two was the most appropriate forum and decided in favour of Nebraska. Various factors connected the dispute with the US, but the most significant was the service of suit clause. Although there had been a general agreement as to English jurisdiction, the parties had agreed that the insured had a specific right to elect US jurisdiction. That right had been exercised. This was something to which insurers freely agreed and that choice must be given full weight. In the specific circumstances of this case, and for the purposes of considering appropriate forum, the service of suit clause took precedence over the general law and jurisdiction clause.

Catlin Syndicate Ltd and Others v Adams Land & Cattle Co (QBD 20.07.06)
11. INSOLVENCY AND SCHEMES

11.1 Voting classes

Creditors voting on a scheme of arrangement under section 425 of the Companies Act 1985 must be placed in different classes and vote at separate meetings if their rights are "so dissimilar as to make it impossible for them to consult together with a view to their common interest" (Sovereign Life Assurance Co v Dodd [1892] 2 QB 573). In BAIC [2005] EWHC 1621) the court considering a solvent scheme of arrangement held that creditors with accrued claims and creditors with IBNR (incurred but not reported) claims should vote at separate meetings.

The judge in WFUM held that, although influential, BAIC did not set down a general rule that creditors with IBNR claims should always be placed in a separate voting class from those with accrued claims. The standard test had to be applied to the facts of each case. Having done this, he concluded that the interests of creditors with outstanding claims (claims notified to the proposed scheme) and those with IBNR claims were so different as to make it impossible for them to consult together with a view to their common interest. An important factor was the very wide range of uncertainty in estimating and valuing the different categories of claim. Broadly speaking, however, outstanding claims were likely to be less uncertain than IBNR claims.

The judge also confirmed that the English court has jurisdiction to sanction schemes for insurers incorporated in another EEA state, provided they have a sufficient connection with England.

The WFUM Scheme - In re Sovereign Marine and General Insurance Co Ltd and others (Chancery Div 09 06.06)

11.2 Points of principle

The aim of this solvent scheme was to enable Cape and its subsidiaries to carry on business so as to be in a better position to meet future claims for damages arising from exposure to asbestos. An initial sum of money was to be paid into a new subsidiary to meet all such claims. Claimants (the scheme creditors) would still be able to bring proceedings against individual scheme companies, but would only be able to enforce payment against the new subsidiary. Applying the standard test for voting classes, the court held that creditors in different categories could be placed in the same class. This was not a cut-off scheme. Claims would be paid as and when they were established, whether or not the scheme was in place.

On a more general note, the court held that, in exceptional cases (of which this was one), it had jurisdiction to sanction a scheme that included provisions for the subsequent amendment of its terms. In addition, the court confirmed that, in the absence of evidence that there was only one member of a voting class, a meeting attended by a single scheme creditor was not a creditors' meeting for the purposes of section 425.

In the matter of Cape Plc and Others (Chancery Div, June 2006)
11.3 The appropriate comparator

This insolvent scheme of arrangement formed an integral part of a settlement agreement between the companies and its insurers under which insurers would provide a sum of money to be held on trust to pay a dividend to meet claims and the companies would enter into schemes that would bind all those with present or future claims under EL policies. When considering the composition of voting classes, therefore, the appropriate comparator was not a winding up, but the continuance of the insurance litigation. In these circumstances, it was appropriate that the scheme creditors should vote in a single class.

Creditors with contingent contribution claims against T&N (such as employers of a claimant) could be scheme creditors, but future possible employers and present employers who had not yet exposed the employee to asbestos could not. Those with claims under the Fatal Accident Act 1976 would be bound by the scheme, but future dependants would not. Amending the EL policies to exclude future FAA dependents would not contravene the obligation to "maintain" insurance under the Employer's Liability (Compulsory Insurance) Act 1969. Nothing in the Act precluded a genuine compromise of a genuine dispute, even if that involved an amendment of policy terms as regards the rights of future dependants.

In the matter of T&N Ltd and Others (16.06.06 Chancery Div)

11.4 Reimbursement of claims handling expenses

Under the terms of this policy, insurers would take control of claims handling if an insolvency event occurred or the Ultimate Net Loss exceeded a certain limit, until the limit of cover was reached. The insured went into administration (an insolvency event). Insurers took over claims handling and argued that reimbursement of claims handling costs should be given priority in the administration under section 19(5) of the Insolvency Act 1986 as payments made under contracts entered into by the administrators.

The House of Lords, reversing the Court of Appeal's decision, held that claims handling costs incurred by insurers on behalf of a company could not properly be said to be liabilities incurred under contracts entered into by the company's administrators and so should not be given priority over the company's other debts under section 19(5). The administrators had had nothing to do with either the contracts under which the liabilities were incurred, nor the contract that gave insurers authority to incur costs on behalf of the company.

Freakley and others v Centre Reinsurance International Co and another (House of Lords 11.10.06)

12. REGULATION

12.1 Lloyd's Names - no right of action under the Insurance Directive ("Directive")

Lloyd's Names who took part in Lloyd's syndicates from 1980 to 1986 brought proceedings against the government alleging that they had suffered loss as a result of the government's failure to implement the Insurance Directive (73/239EEC) into domestic law or to achieve its prescribed result as regards the authorisation and monitoring of Lloyd's syndicates.

The court found that the reference to the protection of third parties in the Directive referred to parties entitled to the benefit of insurance, not to Names, whose position was analogous to
that of an insurer or a shareholder in an insurance company. The purpose of regulation was not to protect the regulated, but those to whom they supply services or products. In any event, the Directive did not grant any right to individuals because such rights were not necessary to achieve the results intended by the Directive (Three Rivers DC v Bank of England (No3) [2003] 2 AC 1). Lastly, the claims were statute-barred by the Limitation Act 1980, as any cause of action arose much earlier than six years before proceedings were issued and the Names had the requisite knowledge much earlier than three years before they began their action.

*Frederick Thomas Poole and others v HM Treasury (QBD 08.11.06)*
APPENDIX 1

Contributors and contacts

This Insurance and Reinsurance review has been prepared by: Matt Illingworth (Associate)

Contact details:

Group: Litigation & Arbitration
Partner contact: Charles Gordon
Telephone: +44 (0)20 7796 6541
Email: charles.gordon@dlapiper.com