Principles of Insurance Law

Introduction

The function and characteristics of insurance

Put broadly, insurance is a contractual process whereby risk is transferred from a person who might incur a loss, to an insurer. This description however only applies to what is called 'indemnity insurance'. Most insurance is written on an indemnity basis, that is the insurer promises to indemnify the policyholder or more accurately the 'insured' against the financial repercussions of an uncertain event. Perhaps the most obvious example of this is motor insurance. In the United Kingdom and indeed in most countries it is compulsory for motorists to be insured at least against liability to third parties but most drivers also insure themselves against loss or damage to their own vehicle (often called 'fully comprehensive') and often for additional risks such as the cost of roadside repairs and recovery and legal expenses associated with an accident. In this way the financial consequences of accidents and other contingencies is assumed by the insurer and removed from the motorist subject to the policy limits if any as to maximum liability and any requirement that the insured bear the first tranche of any loss—called in motor insurance, the 'excess'.[1]

This example illustrates a number of legal issues. Firstly insurance can be used for social purposes. The compulsory nature of motor insurance for third party liability is to ensure that a person injured in a road accident for which a motorist is responsible is not reliant on the solvency of the motorist to receive compensation, indeed by virtue of s 151 of the Road Traffic Act 1988 the injured party has a direct claim against the insurer so that payments which would otherwise have been made by the insurer to an insolvent insured in respect of his liability, will not form part of the insolvent's estate but are paid directly to the third party.[2] Similarly, compulsory insurance must be held by employers in respect of liability for workplace injuries to their employees.[3] Whilst this was not the original reason for such compulsory insurances, it is clear that by such

[1] Called this because the insurer promises to pay the 'excess of loss' above a given figure.

[2] Under the Third Parties (Rights against Insurers) Act 1930 the rights of the insured under any liability policy are transferred to the injured third party. This Act has generated many problems and will be repealed in full and the transfer of rights clarified now the Third Parties (Rights against Insurers) Act 2010 has come into force.

[3] s 1 Employers Liability (Compulsory Insurance) Act 1969.

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mechanisms the state is relieved of costs associated with motor and workplace injuries. As a final example the rapid growth of a market in 'after the event' legal expenses insurance which in effect limits the maximum cost of pursuing or defending a legal claim also serves the purpose of making more palatable the shrinkage in the provision of civil legal aid by the state.

Secondly, 'fully comprehensive' motor insurance clearly covers different types of loss. There is property insurance—the car and possibly its contents—and as we have seen, insurance of liability to third parties. Legal expenses insurance too is a specialist type of liability insurance involving voluntarily incurred liability to pay legal fees. What motor insurance does not cover is economic loss. Suppose the insured is a self-employed van driver who crashes his van which takes six weeks to repair. During this time he cannot carry on his business and so suffers loss of the profits he would have otherwise made but for the accident. Whilst this is a very real loss directly attributable to the occurrence of an insured event, a property and/or liability policy will not respond—he would need to take out a separate loss of profits insurance if he wanted to cover this type of loss.

This division of coverage into property, liability and economic illustrates an important point, the basis of most insurance is, as noted above, indemnity, providing compensation to the policyholder against insured losses but no more. However some insurance is written on a contingency basis so that on the happening of the insured event the insurer will pay a fixed sum which is only indirectly connected with any financial loss suffered. Much life insurance[4] is written on a contingency basis. After all if I insure my own life for £1m I do not suffer a £1m loss when I die—I have no more use for money.[5] There are some apparent exceptions to the indemnity principle outside insurances of the person. For example some motor insurance offers 'new for old' cover, typically through new car sale rooms during the first year or two of a car's ownership. Under such insurance, if a car is damaged beyond economic repair the motorist will receive a brand new car as a replacement even though the value of a new car declines very rapidly during the first years of its life. However most motor insurance is not written on a new for old but a strict indemnity basis so that in our example such an indemnity policy would only provide for the cost of replacement, i.e. the second hand value of the car. Nowadays many household policies also provide 'new for old' cover for damaged furniture, carpets and curtains and in insurance of goods in transit, there can be 'valued' policies where the insurer will pay a fixed sum in the event of loss or damage. These appear to be examples of contingency insurance, but it should be noted the insured owns the property which is insured, that is he has an 'interest' in it in the sense that he will suffer a quantifiable loss in the event that it is damaged and so it is better to see these cases as ones where the parties to the insurance have agreed the quantum in advance.

Finally motor insurance illustrates a further characteristic of insurance, insurances taken on behalf of other people. Often a car owner will allow someone else to drive his car and in the past, under motor policies, the insurer agreed to indemnify the insured against liability such drivers may have against third parties. The problems this arrangement causes are best illustrated by considering *Williams v Baltic Insurance*

[4] Indeed almost all insurances of the person are written on this basis.

[5] Except perhaps to pay the ferryman Charon across the river Styx to Hades!

Association of London Ltd.[6] Here the insured's sister was successfully sued for damages by third parties whom she had injured whilst driving the car. The insured claimed that the insurers were liable to pay him an indemnity equal to the damages she had paid. The contractual difficulty is immediately obvious—the insured has suffered no loss whilst the person who has suffered loss is not party to the insurance contract. However, Roche J held that nevertheless the insurer had to pay the insured, seemingly on the basis that he was effecting the policy on behalf of himself primarily but also as agent for other drivers of the car concluding that he would hold the insurance monies as trustee for her. On this basis it would seem to follow that the sister could also, as principal, have sued in her own right.[7]

What is 'insurance'?

While it is easy to think of clear examples of insurance, generally Parliament, statutory regulators of insurers and the courts have not attempted a definition,[8] being content to give general principles and decide on a case-by-case basis. Probably the most influential 'definition' was that of Chanell J in *Prudential Insurance v Commissioners of Inland Revenue*[9] who in relation to what would today be regarded as a clear example of insurance suggested the following as the requirements for a contract to amount to insurance:

> It must be a contract whereby for some consideration, usually though not necessarily for periodical payments called premiums you secure for yourself some benefit, usually but not necessarily the payment of a sum of money upon the happening of some event . . . (and) the event should be one which involves some amount of uncertainty. There must be uncertainty either about whether the event will happen or not or . . . as to the time at which it will happen. The remaining essential is that . . . the uncertain event . . . must be an event which is prima facie adverse to the interest of the insured.

The issues arising from 'risk not certainty' and the implications that the insured must have an 'interest' under the policy are explored in a little more depth later in this chapter but even at this point it is clear that these 'essentials' do not apply to all insurances while all contracts with these characteristics are not contracts of insurance. For example it is possible to insure against events which have already happened[10] while a retailer's warranty that he will replace the goods if they break down within say three years of purchase falls within Channell J's 'definition' yet almost certainly is not insurance but simply an extension of the normal obligations of quality arising out of sales of goods.[11] The situation is probably different however if an extended warranty is given by a third party for separate consideration.[12] So too contracts of guaranty bear startling resemblance to contracts of insurance. Under a contract of guaranty,[13] A (the

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[6] [1924] 2KB 282 (HC).

[7] There is also an issue of insurable interest which will be considered below. Modern policies tend not to be written on the basis in *Williams*.

[8] There are exceptions, for the earliest clear example see Lawrence J in *Lucena v Crauford* (1802) 2 B & P(NR) 269.

[9] [1906] 2 KB 658.

[10] See s 6(1) Marine Insurance Act 1906.

[11] Though suppose the warranty were for an exceptionally long period or for which the manufacturer makes an explicit charge leaving the purchaser to decide whether he wants to pay for the warranty or not?

[12] Though see the decision of the Ohio Supreme Court to the contrary in *Griffin Systems Inc v Ohio Department of Insurance* 575 NE 2d 803.

[13] Commonly nowadays spelt in Standard English (though not American English) as 'guarantee' which can cause confusion since the word is also used to identify the person to whom the guaranty is given!

guarantor or 'surety') promises B (the guarantee) that if C, a third party who owes duties to B does not perform his obligations, A will perform them. Typically those duties will be to pay a debt owed to be owed by C to B and A may charge for his standing surety. Clearly here, in a sense, A is insuring C's solvency but there are distinctions between insurance and a guaranty in particular that if A charges for his surety it will be C not B who but the particular difference is that a guaranty involves three parties—obligor (C) obligee (B) and surety (A).[14]

Almost all of the cases cited this section involve a government department bringing an action against a business. The reason for this is that in almost all countries the carrying on of insurance is a regulated activity which requires authorization from the state[15] and which is subject to strict supervision. It also used to be a criminal offence in the UK to carry on insurance business without authorization.[16] Consequently it is essential for business people and their advisors to be able to determine whether a proposed business activity constitutes the regulated activity of 'effecting and carrying out of contracts of insurance'.[17] However as we have seen this is not always at all easy.[18]

In addition, once a contract has been classified as 'insurance' the insurer is automatically subrogated to the rights of the insured against third parties once he has indemnified the insured against his losses. Suppose for example you have fully comprehensive motor insurance and are the innocent party in a road accident in which your car is seriously damaged by a negligent driver. Your insurer will indemnify you under the policy for the costs of repair and then 'steps into your shoes' so that it can sue the other driver in negligence, just as you could have done if you had decided not to claim on your policy. In fact the negligent motorist will himself have insurance against loss he causes to other people (third party insurance) so in reality your insurer will be seeking recovery against another insurance company.[19] There are a number of exceptions to the subrogation rights of an insurer, including in cases of 'co-insurance'. Co-insurance occurs where a number of people are insured against the same risk under the same policy but in respect of different interests. In co-insurance the insurer is not subrogated to the rights of one co-insured in order to pursue a claim against another co-insured in respect of the same risk. Co-insurance typically arises where there is a venture in which a number of parties are concerned and have agreed that an insurance be taken out by one of their number for the benefit of each person.[20] In such a case it has been held (obiter) that the reason why an insurer cannot be subrogated in

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[14] See in particular Romer LJ in *Seaton v Heath* [1899] 1 QB 782 (CA) 792–793.

[15] In the UK this is set out in s 19 Financial Services and Markets Act 2000.

[16] Now removed by s 20 FSMA 2000 since the illegality rendered the contract with the business unenforceable leaving the 'policyholder' with no contractual claim against his counterparty.

[17] This is the definition of the relevant regulated activity set out in Art 10 Financial Services and Markets Act 2000 (Regulated Activities) Order 2001.

[18] Helpfully, one of the financial services regulators—the Financial Conduct Authority has issued guidance on what in its view constitutes the regulated activity see FCA Handbook, PERG 6.

[19] Consequently much accident litigation is really about which of two insurers will bear the cost. It also explains why often if you have a car accident the insurers will insist that rather than try to find out who is to blame, which can be very costly and time consuming for them, they will go 'knock for knock'. This means that each insurer will pay for its own insured's losses. Consequently, even if you are innocent, you end up making a claim on your policy which will probably increase the premium you will pay when you renew your policy even with 'protected no claims' policies.

[20] For an example see *National Oil Well (UK) Ltd v Davy Offshore Ltd* [1993] 2 Lloyds Rep 582 (Comm) discussed below at page XX.

such circumstances is that there is an implied term in the policy to the effect that the insurer has surrendered such rights.[21] This may be the correct explanation for the rule but in fact, in the past the courts have explained it as avoiding an absurdity since in effect an insurer would normally be suing a person whom he has agreed to indemnify meaning the claim is circular.[22]

General insurance and life insurance

The insurance industry divides insurance into two broad categories: life insurance which, as its name suggests, involves insurance of the uncertainty of when a person dies,[23] and general insurance which is everything else. General insurance is what we will focus on in this chapter since this is a commercial law book and life insurance has only limited commercial application. Nevertheless it is helpful to be aware of the function of life insurance which often is not insurance as we have described it but solely or mainly an investment.

However, term insurance is insurance pure and simple, in the sense that the insurer will pay under the policy only if the life insured (often called 'the assured' in life insurance business) dies before a particular date. We might imagine a couple buying a house taking out such a policy when they got a mortgage so that if either of them died before the mortgage was repaid the policy would pay out sufficient money to redeem it. However dying too young is not the only misfortune associated with death. Suppose in the nineteenth century I need to work in order to live. I know I cannot work beyond (say) 60 so I take out a policy called a 'pure endowment' which will pay out a lump sum if I reach that age which I use to see me through my retirement. This type of insurance is the origin of modern day 'pension plans' which are classed as life insurance even though they are purely investment contracts.[24] From these pure endowments developed the modern day 'endowment policy' which will pay a fixed sum if the life assured dies before a certain date (like a term policy) and a lump sum if he does not like a pure endowment. Similarly 'whole of life' policies were developed which would make a payment whenever the life assured died. The early life insurance companies recognized that the premiums paid by policyholders particularly of endowment and whole of life type policies could be invested until payments out needed to be made and in consequence substantial surpluses developed in their life funds. Since most insurers were owned by their members, that is their policyholders, these surpluses needed to be distributed and so the practice of adding a share of these investment profits to the benefits payable under policies commenced. In consequence 'with profits' policies

[21] Lord Hope of Craighead in *Co-operative Retail Services Ltd v Taylor Young Partnership Ltd* [2002] UKHL 17, [2002][65], 1 WLR 1419 [65]. Though see Rix LJ in *Tyco Fire & Integrated Solutions (UK) Ltd v Rolls Royce Cars Ltd* [2008] EWCA Civ 286 who suggests that the issue actually depends on the construction of the contract between the co-insureds which imposed the duty to acquire the co-insurance policy. If that contract permits the co-insureds to sue one another then there is no bar to an insurer being subrogated to such a claim.

[22] The claimant will actually be the injured co-insured but the insurer will have control of the claim and any damages recovered in respect of a loss for which it has indemnified the claimant will be paid to the insurer.

[23] Even Benjamin Franklin recognized that along with taxes, death is certain.

[24] In fact they are issued with an accompanying term policy which will pay the value of the policy at the date of death. See ss 620-621 Income and Corporation Taxes Act 1988.

were developed often with no or very small guaranteed payments on death purely as investment vehicles and these were nevertheless accepted as 'insurance' contracts.[25] Therefore most life insurance policies are intended by the purchasers as much as investment vehicles as they are intended to cover the possibility of the death of the life assured and all but pure term policies are classed as 'investments'.

The regulation of insurers

Until 1986 there was no unified approach to the regulation of the provision of financial services in the UK. Some businesses like banks and insurance companies required authorization to do business (but from different bodies) but generally the provision of other services, for example giving investment advice or managing clients' investments did not. Similarly insurance brokers, who act as agents for their clients seeking the most appropriate insurance to meet the clients' needs, were basically unregulated unless actually describing themselves as 'insurance brokers'.[26] Insurers were authorized by the Department of Trade and Industry (DTI) which primarily supervized their financial stability particularly the adequacy of their assets to meet the claims of policyholders, known as prudential supervision. The DTI also became increasingly concerned with the suitability of the owners of the business and of senior managers to be involved in running the business, known generally as 'fitness and properness'. However there was no regulation of how businesses related to their customers—conduct of business—nor to any great extent on their internal management and controls notwithstanding the fact that weak internal controls open businesses up to risks which can endanger their capital bases.

This changed with the Financial Services Act 1986 which created a new supervisory body, the Securities and Investment Board, to regulate conduct of business which it did primarily through a number of 'Self Regulatory Organizations' established by participants in the financial services market. Thus, the way life insurers[27] dealt with their customers became regulated and their conduct supervized initially by the Life Assurance and Unit Trust Regulatory Organisation, though later, following a series of mergers of SROs, by the Personal Investment Authority. Prudential supervision and regulation however remained with the DTI and conduct of business in relation to non-life insurance (general insurance) remained unregulated.

Following a number of regulatory failures not least the pensions mis-selling scandal and the collapse of Equitable Life[28] the 1986 regime of self regulation was scrapped and in 2001 prudential and conduct of business regulation was consolidated under a new regulator, the Financial Services Authority (FSA) when the Financial Services

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[25] For an extreme example see *Fuji Finance v Aetna Insurance Co* [1995] Ch 122 (CA) where there was a single premium payable on a whole of life policy which could be surrendered to the insurer at any time for the value of the policy with the insurer paying 101% of the value of the policy on death. The value of the policy could fall below the amount of the premium depending on how the insurer's investment fund performed.

[26] Under the Insurance Brokers Registration Act 1977 using such a descriptor was unlawful unless the business was registered with the Insurance Brokers' Registration Council. The Act was repealed in 2000.

[27] The 1986 Act was only concerned with 'investments'. It is for this reason that the conduct of business of general insurers was not affected by the Act.

[28] The financial failure of Equitable Life was felt particularly badly by lawyers and academics since it was the pension provider of choice for the legal profession and university lecturers.

Markets Act 2000 came into force. This remains the primary piece of legislation governing the regulation of financial services businesses notwithstanding the fact that following the 2007 crash it was decided to split responsibilities for prudential regulation from responsibility for conduct of business and consequently two new regulatory bodies were formed, the Prudential Regulatory Authority—part of the Bank of England—and the Financial Conduct Authority (FCA). The new regime, established under the Financial Services Act 2012, came into operation on 1 April 2013 and insurers must be authorized by both authorities if they wish to carry out the regulated activity of 'effecting and carrying out of contracts of insurance'.

The size and importance of the UK insurance industry

There are around 560 insurance companies authorized by the UK,[29] 200 Friendly Societies[30] as well as the insurance market, Lloyds of London.[31]

In terms of the size and importance the following is a fair summary of the situation as at the end of 2021:

> The UK insurance industry is the largest in Europe and the fourth largest in the world. It plays an essential part in the UK's economic strength, managing investments of £1.6 trillion (equivalent to 25% of the UK's total net worth) and paying nearly £16bn in taxes to the Government. It employs around 330,000 individuals, of which more than a third are employed directly by insurers with the remainder in auxiliary services such as broking.[32]

There are a range of factors which have contributed to this position, not least the interdependence of insurance and ready access to capital, an access assisted by the growth of London and Edinburgh as major world banking centres. Similarly the rapid expansion in world trade dominated by Great Britain in the nineteenth century meant that underwriting expertise was developed and concentrated in the major ports and especially London. This expertise continues to this day especially in relation to what are called 'non-standard risks' where London Market remains pre-eminent. An important additional factor is the development of English insurance law which is primarily case law based and to which we now need to turn in detail.

The Key Elements of Insurance

Risk not certainty

In his judgment in *Prudential Insurance v Commissioners of Inland Revenue*,[33] Chanell J identified three key elements in a contract of insurance, consideration given by the insured, an undertaking on the part of the insurer, but, and this is the third element, only on the occurrence of a contingency. Channell J identified two types of contingency

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[29] Bank of England Statistics Office.

[30] A Friendly Society is an organization which provides insurance and investments and which is owned by policyholders, i.e. it is a 'mutual' organization. Most started long before the welfare state as mutual aid societies among working class men and women to provide benefits if a member became ill or died.

[31] Lloyds is not an insurer as such but members of Lloyds provide financial backing to the underwriting of insurance, the Council of Lloyds manages the market and is regulated by the FCA.

[32] Source: Key Facts for 2021, the Association of British Insurers.

