



# GOOD FAITH AND (RE)INSURANCE CONTRACTS IN THE UNITED ARAB EMIRATES

**Holman Fenwick Willan recently acted on behalf of an insurer in a landmark case in the UAE courts concerning breaches of the duty of good faith<sup>1</sup>: the insurer successfully counter-claimed against an assured in the Abu Dhabi Courts for rescission of a marine hull insurance policy on the grounds that the assured failed to properly disclose and/or misrepresented its previous claims history in the proposal form at the time of placement.**

The Abu Dhabi Supreme Court accepted that the previous claims history was material for the purposes of Article 385(b) of the UAE Maritime Law, ordered that the policy be rescinded *ab initio* in accordance with Article 388 of the same law, and rejected the assured's claim for a total constructive loss.

In this Briefing we consider good faith under UAE law, what it means for the insurer, the assured and their agents.

## Introduction

The parties to contracts of insurance and reinsurance governed by UAE law are subject to the obligation to perform the contract in "good faith". The position is therefore similar to that in common law jurisdictions where the doctrine of "utmost good faith" applies to such contracts. There are, however, some important differences, which we discuss below.

1. Case No. 434 of 2013.



## Contracts subject to UAE Law

In the UAE, all contracts, including reinsurance and insurance contracts, are governed by the Civil Code (Federal Law No. 5 of 1985). This sets out the law relating to contracts in general and includes provisions that specifically apply to insurance contracts. The Maritime Code (Federal Law No. 26 of 1981) applies to Marine Insurance Contracts.

These codes are supplemented by the Directives of Professional Practice and a Code of Conduct for Insurance Companies issued by the UAE's Insurance Authority (Insurance Authority Resolution No. 3 of 2010 (the IA Directive)).

### A general obligation of "good faith"

In common law jurisdictions, the doctrine of good faith only applies to certain types of contract, including (re)insurance contracts. By contrast, under the Civil Code there is a general obligation to perform any contract that is subject to UAE law in "*a manner consistent with good faith*" (Civil Code Article 246). The obligation applies to all contracts.

In addition, under UAE law, a party's obligations under the contract extend beyond what is expressly contained in the contract to include an obligation to do that which is related to the contract via law, custom or the nature of the transaction (Civil Code Article 246).

### Good faith and (re)insurance contracts

Articles 1026 to 1055 of the Civil Code, which relate to insurance and reinsurance contracts, include further obligations on the parties to act in

"good faith". Indeed, insurance is defined in the Civil Code as a contract whereby the parties "cooperate" (Civil Code Article 1026).

Under UAE law the specific duties in respect of good faith are as follows:

#### 1. The assured's duties of disclosure pre and post placement

The assured is obliged to notify, at the time the contract is entered into, its insurer of all information which is of concern to an insurer when assessing the risk (i.e. assessing whether to underwrite the risk at all, or assessing the terms upon which it is prepared to do so, or assessing the premium) (Civil Code, Article 1032(b)). This is akin to the common law pre-contractual duty of good faith to disclose all the relevant information.

Under Article 1032(c) of the Civil Code, the assured has an additional post-placement duty to notify the insurer of any matter which would increase the risk during the period of cover.

If the assured acts in bad faith and conceals or provides false information to the insurer, the insurer may apply to rescind the policy and apply for a return of the premium (Civil Code, Article 1033(1)).

In the absence of bad faith, non-disclosure by the assured entitles the insurer to apply to rescind the contract. In these circumstances, the insurer must return the premium, either wholly or prorated in proportion to the time the

insurer was not on risk (Civil Code, Article 1033(2)).

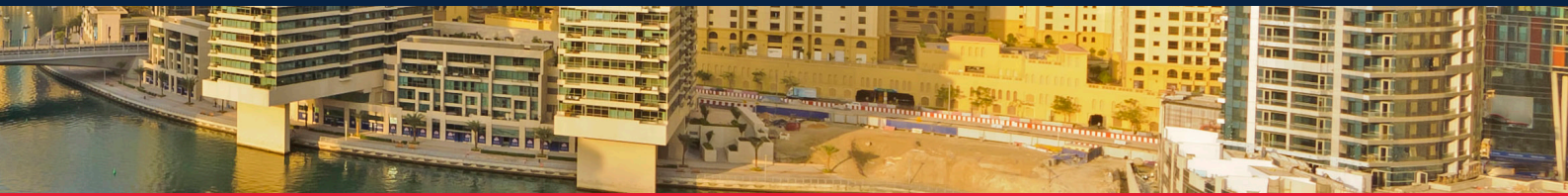
We note that in both situations the Civil Code says that the insurer has to "apply" to rescind the policy. In practice, this means the insurer should take proactive steps to enforce its rights in the event of breaches of the duty of good faith, either by immediately applying to the court to rescind the policy; or by making a counterclaim when faced by a court claim. If insurers simply rely on breaches of good faith as a defence without any further positive action, the court is unlikely to order the rescission of the policy.

#### 2. Marine insurance contracts

There are important differences regarding marine insurance so far as the assured's disclosure obligations are concerned.

As with non-marine insurance, under the Maritime Law, the assured is required to disclose information prior to inception and on an ongoing basis if the risk changes (Maritime Law, Articles 385(b) and (c)).

In the event of non-disclosure, the insurer may require the contract to be rescinded. Unlike the position under non-marine insurance, however, the Maritime Law expressly provides that this is the case even if the information does not relate to any damage suffered. Furthermore, if the assured acted in bad faith, the insurer can "receive" the premium in full; and absent bad faith the insurer can receive half of the premium.



### 3. The insurer's general obligations to act in good faith

From the insurer's perspective, it is obliged under a general duty of good faith when dealing with the assured, both under the Civil Code and the IA Directive. The latter requires the insurer to "*perform its works on the basis of the absolute good faith...*" (IA Directive, Article 3(1)). Furthermore, it is required to inform its staff about this and the other obligations in