[33] [1906] 2 KB 658 (HC).

or risk, firstly an event which may or may not happen and secondly one which is inevitable but the timing of which is uncertain. To this can be added a third, where an event has already occurred but the insured is unaware of this at the time of making the contract, by implication from s 6(1) Marine Insurance Act 1906 (MIA 1906).[34]

This leaves open the issue of whether one can insure against an event which unknown to either party to the contract is inevitable. There seems no reason why not since the insurance contemplated by s 6 MIA 1906 is an example of an inevitable loss, while it is perfectly sensible for a person to seek indemnity against the possibility that he will suffer such a loss. A potential example of this is *Global Process Systems Inc v Syrikat Takaful Malasia Bhd (The Cendor Mopu).*[35] Here a 30 year old oil production rig was being transported by sea from Texas to the Far East by sea in winter. It was known by both parties to have metal fatigue and was insured against damage or loss caused by 'all risks'. The case centres on a clause which excluded loss caused by 'inherent vice', i.e. that there was something about the rig which meant it 'damaged itself', but there are indications in the judgment of Lord Mance which might be taken to support the view that inevitable losses cannot constitute the subject matter of insurance.[36] However the better view is that there is nothing intrinsic in the concept of insurance which prevents insurance of inevitabilities and that Lord Mance should be understood as meaning simply that the policy under consideration (a standard form policy of marine cargo insurance) does not cover such risks because, on a construction of the policy terms it only covers 'fortuities'[37] not that losses from non-fortuitous events cannot be insured.

What amounts to a 'fortuity' at least in relation to property insurance was considered in a Canadian decision *Ontario Ltd v Coachman Insurance.*[38] Here the claimant insured his petrol filling station against 'all risks of direct physical loss or damage from any external cause.' It was discovered that an underground pipe to the petrol storage tank had developed cracks, allowing water to contaminate the petrol. The insurer refused to pay since the loss was an inevitable result of the circumstances and the policy only covered fortuitous loss. The Ontario Divisional Court held, reversing the judge at first instance, that the concept of fortuity does not depend on whether the loss was inevitable due to the physical circumstances. The Court explained that whilst it was true that the policy only covered fortuitous losses, that simply meant that there was no coverage where the insured was a contributory cause or where the insured was aware of and expected the loss. Consequently, whilst the policy would not cover losses which could be expected to arise in the normal course of business of the insured, such as ordinary wear and tear and depreciation; it did cover a loss such as this which was not a common occurrence. This approach has to be contrasted with that in *Leeds Becket University v Travellers Insurance*[39] where the court held that the subsidence in

[34] The MIA 1906 encapsulates much of the common law on insurance and so the principles generally apply beyond simply marine insurance.

[35] [2011] UKSC 5.

[36] See also Cockburn CJ in *Paterson v Harris* (1861) 1 B & S 336, 353: 'the purpose of insurance is to afford protection against contingencies and dangers which may or may not occur; it cannot properly apply to a case where the loss or injury must inevitably take place in the ordinary course of things'.

[37] It should be noted that the policy in question does not expressly require a 'fortuity' but this requirement has been read into 'all risks policies' by the courts.

[38] (2014) 117 OR (3d) 635 (Div Ct).

[39] *Leeds Becket University v Travellers Insurance* [2017] EWHC 558 (TCC).

a wall of a university hall of residence was an inevitable loss not caused by an accident (flood) because it was only a matter of time before its concrete foundations rotted though being dug in the path of a contaminated underground stream.

In conclusion on this issue, whilst there has been a tendency to focus on the risk of the physical occurrence of the event which causes the loss, the true uncertainty that is essential to the existence of a contract of insurance is not whether the event is actually contingent or not but is the existence of uncertainty in the mind of the person seeking insurance as to whether or when he will suffer a loss and it is against this uncertainty that he is insuring. On this view, if in *The Cendor Mopu* for example, the finding of fact being that the structure of the rig was so weakened by metal fatigue before it departed from the port of loading that any prolonged motion on the sea would have caused it to break up, and had the policy contained no exclusion for 'inherent vice', there would still have been valid insurance notwithstanding the fact that the loss was an inevitable result of the intended voyage. Here the insurer and the insured would in effect be insuring among other things the risk that the rig was incapable of reaching its destination intact and this is uncertainty in the minds of the parties, the uncertainty to which Channell J was referring to in the quotation above from *Prudential Insurance v Commissioners of Inland Revenue*.[40]

Insurable interest

What is an insurable interest?

The final essential element identified by Channel J is that: ' the uncertain event. . .must be an event which is . . . prima facie adverse to the interest of the insured'. Another way of putting this is that the insured must have what is called 'an insurable interest' under the policy. Whilst what constitutes an insurable interest is complex and varies between different types of insurance, in essence for a policyholder to have an insurable interest in an event he will benefit from the preservation of the subject matter of the policy or suffer a disadvantage if it is lost.

The primary problem which the requirement of insurable interest seeks to achieve is to differentiate insurance from gambling. For example it is clearly socially undesirable to enter into contracts where the 'insurer' is obliged to pay the other should someone else die (the life assured) if that death would not otherwise disadvantage the insured. Such a contract would provide an incentive to murder, as would one where the amount of loss of the interest suffered by the insured on the death of the life assured is less than the sum payable under the policy. By extension we can see that similar considerations apply to other types of insurance like insuring the house of an unconnected party against fire or insuring his goods against theft. In 1745 The Marine Insurance Act made marine insurance contracts made without insurable interest 'null and void'[41] and ss 1 and 2 of the Life Assurance Act 1774 made policies to which it applied both void and illegal.[42] The 1774 Act does not extend to insurances of goods (including cash) but

[40] [1906] 2 KB 658 (HC).

[41] The 1745 Act was repealed by the Marine Insurance Act 1906 but s 4 of the 1906 Act states that contracts of marine insurance made without insurable interest are void.

[42] The effect of illegality is not only that the 'insurer' need not pay benefits under the policy but need not return the premium either.

from 1845 until 2005 the Gaming Act rendered insurance of these void if made without interest. This may no longer be the case since the 1845 Act has been repealed by the Gambling Act 2005 but since property insurance is written on an indemnity basis, the policyholder will nevertheless need to show the loss or damage to the property caused him a financial loss in order to claim under the policy.[43]

As elsewhere in this chapter there will be no consideration of life insurance but it may help to look at some examples of insurable interest in relation to property insurance which has a clear application in everyday commerce. In the process there must necessarily be some discussion of liability insurance and loss of profits insurance.

Insurable Interest in property and liability insurance

In relation to property insurances which cover loss or damage to land or goods, the courts initially insisted that the insured must either have a legal or equitable interest in the property insured or rights deriving from a contract about the property, in particular buyers of goods after risk in them has passed but title has not and the contingent reversionary 'ownership' of sellers who have passed title to goods but which may be rejected by the buyer. This position stems from subsequent interpretations of the judgments in the early case of *Lucena v Crauford*.[44] In the opinion of Lawrence J, whilst the nature of insurance is indemnity, and this imports the necessity for interest it does not necessarily mean that the insured must have property rights in the subject matter of the insurance merely a 'moral' that is to say a factual certainty of advantage if the goods are not destroyed. However, until comparatively recently the courts chose to follow the opinion of Lord Eldon who in *Lucena* insisted on the need for interest to involve a right in the property which is the subject matter of the insurance or a right deriving from a contract about such property.

Lucena v Crauford (1806) 2 Bos & Pul (NR) 269

FACTS: By Act of Parliament, in the period of uncertainty pending the anticipated outbreak of war between Great Britain and The Dutch Republic, a duty was imposed on Admiralty Commissioners to take care of Dutch ships and their cargoes which 'had been or might be thereafter detained in or brought into the ports of the United Kingdom'. The Commissioners insured Dutch ships which had been seized and were at sea bound for the UK. The ships sank and the insurers refused to pay on the basis that the Commissioners did not have an insurable interest at the time of the loss.

HELD: The House of Lords held that since the duties of the Commissioners only commenced once the ships had arrived in the UK and since the loss occurred before arrival, the Commissioners had no insurable interest at the time of the loss and consequently the insurance was void.

COMMENT: Two of the opinions given to the House of Lords have been particularly influential. Lawrence J at p 301 gave a classic definition[45] of the nature of insurance which is worth quoting

[43] The Law Commission in The Second Joint Consultation Paper paras 10.11-10.12 identify three other useful functions for insurable interest, it deters insurance fraud (moral hazard), it protects the insurer from invalid claims and it helps to locate the geographical location of the risk which is important in determining jurisdiction and the proper law of the contract.

[44] (1806) 2 Bos & Pul (NR) 269.

[45] Though as we have seen no 'definition' of insurance has proved satisfactory.

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in full: '[I]nsurance is a contract by which one party in consideration of a price paid to him adequate to the risk becomes security to the other that he shall not suffer loss damage or prejudice by the happening of the perils specified to certain things which may be exposed to them'. In other words the nature of insurance is indemnity against loss so that as Lawrence J points out at p 302 it is in the nature of insurance that the insured should have an interest in the preservation of the subject matter of the contract. However Lawrence J continues 'interest does not necessarily imply a right to the whole or part of a thing . . . but having some relation to or concern in the subject matter of insurance . . . as to have a moral certainty of advantage or benefit [from its continued existence]'.

In contrast Lord Eldon saw the problem as one of finding an adequately precise description of a middle ground between certainty of advantage if the goods remain undamaged, which clearly is an interest, and a mere hope of advantage which clearly is not. He concluded that there was no such middle ground, expressly rejecting the 'moral certainty' test proposed by Lawrence J and determined that, as a result, interest had to be founded on a right in the property or be contractually derived from property rights. Consequently '. . . expectation though founded on the highest probability, was not interest'. He supported this conclusion by pointing out that if 'moral certainty' were adopted as the test then potentially thousands of people would have had an interest in these Dutch vessels from the warehouse keeper who would profit from storing the cargoes to the dock company which would charge for use of the dock, to the stevedores who would be paid to unload the vessels.

The difference between the two approaches is starkly illustrated by the House of Lords decision in *Macaura v Northern Assurance Company*.[46] Here the sole beneficial shareholder and major creditor of a company insured the company's timber, which incidentally was stored on his land, against loss or damage. The goods were destroyed by fire but the insurer refused to pay on the grounds that since a company is a separate legal person apart from its shareholders this amounted to Macaura insuring someone else's property in which he had no interest. The House of Lords held, adopting Lord Eldon's approach that whilst Macaura would clearly suffer a loss in the value of his shares this is not a loss in value of the property insured and consequently since he did not own nor did he have contractual rights deriving from a contract concerning the timber he had no insurable interest and the policy was void.[47]

Notwithstanding the fact that *Macaura* is a House of Lords decision which by strong implication rejects the 'moral certainty' test, later courtshave leaned in favour of finding insurable interest where in effect there is a factual certainty of loss on the part of the insured. Thus in *Sharp v Sphere Drake Insurance Ltd, The Moonacre*[48] the

[46] [1925] AC 619 (HL). On facts very similar to *Macaura* the Canadian Supreme Court in *Constitution Insurance Company of Canada v Kosmopoulos* (1987) 1 SCR 2, found in favour of the insured, adopting the 'moral certainty' test of Lawrence J in *Lucena*.

[47] It has been pointed out that he could have insured the value of his shares. In fact to cover his loss completely he would also have needed insurance against the non-payment of the debt owed to him by the company since the value of the shares would be based on the net value of the company's property, i.e. after payment of debts. Also since he was storing the company's goods he could have insured against his liability to their owner in respect of his failing in his duty of care as bailee. *Macaura* is therefore a good illustration of the principle that a properly constructed property insurance does not cover pure financial loss nor third party liability. For a less well drafted policy (at least from the viewpoint of the insurer) see *National Oil Well (UK) Ltd v Davy Offshore Ltd* [1993] 2 Lloyds Rep 582 (Comm).

[48] [1992] 2 Lloyds Rep 501 (Comm).

property insured was a pleasure yacht owned by a company but insured in the name of the sole shareholder who had also been authorized by the owner to sail and manage the vessel, Deputy Judge Colman held that to amount to an insurable interest a 'right in the insured property' was not confined to property rights but could include a right of enjoyment over the property even though that right was not a property right properly so called.

This extension of the concept of insurable interest seems welcome in *Sharp v Sphere Drake* since the function of ownership of a pleasure boat is not investment but its amenity use and that was exactly what the insured lost. This approach is also entirely consistent with the views of Brett MR who said in *Inglis v Stock*:

> In my opinion it is the duty of a Court always to lean in favour of an insurable interest, if possible, for it seems to me that after underwriters have received the premium, the objection that there was no insurable interest is often, as nearly as possible, a technical objection, and one which has no real merit. . .

The year after *The Moonacre* the by then Colman J, had a further opportunity to extend the concept of insurable interest in *National Oil Well (UK) Ltd v Davy Offshore Ltd.*[49] Here a supplier of goods which were to be incorporated into a major construction project, argued that he had an insurable interest under a 'Constructors' All Risks' (CAR) policy in the property under construction itself. Colman J held that there was nothing in principle preventing this notwithstanding the fact that the supplier had no property rights in the property at all. Clearly, whether the policy in question actually covers the interest that a potential insured might have is dependent on the construction of the insurance policy in the context in which it is taken out, but the possibility of the extension of the concept of insurable interest can have unexpected consequences for insurers which consequences have manifested themselves particularly in the context of co-insurance where as we have seen, several parties are *prima facie* insured under the same policy in respect of different risks.

National Oil Well (UK) Ltd v Davy Offshore Ltd [1993] 2 Lloyds Rep 582 (Comm).

FACTS: National Oil Well (NOW) supplied engineering equipment to Davy Offshore (Davy) which was the main contractor on a project to build an offshore oil production platform. The contract between them provided that Davy should take out and maintain a Constructors' All Risks policy insuring the platform, and under which Davy and NOW were identified as being insured. Davy refused to pay NOW for the goods on the basis they were defective and had caused damage to the platform. Davy had been indemnified by the insurers for this damage under the CAR policy. NOW sued for the price and the insurers, who had been subrogated to Davy's rights, defended the action on Davy's behalf and counterclaimed for negligence and/or breach of contract. NOW in turn argued that because they and Davy were co-insureds under the CAR policy the insurers had no rights of subrogation to Davy's counterclaim. The insurers responded, inter alia that NOW was not a co-insured because they did not have an insurable interest under the policy since they had no property rights in the platform.

[49] [1993] 2 Lloyds Rep 582 (Comm).

HELD: Colman J held that NOW had an insurable interest in the platform because it had potential liability to Davy (or others insured under the policy) if it supplied goods which caused loss or damage to the structure, the risk of being materially adversely affected by loss of or damage to the platform by one of the insured perils was sufficient to found an insurable interest.

COMMENT: This case involves an offshore oil platform and so the contractual arrangements are specific to marine construction projects. A more common circumstance in which CAR policies are to be found is in building developments on land where the developer and the main contractor agree that the main contractor will carry out building works and one or the other of them is required to take out and maintain a CAR policy in the joint names of the developer, the contractor and any sub-contractors who are therefore prima facie co-insured under the policy. Under the terms of the building contract, in the event of damage or loss of the construction works before completion, the contractor must make good the loss or damage and proceed to completion of the building and the developer who will receive the insurance payout must use the money to pay for the work. The purpose of CAR policies is therefore to provide a fund for the reinstatement of the works in the event of their being damaged. Cover is typically extended to cover loss or damage from the insured risks to the building contractor's and sub contractors' property while on site. But as with all 'All Risks' policies, CAR policies are not normally construed to cover all types of *loss*. Thus the policy wording of CAR policies apparently show they are property insurances not loss of profit or liability insurances.[50]

Consequently, on a normal construction of such policies, were a building nearing completion to burn down, an electrical sub-contractor for example might lose cable, tools and equipment in the fire and could make a claim for these (property) loss under the policy. However he could not claim for loss of profit because, for example, he cannot work until the rebuilding is sufficiently advanced as to make it possible to 'fit the electrics'.[51] However in *National Oil Well* Colman J found the distinction between property and liability insurance no obstacle:

> . . . there is no question that the insured [supplier/installer] would have an insurable interest in his potential liability [under a liability policy]. But the fact that he has an insurable interest for that kind of risks (sic) does not lead to the conclusion that he cannot have an insurable interest in the property itself for the purposes of a policy on property risks.[52]

The reason for this is best explained by turning to the example of an electrical sub-contractor referred to in the *National Oilwell* case box above. Typically the insurer will have agreed to indemnify the subcontractor against loss 'in respect of his interest' in the building. Literally the subcontractor has no interest in the building as such but as *National Oil Well* shows he does have an interest in an insurance against his liability to the developer the contractors and other subcontractors for breach of contract or negligence and indeed he would have an interest in policy covering his loss of profits. On normal contractual principles this express promise of indemnity should be construed where possible as having some legal effect—in other words the insurer must be insuring him against something and that must be against these purely financial risks arising if the building is lost or damaged. As Mance J said in *Cepheus Shipping Corp v Guardian Royal Exchange Assurance plc, The Capricorn* if

[50] In fact they will also cover third party liabilities, e.g. claims made by adjoining landowners.

[51] 'Advance(d) Loss of Profits' insurance is available to cover such losses.

[52] At p 611.

insurers 'make a contract in deliberate terms which covers their assured in respect of a specific situation, a Court is likely to hesitate before accepting a defence of lack of insurable interest'.[53]

The typical use of CAR policies is part of a scheme under the industry standard contract called the JCT the intention of which is to avoid lengthy, messy and often inconclusive inquiries into the causes of loss or damage to buildings under construction. The issue raised in *National Oil Well* in relation to insurable interest so far as it affects CAR policies effected under the JCT has gone away as a result of the later decision in *Co-operative Retail Services Ltd v Taylor Young Partnership Ltd*.[54] Here the House of Lords held that CAR policies effected as part of the JCT scheme are part of a contractual arrangement where the employer, main contractor and sub-contractors surrender all rights of suit between themselves in return for the CAR policy being effected. In such circumstances the CAR policy will cover no more than the cost of reinstatement and as a result they have in effect agreed that each party will potentially be left with losses which they cannot recover from one another nor under the CAR. A party wishing to protect himself against other losses must insure them separately.[55] However as Rix LJ pointed out in *Tyco Fire & Integrated Solutions (UK) Ltd v Rolls Royce Cars Ltd*,[56] although the provision in the underlying contract that a co-insurance must be effected may provide very strong evidence that the parties intend to exclude mutual liability for negligence in relation to the subject matter of the insurance, an express term to the contrary would prevail. In such circumstances whether one of the co-insured under such a policy actually has an insurable interest is a matter for construction of the policy and except where the insuring clause of the policy makes it clear that indemnity is given only in respect of damage or loss to the property and no other type of loss there is every reason to construe it as covering such interest that the policyholder has.

This suggestion is based on an analysis of the judgment of Waller LJ in *Feasey v Sun Life Assurance Co of Canada*,[57] and although it should be noted that *Feasey* involved life insurance and not property insurance, nor was it a case of co-insurance, Waller LJ's principles appear equally applicable to property and indemnity insurance and a fortiori to co-insurance cases.

In *Feasey* the Court of Appeal and Waller LJ in particular took the opportunity to analyse 200 years of case law on insurable interest and to the extent possible to reconcile the authorities. Waller LJ divided into cases into four groups as follows, of which one concern life insurance alone:

> Group (1) are those cases where the court has defined the subject matter as an item of property; where the insurance is to recover the value of that property; and where thus there must be an interest in the property—real or equitable—for the insured to suffer loss which he can recover under

[53] [1995] 1 Lloyd's Rep 622 (641). It is well known to insurance market professionals that lack of insurable interest is usually advanced by insurers who either strongly suspect fraud on the part of the insured but cannot prove it (as in *Macaura*) or where the policy wording is deficient and covers far more than the insurer intended (*National Oil Well*). Commercial judges are aware of this and respond accordingly.

[54] [2002] UKHL 17, [2002] 1 WLR 1419.

[55] However, returning to the electrical contractor example, since he has no liability to co-insureds by virtue of the JCT agreement the only other interest he has in the building itself is presumably loss of profits/increased cost of working. Does that mean that CARs must by inference cover such types of loss?

[56] [2008] EWCA Civ 286.

[57] [2003] EWCA Civ 885 [97], [2003] 2 All ER (Comm) 587 [97].

the policy. . .[58] [Group (2) concerns life insurance] . . . Group (3). There are then cases where even though the subject matter may appear to be a particular item of property, properly construed the policy extends beyond the item and embraces such insurable interest as the insured has.[59]. . . Group 4 are policies in which the court has recognised interests which are not even strictly pecuniary.[60]

This analysis is extremely valuable, focussing as it does on the construction of the terms of the policy so as to determine the subject matter of the insurance. Only once this is done is it possible, by considering all of the surrounding circumstances, to determine whether the insured has an insurable interest in the subject matter insured or not. Thus as we have seen in cases such as *National Oil Well* what appears initially to be a pure property insurance covering only property and analogous rights turns out on careful construction to include cover for third party liability. As Waller LJ says: 'It may be more usual to cover liability with liability insurance. But there is no hard and fast rule and where the subject of insurance is intended to be and can properly be construed as embracing the insurable interest in relation to liability, there is no reason not to so construe it.'[61]

Insurable interest and insurance for the benefit of others.

As noted above, Roche J held in *Williams v Baltic Insurance Association of London Ltd*[62] that there is on principle no reason why A cannot effect insurance for the benefit of B either as agent (as seems to be the basis of the decision in *Williams*) or as trustee for B. However whether such an agency or trust relationship actually arises is a matter of fact and as *Vanderpitte v Preferred Accident Insurance Corporation of New York*[63] demonstrates if such a relationship is not in evidence then lack of insurable interest by A in the potential liability of B poses a potentially unanswerable defence to a claim on the policy by A[64] while the lack of privity poses difficulties for an action by B. To a very great extent the Contract (Rights of Third Parties Act) 1999 (CRTPA 1999) provides a solution but it should be recalled that it does not apply 'if on a proper construction of the contract it appears the parties did not intend the term to be enforceable by the third party'.[65] Typically motor policies would promise indemnity to B who could therefore benefit from the CRTPA 1999 but such indemnity is often subject to specific exclusions, e.g. if B is an inexperienced driver or has certain types of criminal conviction.

Reform of Insurable Interest

The origin of the need for insurable interest it has been said lies in statute and does not exist as part of common law[66] and this appears to be the view of the Law Commission.[67]

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58 At [81]. He included *Macaura* and *Lucena* in this group.

59 At [87] He includes *Wilson v Jones* (1867) LR 2 Ex 139 in this group where insurance by a shareholder apparently in the property belonging to the company (a telegraph cable being laid under the Atlantic Ocean) was construed as including insurance of the loss in value of his shares were the cable lost. Cf *Macaura*.

60 At [90]. He includes *The Moonacre* in this group.

61 At [95].

62 [1924] 2KB 282 (HC).

63 [1933] AC 70 (PC).

64 Though surely in the case of motor policies A has an insurable interest in B's liability on the basis that if B is driving with A's consent whilst uninsured, A would be committing a criminal offence and would also be open to direct negligence claims from the injured third party for permitting B to drive whilst uninsured. The problem of course it that whilst A may have an insurable interest he is only indemnified against his own loss and if he is not sued or prosecuted he has no loss.

65 s 1(2).

66 Roche J in *Williams v Baltic Insurance Association of London Ltd* [1924] 2KB 282 (288) (HC).

67 Law Commission 4th Issues Paper on Insurance Contract Law, 11.29–11.34.

The Law Commission's *Issues Paper on Insurance Contract Law* published in March 2015[68] is the last of four such papers seeking views on reform or abolition of the doctrine, at least in respect of indemnity insurance since it adds nothing to the fact that the insured is only entitled to an indemnity for financial loss suffered as a result of the insured event. Thus, goes the argument, if the doctrine of insurable interest were abolished and for example I had insured my neighbour's house against fire, whilst I would have a valid policy, it would provide cover only in respect of my loss caused by the property damage caused by fire to my neighbour's house. Consequently unless I have some sort of property right in my neighbour's house I suffer no loss covered by the policy. Obviously, my house may suffer damage caused by the fire but I would need to have a policy covering loss to my house if I wanted to make a claim for that loss.[69] However there has been strong opposition to the possibility of its abolition and the Law Commission and found little call for clarification or reform in relation to most general insurance has only proceeded to suggest reform in respect of 'insurances of the person like life or health insurance'.[70]

Construction of Policies of Insurance

Introduction

It can be seen from the discussion of insurable interest that a key issue before a successful claim can be made under an insurance policy is whether the policy covers the interest of the claimant. If it does then there is the issue whether the loss was caused by an insured risk which we will deal with in the next section. However before the issue of causation becomes relevant the claimant must show that he has complied with the terms of the policy.

Although in the past the interpretation of insurance policies often seemed to apply subtly different principles to those applied to the interpretation of contracts in general it is now settled that insurance wordings are to be understood using the principles set out by Lord Hodge in *Wood v Capita Insurance Services Ltd*.[71] In other words, on all fours with any other contract.[72] That said there is a particular usage in insurance policies which needs explanation namely the meaning of warranties and conditions.

Conditions and warranties

The common law recognizes that not all terms of contract are of equal importance. Once this position had been established the law initially divided them into two types: conditions, being essential terms, breach of which entitles the innocent party to treat

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[68] Available at http://lawcommission.justice.gov.uk/areas/insurance-contract-law.htm.

[69] Suppose the fire to my neighbour's house causes no damage to my property but reduces the value of my house. Unless the court were to construe my policy on my neighbour's house as covering loss in value to my house (i.e. a 'Group 3' type case under Waller LJ's analysis in *Feasey*) I could make no claim.

[70] The draft bill was published on 20 June 2018. The original bill suggesting extension and clarification of insurable interest was intended to counter the possibility that following the repeal of the Gaming Act 1845 by the Gambling Act 2005, the requirement for insurable interest has been abolished save those covered by the Life Assurance Act 1774 and the Marine Insurance Act 1906.

[71] [2017] UKSC 24; [2017] AC 1173, [10–13].

[72] An excellent summary of the rules for construing insurance policies is to be found in *Bluebon Limited v Ageas (UK) Limited* [2017] EWHC 3301 (Comm) [24]–[30]. See also the case analysis which closes this chapter.

the contract as terminated and/or sue for damages; and, warranties, being subsidiary terms, breach of which only entitles the innocent party to sue for damages. To this have been added 'innominate' terms where the availability of the right to terminate is dependent on the severity of the repercussions of the breach.[73]

Warranties

The division of terms into conditions and warranties (and also apparently innominate terms)[74] also applies in insurance but confusingly here 'warranties' are also fundamental terms and 'conditions' can be subsidiary terms of an insurance contract—warranties are a special type of condition. As s 33(3) Marine Insurance Act 1906[75] states:

> A warranty . . . is a condition[76] which must be exactly complied with, whether it be material to the risk or not. If it be not so complied with, then, subject to any express provision in the policy, the insurer is discharged from liability as from the date of the breach of warranty, but without prejudice to any liability incurred by him before that date.

Typically, before entering into a contract of insurance, the insurer will require the proposed insured to enter into a number of representations which will be expressed as warranties and as s 33 makes clear, failure to meet the requirement for strict compliance with insurance warranties can have profound effects on an insured as for example in *Argo Systems FZE v Liberty Insurance PTE Ltd (The Copa Casino)*.[77] Here the insured's ship was being towed by tug from Mobile in the US to India. The industry standard contract for such a voyage holds the tug's owners and operators harmless and released from any liability to the owner of the vessel. Nevertheless the insurance contract contained an express warranty by the insured that he had not entered into any 'hold harmless' arrangement with tug's owners and operators. Mackie J at first instance held that there had been a breach of the warranty and so prima facie the insurers were automatically discharged from liability. In fact the effect of the warranty was to deprive the insured of materially all benefit of the contract of insurance and the insured argued that in order to give business efficacy to the contract, it was necessary to imply a term that the warranty did not apply to releases which were part of industry standard form agreements. This submission was rejected in only a few lines by Mackie J, because such standard forms can be amended, how would the insurers know whether such an amendment had taken place?[78] The absence of 'hold harmless' and release clauses are potentially important to the insurers since such clauses prevent

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[73] See for example *Cehave NV v Bremer Handelsgesellschaft mbh, The Hansa Nord* [1976] QB 44 (CA).

[74] *Alfred McAlpine plc v BAI (Run Off) Ltd* [2000] Lloyds Rep IR 352 (CA). See also *Friends Provident Life and Pensions Ltd v Sirius* [2005] Lloyds Rep IR 135 (CA). There is some question whether a sufficiently serious breach of an innominate term would only lead to a right to avoid the claim to which the breach relates or the whole policy. See the difference of opinion in *Friends Provident* between Mance LJ and Waller LJ.

[75] Much of the MIA 1906 reflects the Common Law applicable to all contracts of insurance and s33(3) is no exception.

[76] As we shall see this word is in fact misleading.

[77] *Argo Systems FZE v Liberty Insurance Pte Ltd, The Copa Casino*[2011] EWHC 301 (Comm); [2011] 1 All ER.

[78] The warranty in this case was contained in an old version of the standard insurance policy (Institute Voyage Clauses (Hull) 1983 edn). This policy was amended in 1995 so that the warranty no longer applies to releases which the insured is 'compelled' to accept as part of 'customary towage'.

their making subrogated claims against the tug's owners and operators if the loss is caused by their breach of contract or negligence. However neither party raised the question whether the insurer was prejudiced by the breach of warranty—such inquiries are irrelevant, trivial breaches of warranty are enough to terminate the insurer's liability.[79]

The *Copa Casino* also illustrates another feature of the effect of s 33(3). In a non-insurance contract, a breach of a condition gives the innocent party a right to elect either to terminate the contract for repudiatory breach or to affirm the contract. Where, with knowledge of the relevant facts, the party with the right to terminate the contract 'acts in a manner which is consistent only with it having chosen one or other of two alternative and inconsistent courses of action open to it (i.e. to terminate or affirm the contract), then it will be held to have made its election accordingly'.[80] This is known as 'waiver by election'.

However, notwithstanding the use of the word 'condition ' to describe an insurance warranty, s 33(3) makes it clear that a breach of an insurance warranty automatically discharges the insurer from liability at the moment of breach, he need do nothing by way of an election.[81] Consequently there are no rights to waive. In such cases the insured must rely on the doctrine of 'waiver by estoppel'. Waiver by estoppel is subtly different to waiver by election, requiring an unequivocal representation either by act or omission that he will not rely on his legal rights which is acted on by the insured and that it would be inequitable to allow him to rely on them now. Thus in the *Copa Casino*, Mackie J held that the failure by the insurer for seven years to inform the insured that it would be relying on the 'hold harmless' clause estopped it from pleading the point. He was reversed on this point on appeal, an unequivocal representation that a defendant would not enforce his rights arising from the breach, was needed and mere silence without more was not enough.[82] By contrast Judge Richard Seymour QC in *Tele2 International Card Company v Post Office Ltd* held that a delay of just under a year in enforcing a contractual right to terminate a non-insurance contract would have amounted to a waiver by election of that right but for a contractual provision to the contrary.[83]

Similarly in the case of termination of a non-insurance contract for breach of a condition or other contractual provision permitting it the innocent party is discharged from future performance from the point of termination with a claim for damages for breach in respect of any recoverable loss for breach. A breach of an insurance warranty relieves the insurer of liability from the moment of the breach so that payments made in respect of claims under the policy where the casualty occurred after the breach are recoverable.

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[79] See e.g. *Overseas Commodities Ltd v Style* [1959] 1 Lloyds Rep 546 (QBD) (Comm)—breach of warranty in a contract for the carriage of goods by sea that tins of pork shoulder would be date stamped—insurer relieved of liability.

[80] *Tele2 International Card Company SA and others v Post Office Ltd* [2009] EWCA Civ 9 [52] Aikens LJ summarizing Lord Goff in *Motor Oil Hellas (Corinth) Refineries SA v Shipping Corporation of India (The Kanchenjunga)* [1990] 1 Lloyd's Rep 391 (397–399).

[81] See *Bank of Nova Scotia v Helenic Mutual War Risks Association (Bermuda) Ltd (The Good Luck)* [1992] 1 AC 233 (HL).

[82] [2011] EWCA Civ 1572,[2012] 2 All ER (Comm) 126.

[83] A so called 'non-waiver clause'. He was reversed on appeal ([2009] EWCA Civ 9, [2009] All ER (D) 144 (Jan)) but not on the effect of delay.

Equally it is of no consequence that there is no causal connection between the loss occasioning the claim so that failure for example to inspect a fire sprinkler system every month normally would be sufficient to permit the insurers to deny liability for storm damage. This would remain true even if only one inspection had been a few days late and thereafter inspections had been on schedule up to the date of the casualty.[84] It is immaterial to the insurer's rights that the breach has been remedied. The most dramatic instance and origin of this rule is *De Hahn v Hartley*[85] where there was a warranty that a ship would leave Liverpool with a crew of at least 50. The purpose of the warranty was a protection against the ship being captured by pirates on its way to the West Indies. It left with a crew of 46 but picked up another six sailors within six hours of sailing but was lost to pirates much later in the voyage. Lord Mansfield held that warranties must be complied with strictly and the insurers were discharged from liability.

In the process of seeking insurance, the insured will be required to disclose a range of matters to the insurer. Some of these may prove important to the insurer, others not so, some may be expressed as warranties, others not. Under normal contractual conditions such disclosures would amount to representations not terms of the contract. However, it became a common practice among insurers to insert what are called 'basis of the contract clauses' in insurance policy wordings. Under such clauses the truth of all representations made by the insured in the proposal process, however expressed are made conditions precedent to the liability of the insurer. Thus even innocent misrepresentations of matters however immaterial and however unconnected with the any loss discharged the insurers from liability.[86] So for example in *Dawsons Ltd v Bonnin*[87] the insured inadvertently declared on the proposal form that the lorry which was the subject matter of the insurance was parked overnight at its business premises when in fact it was parked some miles away in a location which reduced the risk of loss. Nevertheless the House of Lords held that the basis of the contract clause permitted the insurer to refuse a claim while expressing regret that the law required this conclusion.

The response of the courts to extensive insurance warranties

The courts have adopted a range of techniques seeking to ameliorate the strictness of the law on insurance warranties.

Firstly the doctrine of contra proferentem was often applied so that any lack of clarity in an insurance wording was construed against party who drafted it—namely the insurers. Thus in *Cornhill Insurance v D E Stamp Felt Roofing*[88] clause 3 of the policy made it a condition precedent to liability that the insured had a particular procedure for reducing the likelihood of fires caused during the use of propane fuelled heaters of roofing tar. The insured had such a procedure but did not follow it and a fire ensued. In giving the main judgment in the Court of Appeal Longmore LJ made clear the rationale for the decision that the insured had complied with the condition when he said:

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[84] Though in *Kler Knitwear Ltd v Lombard General Insurance Co Ltd* [2000] Lloyds Rep IR 47 from which this example was taken Morland J held that, on proper construction, the contractual term was simply a suspensory warranty which once remedied was of no effect save in respect of casualties occurring during the period of breach.

[85] (1786) 1 TR 343.

[86] See the analysis of Jackson LJ in *Genesis Housing Association Ltd v Liberty Syndicate Management Ltd* [2013] EWCA Civ 1173,[2013] WLR D 368

[87] [1922] 2 AC 413 (HL).

[88] [2002] EWCA Civ 395.

Taking condition 3 as a whole, it is, in my view, a condition precedent to liability merely that arrangements have been put in place not that they are in fact complied with. . . . In construing the policy, one has to bear in mind that condition 3 is a condition precedent to liability. If it is not complied with, insurers can escape liability even if the failure to comply with the condition does not in any way cause the loss.

However in line with the *Wood v Capita* principles, in relation to the contra proferentem doctrine there has been a return to the orthodoxy set out by Lord Lindley in *Cornish v Accident Insurance Co Limited*[89] where he said:

. . . in a case of real doubt, the policy ought to be construed most strongly against the insurers; they frame the policy and insert the exceptions. But this principle ought only to be applied for the purpose of removing a doubt, not for the purpose of creating a doubt, or magnifying an ambiguity, when the circumstances of the case raise no real difficulty.

Secondly the courts construed some terms as merely as suspending the insurer's liability until the breach was remedied notwithstanding clear language indicating the contrary. For example in *Kler Knitwear Ltd v Lombard General Insurance Co Ltd*[90] the insured renewed an existing policy for a further year and warranted that the sprinkler system at its factory would be inspected by a competent engineer within 30 days of renewal and that all recommended rectification work commissioned within 14 days of the engineer's report. In fact the inspection was not carried out for 60 days. The factory was later damaged by a storm and the insurers rejected a claim for the losses it caused on the basis that the sprinkler warranty had been breached. The policy contained this clause:

Every Warranty . . . shall apply during the whole currency of this Insurance and non-compliance . . . whether it increases the risk or not, or whether material or not to any claim shall be a bar to any claim . . . provided that whenever this Insurance is renewed a claim in respect of Damage occurring during the renewal period shall not be barred by reason of . . . (non compliance with a Warranty) at any time before the commencement of such period.

Morland J held that the sprinkler warranty was suspensory only so that once remedied the warranty no longer barred a claim notwithstanding the fact that this interpretation required the proviso quoted above to be ignored.

Thirdly in some instances the courts have construed particular warranties as applying only to some of the risks covered in the policy. Thus in *Printpak v AGF Insurance Ltd*[91] the policy provided for the insured to select from a range of covers for a number of risks for example loss through explosion, impact, fire and theft and each type of risk was set out in a separate section. The insured selected both fire and theft covers. Amongst the warranties in the theft section was one that a burglar alarm was fitted to the premises and was fully functional at all time the building was unoccupied. The insurers denied liability for fire damage as the alarm was switched off at the time of the incident. The Court of Appeal concluded that on a true construction, even though the alarm warranty was not specifically confined to theft cover, that was the effect of the sectional policy. Thus the requirement that a burglar alarm be fitted was a risk specific warranty which would only affect burglary claims and not act as a condition precedent to liability under the policy.[92]

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[89] (1889) 23 QBD 453.

[90] [2000] Lloyds Rep IR 47.

[91] [1999] 1 All ER (Comm) 466 (CA).

[92] There is an excellent summary of the differences between suspensory warranties, conditions precedent to liability and risk specific warranties in *Bluebon Limited v Ageas (UK) Limited* [2017] EWHC 3301 (Comm) [10]—[12].

Finally, as we have seen, the courts have used the express terms of s 34(3) MIA 1906 that an insurer can waive the benefit of a breach of warranty by virtue of the doctrine of estoppel by an unequivocal representation by the insurer that it will not rely on the fact that the contract is void, relied on by the insured, such that it would be inequitable for the insurer, later to rely on the nullity point. Typically the representation will be by action but must be unequivocal. Common examples would be that with full knowledge of the breach[93] the insurer continued to accept premiums or processes a claim.

Conditions

Insurance wordings may make certain matters 'conditions precedent' to the validity of the contract. As the wording suggests, breach of such a term has serious consequences for the insured. In consequence the courts will generally avoid construing conditions precedent to validity even where the words of the policy are apparently clear.[94]

Kazakstan Wool Processors (Europe) Ltd v Nederlandsche Credietversekering Maatschappij NV [2000] Lloyds Rep IR 371 (CA).

FACTS: The insurers, Nederlandische, insured KWP against the risk that buyers of their wool defaulted in payment. The premium was payable monthly calculated as a percentage of the value of the wool exported the previous month. KWP had a duty to report the value of all such exports (including nil returns) by the 10th of each month during the 14 month term of the policy. Majorbuyers of KWP's wool defaulted and KWP notified Nederlandische as required by the policy in May 1998. It then ceased trading so that it exported no wool in June 1998 but did not make a 'nil return' by 10 July. On 11 July 1998, Nederlandische sought to 'disclaim all liability' under the policy relying on the following provision:

> the due performance and observance of every stipulation in the policy . . . shall be a condition precedent to any liability on our part. In the event of any breach of any condition precedent we also have the right to retain any premium paid and give written notice terminating the policy and all liability under it . . .

If this term were construed literally, the insurer could retroactively cancel cover so that it would have no liability for the apparently insured losses suffered by KWP prior to the technical breach of the duty to report the value of exports in the previous month. KWP argued that the provision did not operate retroactively and merely suspended liability until the breach was remedied which once done would reactivate the insurer's liability for future claims.

HELD: If as Nederlandische argued the term were construed literally then it would only be at the end of the policy term that it could be determined whether KWP had complied with its monthly reporting duties. This could not be what the parties had contemplated as the effect of the disputed term. Consequently it could not extinguish liability for losses incurred before termination. However the term was clear that once notice of termination had been served, liability for all future losses was extinguished.

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[93] Constructive notice through being out on inquiry is not enough (*Hadenfayre Ltd v British National Insurance Society Ltd* [1984] 2 Lloyds Rep (HC) 393,400 Lloyd J).

[94] *Kazakstan Wool Processors (Europe) Ltd v Nederlandsche Credietversekering Maatschappij NV* [2000] Lloyds Rep IR 371 (CA).

COMMENTARY: The approach of Waller LJ is instructive for a number of reasons. Firstly there is a clear determination to apply a contra proferentem construction to the disputed term. The fact that a literal interpretation gave rise to the fact that the insurer's liability could not crystalize until the end of the policy term was sufficient to justify a more nuanced interpretation notwithstanding Nederlandische's contention that the effect of the term was that the insurer must pay claims as reported but with a right of reimbursement should a breach occur in the future. Secondly, the fact that Waller LJ did not accept that KWP's second argument that the term was merely suspensive of liability shows that where terms are clear the court will apply them however unattractive the result. Here it was clear to both parties that the claims notified in May were the first of many and that the sums payable by Nederlandische would be very substantial. Without doubt Nederlandische was alert to any breach, however trivial by KWP, so as to reduce or eliminate its liability. Nevertheless, Waller LJ felt bound to give effect to the clear wording that liability for the anticipated losses ceased from the date of the notice of termination. Finally the case demonstrates how much skill is involved in drafting policies—even apparently clear wordings can, when subjected to concentrated analysis by experienced lawyers, become ambiguous and give rise to anomalous results.

Insurance conditions may, instead of being conditions precedent to validity of the whole contact be simply precedent to liability for a particular claim. For example, in *Kazakstan Wool Processors*,[95] as with most policies, the insured was under a duty to report losses insured under the policy immediately it became aware of them. Rather unusually the policy sought to make a breach of that duty, and any others, a condition precedent to *validity*. Typically however policies will express such a duty either as a 'condition precedent' or as a 'condition precedent to liability' or as a 'condition precedent to recovery'. The result of a breach of such a term whichever wording is used will be to invalidate the late notified claim but not the policy as a whole so that the insured may retain payments made for prior losses and make claims in respect of losses in the future.[96]

Finally conditions may simply be collateral provisions, breach of which sound in damages. In other words conditions which are not conditions precedent are in effect in insurance law, the same as warranties are elsewhere in the law of contract.

As we have seen, breach of a condition precedent gives the insurer (depending on the type of condition precedent) an option either to affirm the contract and waive his rights to rely on the breach or to terminate the policy (condition precedent to validity) or to deny a particular claim (condition precedent to liability). It should be noted that this is different to a breach of warranty where the policy automatically terminates without any action on the insurer's part. In consequence the doctrine of waiver properly so called applies to breaches of condition precedent. Although otherwise sharing common characteristics with estoppel, waiver does not require the insured to act in reliance of an unequivocal representation by the insurer. However it does require the insurer to act in such a way as to show that it has opted to affirm the contract in full knowledge of the facts giving rise to the option. To illustrate the distinction imagine a policy which indemnifies a manufacturer against damage to a factory. The policy

[95] *Kazakstan Wool Processors (Europe) Ltd v Nederlandsche Credietversekering Maatschappij NV* [2000] Lloyds Rep IR 371 (CA).

[96] *Hood's Trustees v Southern Union General Insurance Co of Australasia* [1928] Ch 792 (CA).

states that the insured must notify the insurer immediately, if as a result of the incident giving rise to the loss, he is to be prosecuted for breach of health and safety legislation. Suppose the Health and Safety Executive serve notice of intending prosecution on the manufacturer and copy the notification to the insurer. Two or three days later, since the manufacturer has not given notice of the prosecution, the insurer writes and asks why the manufacturer has not made the necessary notification. In such a case, if the policy had imposed a notification *warranty* then the insurer would not be estopped from relying on the invalidity of the contract until the insured had acted on the clear representation in the letter that it was treating the policy as valid. The insured would also have to show that as a result of the detrimental reliance it would be inequitable for the insurer to plead invalidity. However, if the policy had imposed a condition precedent to liability, the insurer has almost certainly affirmed the contract and waived its rights arising from the breach.

Changes in the law: Warranties

Subject to a right of opt out in respect of non-consumer insurance,[97] for contracts of insurance or variations to such contracts, entered into on or after 12 August 2016, a new legal regime applies to a number of the issues discussed above. From that date:

1. By virtue of s9(2), representations made in respect of a proposed non-consumer insurance contract (or a variation to it) cannot be converted into a warranty by means of any contractual provision, whether contained in the insurance contract or otherwise. Consequently basis of the contract clauses are of no effect. The Law Commission asserts that the effect of s9 is not to deprive insurers of the benefit of 'including conditions which are so fundamental that breach by the insured should discharge the insurer from all liability' but warns that the insurer should ensure that the consequences of breach 'are set out fully in the contract' and sufficient steps should be taken to draw the insured's attention to it.'[98]

With respect to the Law Commission this is not what the section actually says[99] and it remains to be seen whether the courts construe s9 as applying only to the blanket conversion of representations into warranties (thought the section does not seem expressly to be so confined) or more widely. In any event even where a warranty is held to fall foul of s9 the insurer can still rely on the fact that any misrepresentations may breach the duty of fair disclosure.

2. By virtue of s10the rule that, where there is a breach of warranty by the insured, the insurer is automatically discharged from liability is replaced with one that liability of the insurer is suspended during the period of the breach but is revived should the breach be remedied.

As well as obvious cases of remedy, S10(5) and (6)ensure that even where literally a breach cannot be remedied - for example because it requires that at a certain time something is to be done and it is not done or something is the case and it is not - so long as'the risk to which the warranty relates later becomes essentially the same as that originally contemplated by the parties' - the breach is nevertheless remedied.By way of illustration, had s10 applied in *De Hahn*the outcome would have been different.

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[97] For the right of opt out in non-consumer insurance see below.

[98] Law Commission, *Insurance Contract Law: Business Disclosure; Warranties; Insurers' Remedies for Fraudulent Claims and Late Payment*(Law Com No 353, 2014) para 14.22.

[99] It should be noted that by virtue of s16(1) the parties cannot contract out of the effect of s9.

The warranty required a crew of 60 when the ship set sail. Once the ship left Liverpool undermanned nothing could be done, literally, to remedy this breach. Nevertheless once the shortfall had been made up,there would be no difference to the risk of being taken by pirates whether the men had been on boardfrom the beginning of the voyage or not. Consequently the initial breach would be remedied for the purposes of s10 (5).

Insurance Act 2015, s 10—Breach of Warranty

(1) Any rule of law that breach of a warranty (express or implied) in a contract of insurance results in the discharge of the insurer's liability under the contract is abolished.

(2) An insurer has no liability under a contract of insurance in respect of any loss occurring, or attributable to something happening, after a warranty (express or implied) in the contract has been breached but before the breach has been remedied.

(3) But subsection (2) does not apply if—
   (a) because of a change of circumstances, the warranty ceases to be applicable to the circumstances of the contract,
   (b) compliance with the warranty is rendered unlawful by any subsequent law, or
   (c) the insurer waives the breach of warranty.

(4) Subsection (2) does not affect the liability of the insurer in respect of losses occurring, or attributable to something happening—
   (a) before the breach of warranty, or
   (b) if the breach can be remedied, after it has been remedied.

(5) For the purposes of this section, a breach of warranty is to be taken as remedied—
   (a) in a case falling within subsection (6), if the risk to which the warranty relates later becomes essentially the same as that originally contemplated by the parties,
   (b) in any other case, if the insured ceases to be in breach of the warranty.

(6) A case falls within this subsection if—
   (a) the warranty in question requires that by an ascertainable time something is to be done (or not done), or a condition is to be fulfilled, or something is (or is not) to be the case, and
   (b) that requirement is not complied with.

(7) In the Marine Insurance Act 1906—
   (a) in section 33 (nature of warranty), in subsection (3), the second sentence is omitted,
   (b) section 34 (when breach of warranty excused) is omitted.

We can also refer to the warranties in *Sugar Hut Group v Great Lakes Reinsurance*[100] as illustrative of how these provisions of the 2015 Act might operate. Here an insurance policy covered four nightclubs with a common owner against a range of risks including fire. Among the warranties, which are typical provisions in an insurance of commercial premises where cooking takes place, were that the ducting through which air from the kitchens was extracted would not be in contact with combustible material,

[100] *Sugar Hut Group Ltd and others v Great Lakes Reinsurance (UK) plc and others* [2010] EWHC 2636 (Comm), [2011] Lloyds Rep IR 198.

would be inspected every six months and cleaned every two months. In addition, the insured warranted that the kitchen refuse bins in the yard at the rear of the premises would be made of metal and a burglar alarm of a particular specification would be fitted. The nightclub in Brentwood burnt down but the insurers denied liability inter alia for breach of warranties.[101] In *Sugar Hut* each of these warranties were broken and remained un-remedied at the time of the fire, however, had there only been previous gaps in the inspection and cleaning routines of the ducting but at the time of the fire they were back on schedule, then ss 10 (5) and(6) would ensure that at the time of the fire the insurers were back on risk. Similarly in *Sugar Hut*, the burglar alarm was required to be connected to a central alarm centre run by a particular provider. In fact it was simply connected to an employee's home, but had it initially been connected to the employee's home but later was redirected to a central alarm centre run by an equally reputable provider to that specified in the warranty, then ss10 (5) would have the effect of treating the breach as remedied and the insurers would resume cover.

Changes in the law: Warranties and conditions the effect of breach[102]

The 2015 Act was preceded by a long process of consultation by the Law Commission. There were strong representations to the Commission that insurers should not be able to escape liability where an insured could show that the breach of warranty did not cause the loss for which they were claiming. This is the position in New Zealand and other Commonwealth jurisdictions. Ultimately the Commission rejected this proposal on the basis that such a move would precipitate lengthy and potentially expensive investigations into causation of casualties, in favour of what is now contained in s 11 of the Act.

Insurance Act 2015, s11—Terms not relevant to the actual loss

(1) This section applies to a term (express or implied) of a contract of insurance, other than a term defining the risk as a whole, if compliance with it would tend to reduce the risk of one or more of the following—
 (a) loss of a particular kind,
 (b) loss at a particular location,
 (c) loss at a particular time.

(2) If a loss occurs, and the term has not been complied with, the insurer may not rely on the non-compliance to exclude, limit or discharge its liability under the contract for the loss if the insured satisfies subsection (3).

(3) The insured satisfies this subsection if it shows that the non-compliance with the term could not have increased the risk of the loss which actually occurred in the circumstances in which it occurred.

(4) This section may apply in addition to section 10.

[101] This nightclub had been a regular backdrop to episodes of the TV 'reality' show 'The Only Way is Essex'.

[102] Owing to the breadth of the legislation it seems s 11 would also apply to innominate terms.

By virtue of this section an insurer cannot avoid liability by reason of a breach of warranty or any other term of the contract if the insured can show that the term is not relevant to the kind, time or place of loss.[103] However whether the breach actually contributed to the loss is irrelevant. By way of illustration in *Sugar Hut* the warranty over the kitchen bins and the contact of the ducting with combustible material had both been breached at the Brentwood club where the fire took place. Clearly each warranty was aimed at reducing the risk of fire but the breaches did not contribute to the actual fire which consumed the premises. Were these facts to recur it is not clear whether under the new law the insurer could rely on the breach of warranties or not. The fact the breach had no causal connection the fire (which was probably the result of arson)[104] is obviously irrelevant under s 11. Equally clearly, compliance with the warranty would tend to reduce the risk of fire at any time thus satisfying ss 11(1)(a) and (c). What is less clear is what is meant by 'particular location' in s 11(1)(b). How specific does the location have to be? If for example the seat of the fire had been in the bar, would it matter that the warranties were not directed at reducing the likelihood of fire in the bar but in the kitchen and back yard respectively? Taking this further, in *Sugar Hut* one policy covered four geographical locations. Could breaches of warranties at say the Fulham club have been relied on by the insurers in respect of a loss at Brentwood even though there were no similar breaches at that location? The Law Commission's delphic conclusion on this latter point is that 'the outcome depends on whether the courts would apply a single warranty to different locations' while stating that they believed that the insurers ought not to be absolved from liability in such a case.[105]

What is clearer is that were *Kazakstan Wool Processors*[106] to recur, regardless of the characterization of the term requiring notification of the amount of wool exported in the previous month, the insurer could not have avoided liability for claims in respect of losses notified prior to the breach nor in respect of subsequent losses since the breach was unconnected with the risk of loss. Clearly the *amount* of wool exported does affect the likelihood of loss but the *breach* (non-notification) does not.

The effect ss 10 and 11 Insurance Act 2015

Clearly, in respect of policies to which ss 10 and 11 apply, some of the more draconian repercussion of insurance warranties and conditions precedent will no longer occur. However these sections are not revolutionary but evolutionary in effect.

Firstly where a breach of warranty or condition precedent occurs which could 'have increased the risk of the loss which actually occurred in the circumstances in which it occurred'[107] then, presumably, even if the increase is small, the impact on the validity of the policy or of the claim will not be. The effect of breaches of warranties and conditions precedent remains avoidance of policy or claim not adjustments in the amount payable to reflect the causal connection between the breach and the loss incurred.

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[103] Law Commission, *Insurance Contract Law: Business Disclosure; Warranties; Insurers' Remedies for Fraudulent Claims and Late Payment* (Law Com No 353), 2014, para 18.39.

[104] See http://www.mirror.co.uk/3am/celebrity-news/sugar-hut-owner-mick-norcross-4470730 accessed 13 13th July 2015.

[105] Law Commission, *Insurance Contract Law: Business Disclosure; Warranties; Insurers' Remedies for Fraudulent Claims and Late Payment* (Law Com No 353), 2014, paras 18.67 and 18.68.

[106] *Kazakstan Wool Processors (Europe) Ltd v Nederlandsche Credietversekering Maatschappij NV* [2000] Lloyds Rep IR 371 (CA).

[107] s 11(3).

Secondly the burden of proof is on the insured to show he falls inside s 11(3) so that he must show that the breach *could* not have increased the risk of the loss[108] that actually occurred. Returning to *Sugar Hut*[109] for a moment, the investigation following the incident concluded that the cause of the fire was probably arson but although a man was arrested for the crime there was no prosecution. If the investigation had been even slightly less specific, the inclusion of the word 'could' in s 11(3) would have meant that the insured would have had to show that the building would still have been as extensively damaged even if the bins had been metal and the ventilation filters had been clean and isolated from combustible material. Determining causation, particularly causation in respect of the extent of a loss is notoriously difficult. In many instances despite extensive expert scientific examination, the results are inconclusive leaving the insured in no better position under the 'new' law since proving that something could not have contributed to the loss will be impossible on the balance of probabilities and will inevitably lead to 'battles of the experts'.

Finally, lest it be thought that after the 2015 Act comes into effect we can treat older cases as of historical interest only, the 2015 Act provides for the parties to opt out of the effect of ss 10 and 11 (though not s 9) in the case of non-consumer insurance.[110] It is therefore for the parties to decide whether the 'new' law will apply to them or not. This issue is covered in more detail below.

Although there do seem to be some difficulties in determining how the Insurance Act 2015 is to be interpreted in relation to warranties and conditions, currently there are no reported cases on it, though there are a number which while applying the 'old law' point out that the outcome would have been no different under the Act.[111]

Cover and causation under contracts of insurance

Introduction

We have seen so far, especially when considering the matter of insurable interest that there are different types of risk which may be insured for example property risks, i.e. insurance against the loss in value of the insured property, and 'pure' financial losses such as loss of profits, third party liability, additional costs of working or legal and other professional expenses voluntarily incurred; in each instance caused[112] by specified events giving rise to such losses. Since the insurer has liability under a policy only in respect of risks insured under the policy and we can appreciate that liability is dependent on:

1. The type of risk the policy covers; and
2. Whether the loss arises out of events the policy specifies as being covered.

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[108] It should be noted that I have assumed that 'risk of loss' means both the risk that the loss occurred at all and the extent of the loss. The words certainly bear that meaning.

[109] *Sugar Hut Group Ltd and others v Great Lakes Reinsurance (UK) plc and others* [2010] EWHC 2636 (Comm), [2011] Lloyds Rep IR 198.

[110] s 16 Insurance Act 2015.

[111] See for example *Dalecroft Properties Limited v Subscribing Underwriters* [2017] EWHC 1263 (Comm).

[112] In fact a range of wordings showing that the loss must be connected to a specified event or events may be used in the policy.

In other words, we can say that insurers assume the risk of loss of a type or types specified in the policy caused by the event or events specified in the policy. This section focuses on the second of these two factors.[113]

Proximate cause

Consider the following example.

Eg COMCORP LTD

ComCorp has an insurance policy which insures it against damage to its goods caused by fire. A fire breaks out and flames destroy the contents of the factory. Smoke from the fire enters ComCorp's warehouse ruining the goods stored there. The Fire Service is called and manages to rescue some of the contents of the ComCorp's offices which are put on the pavement in front of the buildings from where they are stolen. Finally as a result of water which the Fire Service sprayed onto the offices in order to prevent the fire from spreading from the factory, a valuable collection of watercolour paintings is destroyed. It is now clear that the fire would not have affected the office buildings regardless of whether they had been doused in water or not. Which, if any, of these losses are covered by the policy?

The destruction of the contents of the factory is clear enough—the loss was obviously caused by the fire. But what if the fire had been lit by an arsonist, surely the loss is caused by the criminal: after all, if instead of burning the factory down he had stolen the contents, then there would have been no insurance cover. What about the contents of the warehouse? Obviously they were not damaged by fire but by smoke caused by the fire. How directly does the insured risk have to be connected with the loss for there to be coverage? This leads us to the goods stolen from the pavement. But for the fire they would not have been stolen but they were not damaged by fire, surely (to adopt an expression more commonly used in tort and criminal law) the theft is a break in the chain of causation? Finally the watercolours, but for the fire there would have been no loss. Is that sufficient for the fire to have caused the loss?

The courts have always approached the question of causation by in effect asking 'what did the insurer and the insured agree should be covered?' However the approach in answering the question has changed over the years.[114] In the nineteenth century the courts tended to adopt a test which treated the parties as intending to cover losses caused by the occurrence closest in time to the loss. This was called the 'proximate' cause. On that basis the losses in the factory, though initiated by an arsonist would have been covered[115] but probably not the other losses.[116]

[113] What follows is an expanded version of what appears in Chapter 22 but with alternative examples.
[114] See for example Malcolm Clarke 'Insurance: The Proximate Cause in English Law' [1981] CLJ 284.
[115] *Gordon v Rimmington* (1807) 1 Camp 123.
[116] See the problems for the court as late as 1906 with smoke and water damage accompanying a fire in *The Diamond* [1906] P 282 (PDA). See *Marsden v City and County Insurance Co* [1865] LR 1CP 232 on thefts from the pavement.
[117] [1918] AC 350 (HL).

However, it was finally accepted by the House of Lords in *Leyland Shipping v Norwich Union Fire Insurance Society Ltd*[117] that, while from Aristotle[118] onwards, philosophers had argued about what might cause an event, for legal purposes the proximate cause is not necessarily the most proximate in time to the loss, but 'proximate in efficiency'[119] that is 'what was the effective cause of the loss?' But are we much further forward with this formulation, in particular by what criteria is the effect of the causes to be assessed?

The answer seems to be reference to the 'common sense and intelligence of the common man'.[120] To the same effect is *Noten v Harding*.[121] Here a cargo of leather gloves were damaged when moisture in the gloves was evaporated during the daytime as the metal container in which they were stored was heated by the natural effects of the sun. At night, as the air cooled, the moisture in the atmosphere of the container condensed and formed droplets of water on the steel sides and roof of the container which 'rained' down on the gloves ruining them. In the process of deciding whether the damage to goods was caused by the goods themselves or by an external cause, Bingham LJ asked: '[W]hat was the real or dominant cause of that damage? Unchallenged and unchallengeable authority shows that this is a question to be answered applying the common sense of a business or seafaring man.'[122] But as he then remarked 'the parties to the appeal put different answers into the mouth of this hypothetical oracle'. That said the Court of Appeal decided unanimously that the proximate cause was the moisture in the gloves—they had damaged themselves. Exactly the opposite conclusion had been reached in an almost identical case 60 years earlier[123] which although distinguishable from *Noten* is probably best explained as reflecting a different view of causation.

On this basis each of the losses ComCorp suffered in our example above would be covered and this certainly accords with common sense. In fact a range of wordings showing that the loss must be connected to a specified event or events may be used instead of 'caused', for example 'arising out of' [specification of event] or 'reasonably attributable to [specification of event]'.[124] However these will nevertheless still import the proximate cause test on the basis that the test can only be ousted by clear words providing an alternative.[125] Often a better strategy for an insurer is to express the main insuring clause simply and apparently widely but then to limit its scope through a set of carefully drafted exclusions.[126]

However, whilst there is a 'homely' feel about a test based on the common sense of the common man, it must be doubtful whether it is an appropriate tool for assessing the intentions of experienced operators in the insurance market. It must be correct

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[118] See William Charlton, *Aristotle Physics Books I and II* (Clarendon Press 1983) 193.

[119] *Leyland Shipping v Norwich Union Fire Insurance Society Ltd* [1918] AC 350 (HL) 369 (Lord Shaw).

[120] Lord Greene MR in *Athel Line Ltd v Liverpool & London War Risks Insurance Association Ltd* [1946] 1 KB 117 (CA) 122.

[121] *TM Noten BV v Harding* [1990] Lloyd's Rep 283 (CA).

[122] ibid 288. For a more detailed consideration of the issues, see p XXX.

[123] *CT Bowring & Co Ltd v Amsterdam London Insurance Co* (1930) 36 Ll LR 309.

[124] This latter expression for example is adopted by the Institute Cargo Clauses which are considered at length in Chapter 22.

[125] *Coxe v Employers' Liability Assurance Corpn Ltd* [1916] 2 KB 629 (CA) 634 Scrutton J. See *Lawrence v Accidental Insurance Co Ltd* (1881) 7 QBD (HC)—coverage of death but only where accident was the 'direct and sole' cause of death—wording simply imported the proximate cause test.

[126] See for example *Wayne Tank & Pump Co Ltd v Employers' Liability Assurance Corpn Ltd* [1974] QB 57 (CA).

that if the specific meaning of a particular wording has been accepted by the market, that must be what the parties intended even if it does not correspond with common sense, at least where the insured was represented by an experienced insurance broker.

Until comparatively recently the courts looked for a dominant cause of a loss and having found it treated this as the proximate cause of the loss, but in the last 40 years it has been accepted that in some cases there may be two or more proximate causes. The issue arises of how to deal with such cases, and the answer depends on what the policy covers and what it excludes from coverage.

Wayne Tank & Pump Co Ltd v Employers' Liability Assurance Corpn Ltd[1974] QB 57 (CA)

FACTS: Wayne Tank designed and installed equipment for transporting liquid wax in the factory of Harbutt's Plasticine. They were covered by a public liability policy with Employers' Liability Ltd under a main insuring clause, for legal liability 'consequent upon . . . damage to property as a result of accidents' happening at the factory. This coverage was subject to a clause excluding liability 'consequent on damage caused by the nature or condition of any goods . . . supplied by [the insured]'. The equipment Wayne Tank installed was totally unsuitable for its purpose. A fire broke out in the factory and Harbutt's successfully sued them for damages for breach of contract. In that action the court held there were two causes of the fire (1) the dangerous nature of the equipment, and (2) Harbutt's employee leaving the equipment unattended. Wayne Tank claimed on the public liability policy.

HELD: The Court of Appeal held unanimously that Employers' Liability Ltd was not liable under the policy. Lord Denning MR and Roskill LJ held that in cases where there were two competing causes the proximate cause of a loss is the dominant or effective cause even if it was more remote in time. Here the dominant and effective cause of the fire was the dangerous nature of the equipment. Cairns LJ however held that here there were two proximate causes. The loss from both causes fell inside the main insuring clause but the loss from one of the causes fell within the exclusion clause. In such a case the insurers were entitled to rely on the exception and were not liable for the loss.

COMMENT: Lord Denning MR and Roskill LJ followed the traditional approach of determining *a* dominant cause and whether the case was viewed by a 'common man' or by an insurance professional it is clear that neither party could have contemplated the policy covered a loss like that actually incurred. Cairns LJ adopted a novel approach accepting the possibility of two (or more) proximate causes and solved the difficulty this finding caused in this case through a common sensical construction of the policy

The position seems to be this:

- If there are two causes of the loss, both covered by the insuring clause but one is the subject of a specific exclusion, the policy does not cover the loss.[127]
- If there are two causes of loss, one covered by the insuring clause, the other neither covered nor specifically excluded either, the policy covers the loss.[128]

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[127] Cairns LJ in*Wayne Tank & Pump Co Ltd v Employers' Liability Assurance Corpn Ltd*[1974] QB 57 (CA).

[128] *JJ Lloyd Instruments Ltd v Northern Star Insurance Co Ltd (The Miss Jay Jay)* [1987] 1 Lloyds Rep 32 (HC). Overruled in effect as to its interpretation of the policy in question by *Global Process Systems Inc and another v Syarikat Takaful Malaysia Berhad, The Cendor MOPU* [2011] UKSC 5.

To make any further assertions in relation to cases involving more than one proximate cause would be foolhardy in the light of the concerns evident in Lord Mance's judgment in *The Cendor Mopu*[129] and even these two statements must be made tentatively. It may be that future decisions will conclude that the rules differ between property and liability insurances and whether the causes are concurrent as in *The Miss JJ*[130] or consecutive as in *Wayne Pump*.

Finally in relation to causation there is the issue of the effect of the impact of the insured's actions if they form part of the chain of causation. These actions can be divided into three types. Firstly where the insured intentionally caused the loss, for example the insured started a fire with a view of burning down his own property. Here not only would any insurance the arsonist had against loss by fire not respond but nor would any public liability insurance if the fire spread to neighbouring properties. These types of cases have been typically decided on the basis of the 'risk not certainty' rule discussed above. In other words the loss is not a 'fortuity'.

The second type of case is where the insured does an act deliberately which causes a loss but does it with the intent of reducing loss overall. For example in *Canada Rice Mills v Union and General*[131] goods were damaged whilst in a ship through overheating when the ventilation system was closed to prevent sea water entering the hold where the goods were stowed. The policy covered damage by 'perils of the sea', but was the damage caused by the sea? The Privy Council held that it was, in the words of Lord Wright:

> . . . where the weather conditions so require, the closing of the ventilators is not to be regarded as a separate or independent cause, interposed between the peril of the sea and the damage, but as being such a mere matter of routine seamanship necessitated by the peril that the damage can be regarded as the direct result of the peril . . .[132]

In other words, there was no break in the chain of causation between the action of the sea and the damage. The same would be true if the act were done with the knowledge that it would cause the loss if the intention is to avoid greater loss.[133]

The final type of case is where the loss was of a type covered by the policy but a negligent act by the insured is potentially the proximate cause. This issue was considered in a case which whilst it did not involve insurance per se has nevertheless been regarded as the leading authority in this matter. In *Attorney-General v Adelaide Steamship Company, The Warida.*[134] Here The Warrida, a ship chartered by the British Government for war work during the First World War, was carrying wounded soldiers back to Britain. While taking anti-submarine manoeuvres there was a collision with

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[129] *Global Process Systems Inc and another v Syarikat Takaful Malaysia Berhad (The Cendor Mopu)* [2011] UKSC 5 [88].

[130] *J J Lloyd Instruments Ltd -v- Northern Star Insurance Co Ltd (The 'Miss Jay Jay')* CA [1987] 1 Lloyd's Rep 32.

[131] *Canada Rice Mills Ltd v Union and General* Insurance Co [1941] AC 55 (PC).

[132] At page 70.

[133] *Symington & Co v Union Insurance Society of Canton Ltd* (1928) 32 Lloyds Law Rep 287 (CA). Insurers of fire risk liable when goods thrown into the water in order to provide a fire break when fire broke out in the vicinity.

[134] *Attorney-General v Adelaide Steamship Company Limited* [1923] AC 292 (HL). This was an important test case since the charter was in standard form with many thousands of merchant vessels having been requisitioned to help in the war effort.

another vessel which would not have occurred but for the negligence of The Warida's master. Under the terms of the charter the Government was not liable for injury by collision or other cause arising as a sea risk, but was liable for the risks of war including 'all consequences of hostile or warlike operations.' The House of Lords held that losses were clearly covered by the broad terminology of the insuring clause but noting that the situation would be different if loss caused by the negligence of the claimant were excluded by the policy. However, even where there is an express clause to the effect that the insured must take reasonable care to avoid loss, at least in liability policies this has been held to exclude liability for recklessness only.[135] This makes complete sense since a key function of a liability policy is to cover the insured against third party claims most of which would allege a lack of care: were the policy construed literally it would therefore provide little or no cover at all. In the case of property insurance the logic behind construing lack of reasonable care or the like as 'recklessness' is less clear cut, but nevertheless, in cases involving consumers and even small businesses the courts have tended to follow this approach.[136]

Insurers' policy drafting has adapted to the matter, tending nowadays, rather than relying on a general duty to take reasonable care, to make it a condition precedent to liability that the insured take specified steps, for example having a working alarm system which is left on whenever the insured property is left unattended. So long as compliance with the steps is practicable, then the courts will construe the policy accordingly.[137] However the effect of s 11 Insurance Act 2015 needs to be borne in mind—if compliance with the specified steps would not have reduced the risk of the loss which actually eventuated then the insurer cannot rely on the breach to avoid the claim.

Entering into and performing the contract

We have touched on a number of unusual features of insurance law but have not yet mentioned what is the most peculiar aspect of contracts of insurance, namely the fact that they are contracts of *uberimae fidei*—utmost good faith. The principal application of this duty was that it imposed a heavy duty of disclosure on the insured when the contract was entered into but the impact of the duty was only felt if there was a claim since it was almost always at this stage that the insurer discovered any breach of the duty. In this context the duty of utmost good faith has been replaced in relation to non-consumer insurance by a duty of 'fair disclosure'[138] and in consumer insurance by a duty to 'take reasonable care not to make a misrepresentation to the insurer'.[139] However before we can understand the 'new' law we need some understanding of the concept of utmost good faith.

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[135] *Tinline v White Cross Insurance Association Ltd* [1921] 3 KB 327 (HC).

[136] See Veronica Cowan, *Lack of reasonable care conditions*. Ins L & P (1993) 3(1) 4-6. *Sofi v Prudential Assurance* [1993] 2 Lloyd's Rep 559 (CA). But see *Devco Holder v Burrows & Paine* [1993] 2 Lloyd's Rep 567 (CA).

[137] *Milton Furniture Limited v Brit Insurance Limited* [2015] EWCA Civ 671.

[138] s 3 Insurance Act 2015.

[139] s 2(2) Consumer Insurance (Disclosure and Representations) Act 2012.

Utmost good faith

What were the duties?

In 1766 in *Carter v Boehm*,[140] Mansfield CJ introduced into the law of insurance an obligation that the parties owe one another a duty of good faith, and this duty was codified in s 17 of the Marine Insurance Act 1906.[141] The duty principally involves the assured disclosing to the insurer all circumstances which were material to the contract and not misrepresenting any material circumstances. These requirements were the basis of ss 18 and 20 of the Marine Insurance Act 1906[142] and it became established that materiality involved a two-part test.[143] First, looked at objectively a circumstance was material if the hypothetical prudent insurer have taken the circumstance into account in assessing the risk though he need not have thought it decisive. Additionally, but subjectively this time, a circumstance was material only if the particular insurer in question was induced to enter into the contract on the terms agreed by the non/mis-disclosure?

This duty of disclosure applied whether the insurer had asked about the circumstance or not. It was a positive duty to volunteer all of the material circumstances, though the insurer might waive his rights to information, for example by being told that certain information is available and not asking see it.[144] It did not matter that the material non/mis-disclosure was irrelevant to the cause of the loss for which a claim was being made[145] and that the insured did not actually know if on an objective basis ought to have known it.[146] See for example *Glicksman v Lancashire & General Assurance Co* where the insured had no way of knowing that insurers would want to know whether he had ever been refused insurance in the past as he was functionally illiterate in English. The matter was even more problematic since even if he had disclosed the information, the insurer would have accepted the risk at the premium it actually charged.[147] Nevertheless the insurer's claim to avoid the contract was upheld unanimously in the House of Lords.

There was some debate on the extent of the duty of good faith beyond the duty of disclosure in ss 18 and 20 MIA 1906.Some decisions proceeded on the basis that the principles of disclosure did apply, suitably adapted, especially at 'decision points'

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[140] (1766) 3 Burr 1905. [141] As amended by s 14 Insurance Act 2015.

[142] Now repealed by Insurance Act 2015.

[143] *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Ltd* [1995] 1 AC 501 (HL).

[144] ibid. In personal and small business insurance, insurers voluntarily agreed not to treat as non-disclosure any circumstances about which they have not asked a question on the proposal form.

[145] Thus in *Banque Financiere de la Cite SA v Westgate Insurance Co Ltd* [1990] 2 Lloyd's Rep 377 (HL), no point was taken that the fraud that the insured's employee had committed and which the insurers had not disclosed to the insured had nothing to do with the cause of the loss. The case also illustrates that the duty of disclosure under s 17 is mutual.

[146] *Glicksman v Lancashire & General Assurance Co* [1927] AC 139 (HL). All of the judges expressed regret at the outcome, Lord Wrenbury at p 146, going so far as to say that the insurer was 'mean and contemptible'.

[147] *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Ltd* [1995] 1 AC 501 (HL) reaffirmed the view that for the insurer to be induced to enter the contract did not require that the non/mis-disclosure actually affected the insurer's decisions as to taking the risk, the policy terms or the premium he would charge. In the 20 years since *Pine Top* courts have consistently decided exactly the opposite see for example *Drake Insurance v Provident Insurance Plc* [2003] EWCA] Civ 1834, [2004] Lloyds Rep IR 277.

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where the insurer has to decide, for example, whether to charge more for cover because the assured has changed the destination of goods in transit.[148] However it became clear that making a dishonest claim, for example exaggerating the size of a loss[149] did not engage s 17 but was to be treated as a breach of a condition of the contract, permitting prospective termination of duties, including the duty to pay the claim but not requiring the insurer to return of any premium paid nor the insured to return the proceeds of any previous successful claims. Similarly apart from mid-term variations and the duty not to make fraudulent claims, the conclusion was that the duty of good faith once the policy was in force was very limited as were appropriate authorities on the matter. Thus for example in *Ted Baker v Axa*,[150] rather than pursue the issue of the scope of the post contractual duty of good faith the Court of Appeal preferred to deal with the matter on a normal contractual basis.

Case Box: Ted Baker Plc v Axa Insurance Uk Plc [2017] EWCA Civ 4097

FACTS: The policy contained a standard 'claims co-operation' clause which was made a condition precedent to liability for the claim in question. The claim was for loss of profits by Ted Baker caused by an extensive series of frauds and the insurer, Axa, asked for financial data in order to assess the amount of the loss. Some of this data was complex to provide and Ted Baker proposed that the issue of quantum be 'parked' until Axa had accepted the validity of the claim in principle. Axa's representative said that he would ask for instructions from Axa but no answer to the request was ever given. Because the data was not provided the insurer refused the claim for breach of the claims co-operation clause. Did Axa have a duty to inform Ted Baker it was insisting on its rights?

HELD: In the Court of Appeal that if Axa sought to rely on the 'non co-operation' they had a positive duty to inform Ted Baker that they were insisting on seeing the data. Failure to do so meant that on normal contractual grounds they were stopped from asserting their contractual right to decline the claim for breach of the condition.

COMMENTARY: At first instance Eder J focused on the policy wording and held that Axa had no duty in good faith to warn Baker that by failing to provide the data they were breaching a condition since Baker had an experienced insurance professional acting for them who would be fully aware of the repercussions of a breach a conclusion with which the Court of Appeal agreed. However Eder J then held there was no estoppel since there was no representation by Axa whether express or implied. Sir Christopher Clarke concluded that there was no need of a representation, an estoppel may arise if:

> in the light of the circumstances known to the parties, a reasonable person in the position of the person seeking to set up the estoppel . . . [Ted Baker] would expect the other party [Axa] acting honestly and responsibly to take steps to make his position plain. Such an estoppel is a form of estoppel by acquiescence arising out a failure to speak when under a duty to do so.[151]

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[148] *Goulstone v Royal Insurance Company* (1858) 1 F&F 276.

[149] But see *K/S Merc-Scandia XXXXII v Lloyd's Underwriters* (*The Mercandian Continent*) [2001] EWCA Civ 1275, [2001] 2 Lloyd's Rep 563, where the Court of Appeal held that the fraud would have to be such as to amount to a repudiatory breach such that the insurer would have been entitled to terminate the contract on normal contractual principles quite apart from the issue of utmost good faith.

[150] *Ted Baker Plc v Axa Insurance Uk Plc* [2017] EWCA Civ 4097.

[151] At par [82].

What was the effect of material non-disclosure?

Section 17 of the Marine Insurance Act 1906 made it clear that the remedy for pre-contractual material non-disclosure was avoidance of the policy *ab initio*, and it was held that there is no alternative such as a claim for damages either in contract or in tort for the breach of the duty of good faith.[152] Under a void policy, the premium must be returned to the assured, so too any claims previously paid under the insurance must be returned to the insurer. In relation to post-contract non-disclosure at 'decision points', it seems likely that it was merely the variation in the policy that the non/mis-disclosure induced which was avoided *ab initio*, though the whole policy could be terminated on normal contractual principles if the assured's actions amounted to a breach of a condition.[153]

However, where an insured made a dishonest claim, while that claim could be avoided and the policy could be terminated prospectively it was not avoided *ab initio*.[154] Mance LJ in *Gottleib*[155] left open the issue whether an honest claim being pursued in parallel to the dishonest one but which were not actually paid at the date of the fraud will also be lost on the basis that the insurer has terminated the contract for breach of a condition. However, it is clear that any payments already made in respect of honest claims may be retained by the assured. However as the courts have acknowledged there is nothing to prevent an insurer from making it an express term of the contract that dishonesty at claims stage (or indeed at any point during the life of the policy) entitles the insurer to avoid the contract *ab initio*.[156]

Even where the failure by the insured to fully disclose material was purely technical or where the breach had no causal connection with the loss the starting point of the law that it was not an act of bad faith simply to enforce one's contractual rights[157] even where as in *Glicksman* and *Macaura* the insurer was clearly motivated by a desire to resist a claim because of its belief that the insured had 'torched' the insured premises even though it could not prove it because resorting to such the draconian remedy of avoiding the contract *ab initio* did not constitute bad faith.

That said the courts responded with such tools as they felt they had at their disposal—construing policies against the insurer sometimes to breaking point[158] and developing a wide-ranging concept of the doctrine of waiver of rights. Nevertheless the law of insurance as it stood in the year 2000 was recognized by almost all involved in the insurance industry as being unsatisfactory, at least in theory. Consumer[159] insurance disputes were by then dealt with almost exclusively by an ombudsman service originally set up by the Association of British Insurers but subsequently incorporated into the regulatory processes established under the Financial

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152 *Banque Financière de la Cite SA v Westgate Insurance Co Ltd* [1990] 2 Lloyd's Rep 377 (HL).

153 See Longmore LJ in *K/S Merc-Scandia XXXXII v Lloyd's Underwriters (The Mercandian Continent)* [2001] EWCA Civ 1275, [2001] 2 Lloyd's Rep 563.

154 *Manifest Shipping Co Ltd v Uni-Polaris Shipping Co Ltd (The Star Sea)* [2001] UKHL 1, [2003] 1 AC 469.

155 *Axa General Insurance Ltd v Gottlieb* [2005] EWCA Civ 112, [2005] 1 All ER (Comm) 445.

156 See for example *Joseph Fielding Properties (Blackpool) Ltd v Aviva Insurance Ltd* [2010] EWHC 2192, [2011] Lloyd's Rep IR 238 (Mercantile).

157 See for example *Glicksman v Lancashire & General Assurance Co* [1927] AC 139 (HL) and *Macaura v Northern Assurance Company*[1925] AC 619 (HL).

158 See for example *Cornhill Insurance v D E Stamp Felt Roofing* [2002] EWCA Civ 395.

159 This would include 'micro businesses too'.

Services Act 1986 and then under the Financial Services and Markets Act 2000. The Insurance Ombudsman and the successor body the Financial Ombudsman Service were to determine a dispute 'by reference to what is, in his opinion, fair and reasonable in all the circumstances of the case'.[160] Although these 'circumstances' include consideration of the law and industry practice the Ombudsman developed a body of guidance and decisions which differed quite considerably from the strict 'letter of the law' and much of this is reflected in the Consumer Insurance (Disclosure and Representations Act) 2012.

Even where the Ombudsman's service did not have jurisdiction insurers were wary of relying of some of the more draconian aspects of the law and so the insurance industry as a whole—both brokers representing the insureds and the insurers—welcomed the work of the Law Commission which has resulted in Insurance Act 2015 which, as noted above, in non-consumer insurance, replaces the duty of 'utmost good faith' in making disclosures with a duty of 'fair presentation'.[161]

The duty of fair presentation

Although the terminology has changed the Act is evolutionary rather than revolutionary especially as it represents to a great extent the internal practices of reputable brokers and insurers[162] and draws on previous case law. A different regime applies to consumer insurance by virtue of the Consumer Insurance (Disclosure and Representations) Act 2012.

The objective of the Law Commission and indeed of the insurance market as a whole with the 2015 Act was to move to a legal structure where the law promoted good practice. The common law as enshrined in the MIA 1906 had exactly the opposite effect. Insurance brokers, knowing of the onerous duty of disclosure owed by their clients and aware of the fact that they could expect a claim from the client if a policy brokered by them proved void for material non-disclosure, were induced to 'data dump' on the insurer, disclosing huge quantities of material, most of it irrelevant in an unstructured manner. Indeed where a broker knows or suspects the material would be likely to lead to the insurer declining to accept the risk, then data dumping as late as possible provided an opportunity to hide the potentially 'embarrassing' information in amongst totally benign material. Alternatively as in *Pine Top v Pan Atlantic*, the broker would have the problematic material available for inspection by the insurer but deliberately draw the insurer's attention away from it to other matters in the disclosure files. The 'weapon of choice' for the insurers was the 'basis of the contract' clause, making the accuracy of the 'dumped' material a condition precedent to liability. In this way the insurer had a good chance of finding some inaccuracy in the event of a claim it did not wish to meet for one reason or another and could indulge in what is called 'underwriting at claims stage'.

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[160] s 228 Financial Services and Markets Act 2000 and the Financial Conduct Authority Rule Book DISP 3.6.

[161] s 3 IA 2015.

[162] That said few insurers could resist including 'basis of the contract' clauses in commercial insurances and clauses designed to protect their rights against claims of waiver.

Replacing the duty of utmost good faith with a duty of fair presentation was perceived as having two effects benefitting both sides of the insurance markets—the brokers acting for the insured and the insurers:

1. It would reduce the onerous nature of extensive precautionary disclosure; and
2. It would require the insured to 'play fair' in the manner of disclosure, thus making 'basis of the contract' clauses unnecessary.

It was therefore not only a fair compromise but also a move towards making 'market best practice' the only sensible practice.

The 2015 Act adopts this compromise. It sets out the duty of fair presentation in s 3 and there are four key components—when the duty applies, the content of the disclosure, the manner of disclosure and the duty of accuracy or more accurately the duty not to make misrepresentations. We will consider these key components in turn.

Section 3 Insurance Act 2015—The duty of fair presentation

(1) Before a contract of insurance is entered into, the insured must make to the insurer a fair presentation of the risk.

(2) The duty imposed by subsection (1) is referred to in this Act as "the duty of fair presentation".

(3) A fair presentation of the risk is one—
- (a) which makes the disclosure required by subsection (4),
- (b) which makes that disclosure in a manner which would be reasonably clear and accessible to a prudent insurer, and
- (c) in which every material representation as to a matter of fact is substantially correct, and every material representation as to a matter of expectation or belief is made in good faith.

(4) The disclosure required is as follows, except as provided in subsection (5)—
- (a) disclosure of every material circumstance which the insured knows or ought to know, or
- (b) failing that, disclosure which gives the insurer sufficient information to put a prudent insurer on notice that it needs to make further enquiries for the purpose of revealing those material circumstances.

(5) In the absence of enquiry, subsection (4) does not require the insured to disclose a circumstance if—
- (a) it diminishes the risk,
- (b) the insurer knows it,
- (c) the insurer ought to know it,
- (d) the insurer is presumed to know it, or
- (e) it is something as to which the insurer waives information.

When does the statutory duty arise?

By virtue of s 3(1) it arises 'before a contract of insurance is entered into'. Where an existing policy is varied—for example to provide greater cover—then the duty also applies but not to the policy as a whole but only in relation to the change in risk.[163] This seems to reflect the previous law so far as application is concerned.

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[163] s 2(2) IA 2015.

What disclosure is required—content

The issue of what disclosure is required to amount to a fair presentation has two elements—firstly as to content and then as to the manner of disclosure. In relation to content the disclosure required for fair presentation can itself be satisfied in one of two ways. The first way reflects the law as it had developed prior to the Act namely '*disclosure* of every *material circumstance* which *the insured knows or ought to know*'.[164] There are some important terms used in this phrase (italicized for ease of reference) and each needs to be considered in turn.

'Disclosure' can be either oral or written and need not be made in 'one presentation'.[165] This accords precisely with previous practice since particularly in commercial insurance an initial presentation of the risk to the underwriter may well prompt requests for further information and negotiations will often take place, for example as to the extent of cover or procedures to be adopted by the insured to minimize the likelihood of loss.

As noted above, the 2015 Act is the result of a lengthy review process by the Law Commission and intentionally uses the same term 'material circumstance' as was contained in the MIA 1906 with the objective of ensuring existing case law would be used in the interpretation of the concept.[166] Consequently the definition in the Act of material circumstance follows the 1906 model: '[a] circumstance or representation is material if it would influence the judgement of a prudent insurer in determining whether to take the risk and, if so, on what terms.'[167]

The types of circumstance which a prudent insurer will take into account fall into two main classes: physical and moral hazards. Mance J described it thus:

> It is important to realize what is embraced by 'risk'. It is not simply the peril or possibility of loss or damage occurring within the scope of the policy. It embraces other matters which would, if known, be likely to influence a prudent underwriter's decision. It includes what is known as 'moral hazard', which may merely increase the likelihood of it being made to appear (falsely) that loss or damage has occurred falling within the scope of the policy.[168]

Thus for example it would be material to an insurer of goods being carried on a ship to know among other things the identity of the ship, the ports of loading and discharge, the time of year the voyage is to be undertaken and the route, whether the goods are deck cargo and whether they were containerized or not[169] as well as the nature and description of the goods. These are all circumstances which go to physical hazards. However the insurer would also find material issues going to moral hazard which usually involves matters about the assured. Thus, how many claims the assured has brought in the past under previous policies or how many uninsured losses he had suffered in the past in similar circumstances would be material as would be that

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[164] s 3(4) IA 2015. [165] s 7(1).

[166] Law Commission, *Insurance Contract Law: Business Disclosure; Warranties; Insurers' Remedies for Fraudulent Claims and Late Payment* (Law Com No 353, 2014) para 7.25.

[167] s 7(3).

[168] *Insurance Corp of the Channel Islands v Royal Hotel Ltd* [1998] Lloyd's Rep IR 151 (QB) 156.

[169] See *Wünsche Handelsgesellschaft International mbH v Tai Ping Insurance Co Ltd* [1998] 2 Lloyd's Rep 8 (CA), where the Court concluded that the description of the goods at loading as containerized did not imply in the circumstances of the case (the insurance attached at the commencement of transit from inland factories) that they would be containerized throughout the insured transit.

insurance has been declined by another insurer,[170] whether the insured is in financial difficulties or that the assured has been the subject of serious and plausible allegations of fraud, even if they turn out to be false.[171] *Berkshire Assets (West London) Limited v AXA Insurance UK plc*, the first reported case in England where the fair disclosure principles of the 2015 Act fell to be applied, concerned the non-disclosure of criminal proceedings against one of the insured company's directors, commenced three months before the policy was renewed. Although these proceedings were discontinued towards the end of the policy term the insurer refused to pay for damage caused by a faulty sprinkler system on the ground of material non-disclosure.[172] The Court held that at the point of renewal it was a breach of the duty of fair disclosure not to reveal these proceedings and since the insurer had proved that it would not have renewed the policy by reference to its underwriting guidelines it was entitled to avoid the contract.

At the suggestion of market participants, s 7(4) contains a non-exhaustive list of examples of material circumstances taken from case law. Some of these suggestions can be exemplified by the illustrations given above. For example duty to disclose 'special or unusual facts relating to a risk'[173] might well include the fact that the proposer for insurance has suffered multiple losses in the past. Similarly, the duty to disclose any 'particular concerns' the proposer may have which led him to seek the insurance[174] would encompass the fact that he had suffered losses in the past of the type for which he is seeking insurance. Of this non-exhaustive list of examples the potentially most problematic one is contained in s 7(4)(c):

> [A]nything which those concerned with the class of insurance and field of activity in question would generally understand as being something that should be dealt with in a fair presentation of risks of the type in question.

The insured is taken to 'know' what he ought to have known[175] so that there is a danger that an insured acting without an experienced broker may be taken to be under a duty to disclose matters which are well known to be material by market participants but which he is unaware need to be revealed as part of a fair presentation. Having said that the insurer would be aware of the lack of a broker acting for the insured and it can be anticipated that a court would be sympathetic to an argument that the insured had nevertheless made a fair presentation of the risk. The issue of determining whether the knowledge of a person within an organization or within an agent acting for an organization can be imputed to the organization itself was the source of much litigation in the past. Section 4 now provides a set of rules to determine this issue which reflects the position at common law. In addition to 'actual, imputed and constructive notice, the insured also is taken to know what he could have know but chose to ignore'—so called 'Nelsonian blindness'. In the words of s 6 the insured 'knows' 'matters which . . .[he] suspected, and of which . . .[he] would have had knowledge but for deliberately refraining from confirming them or enquiring about them'.

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[170] *Container Transport International Inc v Oceanus Mutual Underwriting Association (Bermuda)* [1984] 1 Lloyd's Rep 476 (CA). Though see *Glasgow Assurance Corp Ltd v Symondson & Co* (1911) 104 LT (KB).

[171] *Brotherton v Aseguradora Colseguros SA* [2003] 2 All ER (Comm) 298 (CA). *North Star Shipping Ltd and Others v Sphere Drake Insurance plc* [2006] EWCA Civ 378, [2006] 2 All ER (Comm) 65. For a post 2015 example see the Scottish case, *Young v Royal and Sun Alliance* [2019] CSOH 32, Outer House of the Court of Session applying the same principles as the common law.

[172] *Berkshire Assets (West London) Limited v AXA Insurance UK plc* [2021] EWHC 2689 (QBD).

[173] s 7(4)(a). [174] s 7(4)(b). [175] s 3(4).

Finally the second way of meeting the duty of fair presentation is to make sufficient disclosure to put the insurer on inquiry.

What disclosure is required—manner of disclosure

The other side of the coin on disclosure involves the method of disclosure. As s 3(4) says the disclosure has to be in a 'manner which would be reasonably clear and accessible to a prudent insurer.' The Law Commission notes that provision of a large volume of data to an insurer is not of itself objectionable if it provides a means whereby the insurer can navigate round the material perhaps accompanied by a fair summary drawing attention to the content of files which is exceptional or unusual.[176] Similarly, while as we have noted there is nothing objectionable per se in disclosures being made over a period of time, a disclosure which is made on a bit by bit basis, the effect of which is to obscure its importance from a 'prudent insurer' would not comprise a 'fair presentation'.

The duty not to make misrepresentations

The final element of the duty of fair presentation is contained in s 3(3)(c), namely the duty not to make misrepresentations. Under this subsection 'every material representation as to a matter of fact' must be 'substantially correct' and 'every material representation as to a matter of expectation or belief' must be made in good faith'. The Act states that a statement is 'substantially correct' if a prudent insurer would not consider the difference between what is represented and what is actually correct to be material'.[177] This formulation of the duty not to make misrepresentations is based on s 20 MIA 1906. Under that Act there were problems distinguishing representations of fact (which had to be substantially true) and statements of opinion or belief (which need only to have been honestly made). No attempt is made in the 2015 Act to resolve these problems. Assuming that the existing case law will be relied on to interpret this duty the terminology used in the representation will not be conclusive. For example, in *Sirius International v Oriental Assurance*[178] Longmore J held that a representation by an insurance broker that it had been informed that there were fire hydrants in the insured premises was a statement of the fact that there were fire hydrants on the premises regardless of the fact that it was expressed in effect as a statement of belief. However a means of distinguishing the two did emerge from the cases, namely where a statement was of an existing state of affairs of which the insured was aware or ought to have been aware, the representation was almost certainly one of fact. Where the statement concerned a future state of affairs or was something of which the insured could not reasonably have been expected to be aware then it was almost certainly a representation of belief or opinion. So applying this test to *Sirius* it is clear that the broker was reporting an existing state of affairs which ought to have been known by the insured. It is expected that this approach will continue under the 2015 Act.

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[176] Adapted from *Container Transport International Inc and Reliance Group Inc v Oceanus Mutual Underwriting Association (Bermuda) Ltd* [1984] 1 Lloyds Rep 476, Stephenson LJ 529.

[177] s 7(5).

[178] *Sirius International Corp v Oriental Assurance Corp* [1999] Lloyds Rep IR 343 (QBD).

Remedy for breach of the duty of fair presentation

As we have seen, under the previous law the remedy for breach of the duty of utmost good faith in relation to contractual disclosures was avoidance of the policy *ab initio* accompanied (normally) by return of any premiums paid. This remedy was recognized as being draconian particularly where the insurer would have accepted the risk and perhaps only charged slightly more by way of premium. It also had the effect of requiring the insured to return any money it had received in respect of previous claims. Additionally there was conflict between admittedly *obiter* statements in the House of Lords in *Pan Atlantic I* that a non/mis-disclosure was material even if, had it been fully disclosed, it would not have affected the terms offered by the insurer and the practice of lower courts to the contrary. Finally there was no dispute over the fact that the non/mis-disclosure need have no causative connection with the loss which eventuated under the policy. These issues have been addressed in s 8 of the Act.

Section 8 Insurance Act 2015—Remedies for breach

(1) The insurer has a remedy against the insured for a breach of the duty of fair presentation only if the insurer shows that, but for the breach, the insurer—
  (a) would not have entered into the contract of insurance at all, or
  (b) would have done so only on different terms.

(2) The remedies are set out in Schedule 1.

(3) A breach for which the insurer has a remedy against the insured is referred to in this Act as a "qualifying breach".

(4) A qualifying breach is either—
  (a) deliberate or reckless, or
  (b) neither deliberate nor reckless.

(5) A qualifying breach is deliberate or reckless if the insured—
  (a) knew that it was in breach of the duty of fair presentation, or
  (b) did not care whether or not it was in breach of that duty.

(6) It is for the insurer to show that a qualifying breach was deliberate or reckless.

Section 8(1) needs no commentary, it settles the matter that in order to obtain a remedy for breach of the duty of fair presentation the insurer must show that but for the breach it would either have offered different terms to the insured or declined to offer insurance at all.

If the breach fulfils either of these requirements then it is a 'qualifying breach', that is, it is a breach which qualifies the insurer for a remedy under the Act.[179] The Act divides 'qualifying breaches' into two types and the remedies vary depending on the type of breach involved.[180]

Deliberate or reckless breaches entitle the insurer to avoid the contract and unlike the position before the Act it is clear that in all cases there is no duty to return any premiums paid.[181] Such a breach committed before the disputed contract was entered into (and this would include where the policy is renewed since these are treated as new

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179 s 8(3). 180 s 8(4). 181 Sch 1 paras 2 and 8.

contracts) permits avoidance *ab initio*. Such a breach committed during the course of a variation permits termination from the date of the breach but does not affect claims made prior to that date. The retention of the remedy of avoidance reflects the fact that insurance contracts remain contracts of utmost good faith and a lack of good faith by either party strikes at the root of the contract.

Where breaches are committed otherwise than deliberately or recklessly the Act seeks to apply normal contractual principles namely that remedies should put the injured party in the same position as he would have been in but for the breach. Thus if the breach relates to pre-contractual disclosure and the insurer can show that if the insured had made a fair presentation it would not have offered insurance on any terms, then it may avoid the contract but must return any premiums paid.[182] If the breach relates to a mid-term variation and the insurer can show that it would not have agreed to the variation on any terms it can avoid the variation but must return any increase in premium arising by virtue of the variation. If, however, the insurer shows that although it would have agreed to offer the insurance (or accept the variation as the case might be) it would have done so on different terms (except as to premium) then it may treat the contract as being on those different terms.[183]

Finally there is the situation where the insurer would have accepted the risk but would have charged a higher premium. The approach of the 2015 Act is to treat this in that same way as 'under insurance'. Suppose I wish to insure a factory worth £10m against fire but I innocently declare it to be worth £8m when negotiating the insurance. The insurer agrees to indemnify me against loss up to £8m and charges me £8,000 p a premium. A fire breaks out and causes £250,000 damage. The insurer discovers my mistaken valuation when he comes to pay my claim and states he would have charged £10,000 p a had he known the real value. In such a case I am said to have under insured my factory by 20% and the effect is that the insurer will pay me only 80% of my claim even though it is far below the maximum sum insured and even though the premium lost to the insurer is only £2,000.[184] Under the 2015 Act there would be the same result if, as a result of any non-fraudulent non-disclosure or mis-disclosure, the insurer charged 80% of the premium he would have charged but for my error.[185]

It should be noted that a non-fraudulent non-disclosure or mis-disclosure may on discovery result in the insurer showing it would have both imposed different terms *and* increased the premium. In such a case there would need to be an inquiry whether there could have been a valid claim under the imaginary policy containing such different terms. If the answer was yes then the claim would be reduced to take account of the underpayment of premium.

Fraudulent claims

Although the subject of much confusion,[186] as noted above, the common law finally seemed to have settled on the conclusion that the doctrine of utmost good faith as set

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[182] Sch 1 para 4. [183] Sch 1 para 5.

[184] It should be noted that in fact, since my representation of the value of the factory has probably been turned into a warranty under the policy though the operation of a 'basis of the contract ' clause the insurer could have avoided the contract *ab initio* under the pre-2015 Act law.

[185] Insurance Act 2015, Sch1 para 6.

[186] For an overview see Law Commission, *Insurance Contract Law: Business Disclosure; Warranties; Insurers' Remedies for Fraudulent Claims and Late Payment* (Law Com No 353, 2014) paras 20.1—20.39.

out in s 17 MIA 1906 did not apply in cases where a claim was fraudulent but such a claim permitted termination of contract on normal contractual principles. That said there remained a number of areas where until recently the law was not entirely clear—for example whether using 'fraudulent devices' to support an otherwise valid claim amounted to fraud for these purposes. Fraudulent devices is an expression used to describe fraudulent means to support otherwise valid claims.

The matter was settled in *The DC Merwestone*[187] which involved insurance of a ship. In this case the insured shipowner falsely stated that its employees had heard but ignored an alarm believing it to have been set off by accident when in fact the alarm appeared not to have been heard at all. The alarm in question was one which was intended to warn that the ship might be flooding and seems to have been made to avoid a possible argument from the insurer that the ship's alarm systems were faulty. At first instance and the Court of Appeal the courts held that the claim was valid but the fraudulent statement permitted termination of the policy following the authority of Mance LJ in *Agapatos v Agnew*.[188] The Supreme Court held by a majority of 4 to 1 that a 'fraudulent device' to support an otherwise valid claim did not permit termination, it is not a fraudulent claim as such. The dissenting judgement was delivered by Lord Mance!

In respect of policies to which the 2015 Act applies the basic position is retained by s 12, namely forfeiture of the instant claim, a right for the insurer to avoid the policy from the date of the fraud and so recover any payments made under the policy in respect of the fraudulent claim but not avoidance of the policy *ab initio*. The Act does not however seek to define fraud presumably leaving it to the courts to apply common law including the decision in *The DC Merwestone*.[189] Nor does it seek to deal with the degree of materiality needed by any fraudulent devices employed to support an otherwise valid claim in order to engage the section.

Contracting out of the 2015 Act

The 2015 Insurance Act affects three broad areas of insurance law; the effect of non-disclosure or misrepresentation at the inception of a policy or at its variation, the effect of breaches of warranties and conditions, and the effect of fraudulent claims on the rights of the parties.

Save as respect one matter the Act makes it clear that subject to the insurer meeting certain conditions, the parties are free to vary or exclude the Act's effects. The one non-excludable provision is s 9 which makes it impossible to convert representations into warranties or conditions precedent to liability[190] but otherwise the s 2 duty of fair disclosure, and the effects of ss 10,11 and 12 can be varied or excluded by the parties.[191]

However any attempt to effect such a variation or exclusion to the detriment of the insured must meet the requirements of s 17.[192]

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[187] *Versloot Dredging BV v HDI-Gerling Industrie Versicherungs, The DC Merwestone* [2016] UKSC 45, [2017] AC 1, [2016] 2 Lloyd's Rep 198.

[188] *Agapatos v Agnew* [2002] EWCA Civ 247, [2002] 3 WLR 616.

[189] See generally *Derry v Peek* (1889) LR 14 App Cas 337 (HL) 374.

[190] s 16(1). [191] s 16(2). [192] s 16(2).

Section 17 Insurance Act 2015

(1) In this section, "the disadvantageous term" means [a term which would put the insured in a worse position as respects any of the other matters provided for in ss 2–13].

(2) The insurer must take sufficient steps to draw the disadvantageous term to the insured's attention before the contract is entered into or the variation agreed.

(3) The disadvantageous term must be clear and unambiguous as to its effect.

(4) In determining whether the requirements of subsections (2) and (3) have been met, the characteristics of insured persons of the kind in question, and the circumstances of the transaction, are to be taken into account.

(5) The insured may not rely on any failure on the part of the insurer to meet the requirements of subsection (2) if the insured (or its agent) had actual knowledge of the disadvantageous term when the contract was entered into or the variation agreed.

Section 17 seeks to strike a balance between the rights of parties to contract on such terms as they see fit against the danger that insurers will use this freedom to disadvantage the insured. Hence the need for transparency. In fact this approach mirrors the general contractual position in respect of any unusual or onerous terms[193] incorporating as it does elements of the *contra proferentem* rule and the rules developed in respect of exclusion clauses.

Section 17(4) is of particular importance since the degree of transparency necessary to carry out the balancing process will vary considerably from insured to insured. The non-consumer insurance regime will apply to all policies not entered into wholly or mainly for purposes unrelated to an individual's trade, business or profession[194] and so will cover one-person micro businesses as well as multi-national corporations. Consequently the insurer needs to tailor the disclosure material to suit the customer—what amounts to transparency when dealing with a specialist insurance broker acting on behalf of a sophisticated client would clearly be insufficient for an insured acting without professional assistance buying insurance for a van over the internet.

Case Analysis – COVID-19 and Business Interruption Insurance

As a conclusion to the substantive part of this chapter there follows a comparatively lengthy analysis of the Supreme Court decision on the liability of insurance companies for the loss of income experienced by businesses because of the COVID-19 epidemic.[195] The case demonstrates the practical difficulties in interpreting insurance policies and how complex the issue of causation of loss can be.

[193] See Dillon LJ in *Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd* [1989]QB 433,439.
[194] s 1 Insurance Act 2015 applying s 1 Consumer Insurance (Disclosure and Representations) Act 2012.
[195] *FCA v Arch and Others* [2021] UKSC 1, [2021] AC 649.

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Business Interruption Insurance

Business interruption insurance provides businesses with an indemnity within the limits specified in the policy to cover loss of income which would otherwise have accrued during periods when the business cannot be continued as normal due to an unexpected event and/or depending on the policy, the increased cost of working during such a period. Typically such cover is provided as an optional extra to business policies which, in separate sections, also provide cover for physical damage to or loss of property as well as some other pure financial losses, commonly called Business or Commercial Combined Policies. Set out in Figure 1 below is an outline of a typical Business Combined Policy.

Policy Section	Contents	Further Explanation
General Provisions applying to all sections	Definitions, Promise to indemnify for Loss covered by the policy, claims procedure, general warranties, duty to pay premiums promptly, if Loss covered by more than one section can only claim under 1 of them.	Egs definition of Loss, claims for Losses to be made as soon as possible, warranty that information disclosed is given with reasonable care, that property covered under the policy will be kept in good condition and repair.
Section 1 Public Liability	Definition of what is covered and exclusions ie what is not covered; typically excludes Employers' Liability, liability from use of vehicles, product liability. Definitions specific to the section. Limit of liability under the section.	Cover for legal liability to third parties eg occupiers' liability, and other negligence based liability pollution or contamination and other nuisance based liability.
Section 2 Employers' Liability	Definition of what is covered and exclusions. Definitions specific to this section. Limit of liability under the section.	Provides statutory Employer's Liability Insurance. Excludes Road Traffic accidents.
Section 3 Fire etc	Definition of what is covered and exclusions. Definitions specific to this section. Limit of liability under the section. Covers loss/damage to property including, money business machines and stock.	Typically covers loss to insured property caused by fire, explosion, lightening earthquake, malicious damage with optional cover for flood
Section 4 Theft	Definition of what is covered and exclusions. Definitions specific to the section. Limit of liability under the section. Covers theft of property including, business machines, keys and stock.	Typically excludes cover for motor vehicles and personal property left out in the open. Often requires the theft to be by violent or forcible entry.
Section 5	Definition of what is covered and exclusions. Definitions specific to this section. Limit of liability under the section.	Typically covers loss of gross profit. May only cover loss arising from a cause insured under another section – eg fire or theft.
Section 6 Fidelity Guarantee	Definition of what is covered and exclusions. Definitions specific to this section. Limit of liability under the section.	Covers loss caused by fraud or dishonesty of an employee committed in the course of employment
Section 7 Personal Injury	Definition of what is covered and exclusions. Definitions specific to this section. Limit of liability under the section.	Provides specified sums in compensation for personal injury to proprietors or employees from accident or assault

Figure 1

In what follows we will analyze, *The Financial Conduct Authority v Arch Insurance and Others*[196] as an example of policy interpretation and causation.

Background to the case

On 6 March 2020, a potentially fatal disease, known colloquially as 'COVID-19 ' became a 'notifiable disease' in England and Wales, meaning that under the Public Health (Control of Disease) Act 1984 any occurrence had to be notified to the local authority covering the location of the outbreak. On 21 March, following extensive non-binding 'stay-at-home' social distancing guidance, Regulations were put in place requiring most businesses to close and requiring individuals to remain in their homes except in a limited number of circumstances, in order to slow the spread of the disease. As a result many businesses were forced to close, while others suffered a reduction in trade through reduced footfall. Some of these businesses had business interruption cover as part of commercial combined policies but the insurers generally refused to pay on the basis that the policies did not cover loss of income arising from a pandemic. They also pointed out that cover for such incidents was not priced into the product and so loss caused by a pandemic was not intended to be covered.

There were a large number of companies which had issued policies with such extensions and each had its own, separate policy wording so it could be anticipated that there would be a lengthy and expensive delay as the courts determined whether there was coverage on a case-by-case basis. At the same time there was considerable political pressure on insurers to pay valid claims rapidly, not least because under the furlough scheme the government was providing businesses with finance to enable them to survive, which was not available to businesses which had valid claims against an insurer. Similarly, under the Conduct of Business Rules issued by the Financial Conduct Authority, an insurer is required to act 'honestly, fairly and professionally in accordance with the best interests of its client'[197] and this obviously requires rapid settlement of valid claims. On the other hand the potential costs of meeting COVID-19 related claims business interruption claims was estimated at £2bn[198] so it was commercially impossible for insurers to admit liability without being sure that they had to pay the claims.

After discussions between the relevant parties it was decided that the Financial Conduct Authority should bring a test case against eight insurers to test the wordings of a representative sample of policies covering a variety of the range of main insuring clauses on the market.[199]

[196] [2021] UKSC 1, [2021] AC 649.

[197] Conduct of Business Sourcebook Rule 2.1.1.

[198] Confirmed by the Association of British Insurers, the insurance industry trade body. It seems this was an over-estimate.

[199] The Financial Conduct Authority estimated that 700 types of policies across over 60 different insurers and 370,000 policyholders could potentially be affected by the test case.

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Analysis of Sample Wordings

Principles of construction to be applied

At first instance Flaux J set out the accepted principles for the construction of insurance policies which are summarized here for ease of reference:

1. 'The court must ascertain what a reasonable person, that is, a person who has all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract, would have understood the contracting parties to have meant by the language used . . . This means disregarding evidence about the subjective intentions of the parties.'[200]
2. 'Contractual interpretation is a unitary exercise; where there are rival meanings, the court can give weight to the implications of rival constructions by reaching a view as to which construction is more consistent with business common sense. Bearing in mind the quality of drafting and that one side may have agreed to something which with hindsight did not serve his interest.'[201]
3. The unitary exercise of interpreting the contract requires the court to consider the commercial consequences of competing constructions, but not so as to rewrite a contract to assist an unwise party, or to penalize an astute party. Where the parties have used unambiguous language, the court should apply it.[202]
4. As a matter of construction not rectification, where the background and context clearly show that 'something must have gone wrong with the language' the court can interpret the agreement in context to 'get as close as possible' to the meaning which the parties intended but only if it is clear what correction should be made.[203]
5. Arguments relying on what is absent from the drafting of the contract often provide little assistance; for example, if in an insurance policy one cover is subject to an exclusion whereas another is not, the absence of that exclusion in respect of the latter cover is not decisive as to its scope.
6. If a clause in an insurance policy covers, or excludes, the risk of damage to a number of items, it is likely that the words used denote things of the same genus (*ejusdem generis*), and each word can take its meaning from the words with which it is linked or surrounded (*noscitur a sociis*) but only if there *is* a common characteristic and always subject to contrary circumstances.
7. Terms in an insurance contract expressed as 'exclusions' should not be construed as if they were exclusion of liability clauses for breaches of duty, they are there to define the limits of cover. In particular the *contra proferentem* 'rule' may have no real application, but if it does it exists where ordinary principles of construction cannot resolve a genuine ambiguity.

The Supreme Court approved of Flaux J's summary in respect of points 1–5 but did not refer to the final two points.

The Construction of Representative Insuring Clauses—Example: RSA 3

One of the clauses selected for particular attention by both the court at first instance and the Supreme Court was the policy identified as RSA3, a Commercial Combined Policy. Though each of the representative policies received consideration the principal

[200] *FCA v Arch Insurance and Others* [2020] EWHC 2448 (Comm) [62].
[201] *Wood v Capita Insurance Services Ltd* [2017] UKSC 24, [2017] AC 1173, Lord Hodge [11].
[202] *FCA v Arch Insurance and Others* [2020] EWHC 2448 (Comm) [64].
[203] ibid [65]

issues concerning construction are illustrated in the analysis of this wording. The policy was issued principally to building contractors, landscape gardeners, and manufacturers and wholesalers of electronics, fabrics, and metal goods. As is typical, the policy had a number of sections covering inter alia property damage, and business interruption. The policyholder could select which sections should apply to his policy and these were specified in that policy schedule.

The policy provided insurance in respect of the business premises of the insured and the business carried on there. It contained 'General Provisions' applying to all sections and general definitions, including those identifying the business premises (the '***Premises***' and the '***Business***').

The relevant part of the main insuring clause for Business Interruption read as follows:

We shall indemnify ***You*** in respect of interruption or interference with the ***Business during*** the ***Indemnity Period*** following:

a) any
  i. occurrence of a Notifiable Disease (as defined below) at the ***Premises*** or attributable to food or drink supplied from the ***Premises***;
  ii. discovery of an organism at the ***Premises*** likely to result in the occurrence of a Notifiable Disease;
  iii. occurrence of a Notifiable Disease within a radius of 25 miles of the ***Premises***. . .

  Additional Definition in respect of Notifiable Diseases

1. Notifiable Disease shall mean illness sustained by any person resulting from:
  i. food or drink poisoning; or
  ii. any human infectious or human contagious disease excluding Acquired Immune Deficiency Syndrome (AIDS) or an AIDS related condition an outbreak of which the competent local authority has stipulated shall be notified to them. . .

The policy was 93 pages long and contained the following exclusion on page 93:

Applicable to all (relevant) sections. . . (t)he insurance by this Policy does not cover any loss or Damage due to contamination pollution soot deposition impairment with dust chemical precipitation adulteration poisoning impurity epidemic and disease . . .

Three main issues arose in relation to this policy:

1. What did 'any . . . occurrence of a Notifiable Disease within a radius of 25 miles of the Premises' mean? Did it mean:
  (a). that the clause only covered the business interruption consequences of any cases of a Notifiable Disease which occur within a radius of 25 miles of the premises insured (RSA's argument)? or
  (b). the business interruption consequences of a Notifiable Disease wherever the disease occurs, provided there was at least one case of illness caused by the disease within the 25-mile radius (FSA's argument).

The court at first instance had accepted the FCA's interpretation, firstly because the clause 'is not expressly confined to cases where the interruption has resulted only from the instance(s) of a Notifiable Disease within the 25 mile radius. . .'[204] The second

[204] *FCA v Arch Insurance and Others* [2020] EWHC 2448 (Comm) [102].

reason was that the list of notifiable diseases at the time of the inception of the policy included diseases capable of dissemination over a wide area, therefore the parties must have contemplated:

> that the authorities might take action in relation to the outbreak of a notifiable disease as a whole, and not to particular parts of an outbreak, and would be most unlikely to take action which had any regard to whether cases fell within or outside a line 25 miles away from any particular insured premises.

The majority in the Supreme Court[205] preferred RSA's interpretation pointing out that as a matter of the English language the wording was clear, the insured peril defined in para iii was (using the policy definition of notifiable disease) business interruption following:

> the occurrence of a(n) illness sustained by any person resulting from . . . any human infectious or human contagious disease an outbreak of which the competent local authority has stipulated shall be notified to them, within a radius of 25 miles of the premises . . .

this was not a case where 'there was something wrong with the language'.

2. The Effect of the Exclusion. The general exclusion stated that the policy did not cover any 'loss or Damage due to . . . poisoning epidemic and disease.' Literally read therefore it meant that loss following the outbreak of a notifiable disease was excluded, notwithstanding its express inclusion in the Business Interruption section. RSA argued that where there were two apparently inconsistent clauses in a contract a court should assume that the parties intended that effect should be given to each of them and where possible find a construction that if possible reconcile them. RSA accepted that there could be no reconciliation between the definition of Notifiable Disease and the exclusion for the words 'disease' or 'poisoning' since if these words of the exclusion applied then the definition of Notifiable Disease would be in effect any '. . . illness sustained by any person resulting from . . . poisoning or . . . human . . . disease. . . excluding loss or Damage due to. . . poisoning . . . and disease'! However RSA argued, effect could be given to the word 'epidemic' thus excluding loss through the COVID-19 epidemic from cover. Both the court at first instance and the Supreme Court dismissed this construction on the basis that the assumption that the parties intended effect should be given to each of two competing clauses was not appropriate where the parties cannot be assumed to be holding both clauses under consideration at the same time. Here this was not the case. The possibility that hypothetical reasonable reader (not an insurance lawyer) reading the general exclusion on p 93 of the RSA 3 would understand it as removing a substantial part of the cover for business interruption apparently conferred on p 38 was ' as unreasonable as it is unrealistic.' The reasonable reader would assume that is such was the intention it would have been placed within the Business Interruption section of the policy.
3. Causation. As we have seen, the Supreme Court held the insured risk was an outbreak of COVID-19 within a 25 mile radius of the insured premises and not as the FCA had argued the outbreak of COVID-19 generally. It follows therefore that the only loss covered under the policy, was loss, the proximate cause of which, was the occurrence of the disease within that radius.[206] RSA argued that as an absolute minimum, for a cause of loss to be a proximate cause it had to pass the 'but for' counterfactual test, i.e. 'but for [events other than the insured risk] would the loss still have occurred? If not then the insured risk is not the proximate cause of the loss.' When applied to the facts of the case the test gives rise to this question:

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[205] Lord Hamblin (who gave the majority opinion) Lord Reed and Lord Leggatt.

[206] By virtue of s 55 Marine Insurance Act 1906 which states '. . . unless the policy otherwise provides, the insurer is liable for any loss proximately caused by a peril insured against, but, subject as aforesaid, he is not liable for any loss which is not proximately caused by a peril insured against.'

But for the outbreak of COVID-19 outside a 25 mile radius of the business premises would the government still have passed the March 21st Regulations? The Supreme Court concluded the answer was probably no.[207]

However the court held that, whilst the 'but for' test was determinative in the vast majority of insurance cases there were some in which it was not.[208] The most obvious instance was that it throws up a huge number of false positives. Taken to extremes the 'big bang' would pass the but for test of causation of COVID-19 since without it there would be (presumably) nothing at all.[209] The Court also referred to cases like *The Miss Jay Jay*[210] where there are two concurrent proximate causes which both pass the but for counterfactual test since they were both necessary but neither was sufficient in itself to cause the loss and where each is of equal importance.[211]

Less trivially the court pointed to circumstances where it appears that what can properly be called a cause of a loss can fail the counterfactual test, citing a hypothetical example where two fires break out simultaneously in a factory either of which would have been sufficient on its own of destroying the property. Were we to ask, 'if fire A had not occurred would the factory have burned down?' the answer would be 'Yes – fire B would have destroyed it' and of course vice versa so neither fire passes the test. Paradoxically we are, so the argument goes, left with a fire with no cause. Similarly, if a crowd of 20 people push a bus over a cliff, when only 14 would have been sufficient for the task it cannot be said of any individual that but for his efforts the bus would not have been damaged yet each member of the crowd individually could be regarded as a cause of the loss.

Therefore the Court reasoned, if, as in *The Miss Jay Jay*, we can have multiple concurrent causes and as in the bus example each cause on its own might not be sufficient to cause the loss then there is nothing in principle:

which precludes an insured peril that in combination with many other similar uninsured events brings about a loss with a sufficient degree of inevitability from being regarded as a cause - indeed as a proximate cause - of the loss, even if the occurrence of the insured peril is neither necessary nor sufficient to bring about the loss by itself. It seems incontrovertible that in the examples we have given there is a causal connection between the event and the loss.[212]

The Court then stated: 'Whether that causal connection is sufficient to trigger the insurer's obligation to indemnify the policyholder depends on what has been agreed between them' that is to say it is a matter of contractual interpretation. The main insuring clause as we have seen read as follows:

We shall indemnify **You** in respect of interruption or interference with the **Business** during the **Indemnity Period** following[213]. . . any occurrence of a Notifiable Disease. . . within a radius of 25 miles of the **Premises**. . .

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[207] Lord Hamblen and Lord Leggatt with whom Lord Reed agreed [179]. Lords Hodge and Briggs did not dissent on this point. In fact, during the first 'wave' there were places which were subject to national controls but which had no incidence of COVID-19 namely The Isles of Scily and some of the Western Isles of Scotland.

[208] Lord Hamblen and Lord Leggatt [181].

[209] My example not the Court's.

[210] *Lloyd Instruments Ltd v Northern Star Insurance Co Ltd (The Miss Jay Jay)* [1985] 1 Lloyd's Rep 264 QBD (Comm).

[211] Cf *Wayne Tank & Pump Co Ltd v Employers' Liability Assurance Corpn Ltd* [1974] QB 57 (CA).

[212] [2021] UKSC 1, [2021] AC 649 [191].

[213] It is important to note that the Court had concluded that in insurance policies the word 'following' was synonymous with such expressions as 'as a result of' or 'in consequence of' stating: 'We do not think it profitable to search for shades of semantic difference between these phrases.' ([2021] UKSC 1, [2021] AC 649 [162]).

The FCA argued that the causation requirement of this clause would be met if there was one case of COVID-19 within the radius and the Court preferred this interpretation. It argued that the parties could be presumed to know that at the time of inception of the policy there were already some notifiable diseases which had caused epidemics—for example SARS—and so a reasonable person would therefore suppose that some occurrences of notifiable diseases at least could be widespread and not confined to geographical area. Consequently such a reasonable person would not conclude that the test for causation was to ask whether the financial losses would still have been incurred even if there were only cases outside the radius.[214]

As an additional support for this view the Court pointed out that the wordings did restrict cover to cases where the loss was solely caused by occurrences of notifiable disease within the radius which would have been an easy addition to the section of the policy.

In summary therefore, for the purposes of this wording, occurrences of notifiable disease both inside and outside the 25 mile radius were to be regarded as concurrent causes of the 21 March Regulations even though no one particular occurrence was sufficient in itself to have caused the Government to act. As a result the insurer was liable for the financial consequences to the insured business of the COVID-19 epidemic.

Comment

1. The majority of the judges[215] considering the wording concluded that the insured peril as set out in the main insuring clause was an outbreak of a notifiable disease which led in turn to the 21 March Regulations, and to treat the radius limitation not as defining the insured peril 'but as a condition for cover which required the disease first to have spread within the radius.'[216] However Lord Briggs (who gave the minority dissenting judgment in the Supreme Court) accepted that linguistically this is not what the clause says, but pointed out, that to decide otherwise would (but for the concurrent causation analysis of the majority) have rendered illusory, the ostensible cover for COVID-19. With respect, cover for an epidemic of COVID-19 is obvious only on a cursory reading, as he says the wording is linguistically clear. A more careful reading of the wording could reconcile the apparent anomaly which *prima facie* may seem to extend cover to COVID-19, namely that cover was provided for loss caused notifiable diseases which were *capable* of being part of an epidemic but only if the outbreak was local.

The reasoning on both sides of the divide is not without its flaws, but the fact there was a divide at all demonstrates how problematic it can be in construing the terms of a contract applying the reasonably informed hypothetical reader. There is a danger, where one of the parties is in effect a 'consumer' to assume poor quality reading and thinking skills and to find ambiguity because of this.[217] There is also a temptation to find ambiguity where there really is none, failing to heed the warning in *Rainy Sky*[218] that the court should apply unambiguous language especially as this was not a case where the quality of the drafting was generally poor nor was the lack of cover for epidemics uncommercial.[219]

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[214] [2021] UKSC 1, [2021] AC 649 [195].

[215] Lords Briggs and Hodge in the Supreme Court and Flaux LJ and Butcher J in the High Court.

[216] [2021] UKSC 1, [2021] AC 649. Lord Briggs with whom Lord Hodge agreed [318].

[217] Or, paradoxically, extraordinary feats of philosophical sophistry, at least if the reader to get to the 'right' answer for the right reason– see Comment 2.

[218] *Rainy Sky S A and others v Kookmin Bank* [2011] UKSC 50, Lord Clarke [23].

[219] See Comment 4 below.

In fact, in this case the abilities of our reasonably informed hypothetical reader should not have been assumed to correspond only with those of the general population. Since RSA3 policies could only be bought through insurance brokers, the appropriate skills and knowledge to be assumed by the Court should surely have been those of a reasonably informed insurance professionals accustomed to the niceties of insurance wordings, leaving even less room for plausible non-literal constructions.

2 The construction placed on the main insuring clause by both judges in the High Court and the minority in the Supreme Court meant they could avoid the issue of causation altogether. But once we adopt the view of the majority in the Supreme Court there is a real difficulty for the 'reasonably informed hypothetical reader'. Paraphrasing Lord Briggs, 'if such reader (rather than an insurance lawyer)'[220] were asked 'does this policy provide cover financial loss following business interruption caused by the March 21st Regulations?' It is perfectly conceivable that they would say 'Yes' (i.e. get the right answer) but he felt it was highly unlikely they would get it for the right reason by answering:

Yes, even though the Regulations would have been imposed had there been no COVID-19 in the vicinity of the business premises such that the loss would have been incurred anyway, so long as there is at least one case of COVID-19 within 25 miles of the premises there is cover; each occurrence of a case of COVID-19, whether inside or outside the radius, is as causally potent as any other case or cases because of the law about non-excluded concurrent cause.

This is particularly unlikely since the hypothetical question would have been asked at the inception of the policy when the possibility that law about non-excluded concurrent cause included cases where the relevant cause was not a necessary part of the chain of causation was only being seriously discussed by philosophers. That said Hamblen J had dealt with a similar situation in *Orient-Express Hotels v* Generali[221] where the insured risk was loss of income through business interruption caused by damage to an hotel in New Orleans. The hotel was damaged by Hurricane Rita and had to be closed while it was repaired. However there was a mandatory evacuation of the whole of New Orleans because of the hurricane throughout the period of closure so that even if the hotel had not been damaged it would still have suffered the same loss. Hamblen J, applying the 'but for' test, held that the damage to the hotel had not caused the loss though he accepted that:

there may be cases in which fairness and reasonableness require that [the but for test] should not be a necessary condition (for example where otherwise) . . . there is no cause of the loss.[222]

Of course, the application of the test in *Arch* does not leave no cause of loss, nevertheless Lord Hamblen overruled his decision in *Orient Express*.

3. The Supreme Court held that the causation is a mixed matter of law and fact[223] and that whether the causal connection between insured risk and loss is sufficient to found liability is a matter of what was agreed. To an extent this is uncontroversial. Whether one event was 'caused' by another is indeed determined by applying a legal test (in effect the common sense view of the reasonably informed person) to the facts.[224] It is also uncontroversial that the terms of an insurance contract can substitute a different

[220] In fact, even *this* insurance lawyer believed that, except where a policy specifically negates the requirement, an insured risk had as a minimum to meet the 'but for test' to have a sufficient nexus to the proximate cause of the loss.

[221] *Orient-Express Hotels v Generali,* [2010] EWHC 1186 (Comm). [222] [33]. [223] [191].

[224] For an example of this test in action, suitably amended to a marine cargo insurance application see *TM Noten BV v Harding* [1990] Lloyd's Rep 283 (CA) Lord Bingham [288]. It is worth noting that in this case there was a dispute about what this 'sage' would conclude.

test of causation rather than require the search for a 'proximate cause', for example including words like 'howsoever caused' or 'whether caused directly or indirectly. It is equally possible to imagine wordings which do away with the need to comply with the 'but for' test even where it takes the cause outside the chain of causation. What is more controversial is the imputation to the parties, aware as they were, that sometimes there can be epidemics of notifiable diseases, that they intended to depart from a 'but for' counterfactual test in the absence of a clear wording or that applying it produced clear commercial nonsense. After all, in normal life reasonable people regularly (normally?) apply the test as the *sole* criterion of causation.

4. Support on the non-applicability of the 'but for' counterfactual test was found by the Court from the fact that it was:

> contrary to the commercial intent of the clause to treat uninsured cases of a notifiable disease occurring outside the territorial scope of the cover as depriving the policyholder of an indemnity in respect of interruption also caused by cases of disease which the policy is expressed to cover.[225]

At first blush, and put this way the argument appears plausible. But if we view the clause both from the insurer's and the consumer's points of view providing cover for localized outbreaks of notifiable diseases (but not epidemics) is totally commercial. RSA's general insurance portfolio included many thousands of policies of this and similar types issued to businesses throughout the country. As we know the financial impact of a disease on a business is totally unpredictable but by providing cover only in the case of a localized outbreak it meant that the number of valid claims arising from any one outbreak would be comparatively low and so a comparatively low premium could be charged for the cover. Clearly, this knowledge would not be available to the 'normal' 'reasonably informed hypothetical reader' but would have been self-evident to a professional insurance broker acting for the policyholder. It is surprising this issue was not considered.

The fact that the insurer could have included a specific exclusion for epidemics was also a reason given for the Court's conclusions on causation, perhaps failing to heed the warning given in the Court of Appeal in *Netherlands v Deutsche Bank AG*[226] and repeated by Flaux J at first instance, that arguments relying on what is absent from the drafting of the contract often provide little assistance, made all the more surprising by the fact that the Court itself had approved the warning 150 paragraphs earlier in its judgment.[227]

5. The hypothetical examples of instances of concurrent events collectively causing a loss but being individually insufficient to do so given by Lord Hamblen deserve closer inspection. In the case of the bus and the cliff it might well be asked—isn't the proximate cause the reason more likely to be why the crowd acted as they did since crowds generally don't attack buses without cause rather than focusing solely on the actions of any individual since in an insurance context it is unlikely that whether any individual member of the crowd caused the loss would be relevant. For example, imagine an insurance against damage to a bus company's property 'caused by an employee'. Suppose an employee was among the crowd that destroyed the bus so as to clear the roadway to permit the passage of emergency vehicles. It is at least plausible to argue that the common sense view in this example would be that the loss of the bus was proximately caused by the same event which necessitated the passage of the ambulances and fire engines. In other words this is not a case where applying the 'but for' test results in an event with no cause.

[225] [2021] UKSC 1, [2021] AC 649 [195].
[226] [2019] EWCA Civ 771 at [59].
[227] [2021] UKSC 1, [2021] AC 649 [195] [47]

The other example given involves a multitude of people individually and not in concert, adding a teaspoon of water to a flooding river or adding a match to a raging forest fire. Should such trivial contributions be ignored as *de minimis* or can they be regarded as causes? The answer in an insurance context, as the Court says, depends on what has been promised by the insurer. Suppose the risk insured is 'property damage arising from flood other than by caused malicious hand'. Whether and to the financial extent the policy provides cover is a matter of fact. If, for example, the insurer can show that no damage would have arisen if the malicious members of the multitude had not added their teaspoons of water, then the risk insured did not cause the loss. The question whether any one individual could be said to have caused the flood is immaterial to causation. Similarly if as a matter of fact the flood would still have caused damage, but the teaspoons increased that damage then that increase is not covered but the non-malicious damage is.[228] But note, in each case the cause of loss would meet the 'but for' counterfactual test.

It needs to be asked whether the examples given by Lord Hamblen really support his contention that, at least in an insurance context, and outside a legal philosophy seminar, (which are generally not overpopulated with 'reasonable readers') there is nothing in principle why a cause need be part of a chain of causation at least outside cases involving fault based liability like tort or crime.[229]

6 It seems surprising that the majority in the Supreme Court concluded that the word 'following', in the main insuring clause ('business interruption . . . following . . . the outbreak of a Notifiable Disease') meant the same as 'as a result of' or 'in consequence of'. Taken literally 'following' seems to modify the need for a causal connection between the outbreak of the disease and the cause of the loss such that the only connection need be temporal and not causal in the strict sense of the word. In other words it could be construed as removing the need for 'but for' causation and thus avoided the need for consideration of the inapplicability of the 'but for' counterfactual as a matter of principle rather than of construction. The Court's construction accords with common legal understanding but the Court itself noted that 'following' might be construed as modifying the normal need for causation so one is left wondering why the Court did not apply the hypothetical mind of the reasonable reader to the word rather than accepting a technical construction.[230]

Conclusion

- Insurance provides a vital service to the British economy in transferring risk of loss from individuals and organizations which are incapable of bearing the loss to organizations that are.
- In order to be able to claim on insurance the insured must be able to show that the loss was caused by a risk covered by the policy, and that he had an insurable interest in the subject matter of the insurance.

[228] Assuming the clause is not construed as excluding liability for flood if any of the flood is attributable to malicious hand.
[229] Perhaps after *Arch* a chain provides the wrong analogy. Perhaps a cable is a better one since it can have multiple strands which at some points of the cable length are necessary and sufficient at others are necessary but insufficient for the cable to remain intact, while at other points the strands are insufficient and unnecessary on their own but collectively are both necessary and sufficient.
[230] 2021] UKSC 1, [2021] AC 649 [162].

- Most insurance indemnifies the insured against actual loss.
- Structurally an insurance contract typically contains a main insuring clause identifying the risk covered, exclusions from that cover, and warranties which may be conditions precedent to the insurer's liability, suspensory warranties or risk specific warranties.
- Under the 2015 Act an insurer can only decline a claim for breach of a warranty if the breach would have increased the likelihood of loss of the type which occurred.
- Insurance contracts are contracts of utmost good faith but the duty to disclose all material facts along with extensive warranties and 'basis of the contract' clauses operated to the advantage of the insurer until the Insurance Act 2015.
- Under the 2015 Act utmost good faith now imposes a duty of 'fair disclosure' on the insured. Insurers can avoid the contract for a non-fraudulent breach only if without it they would not have covered the risk.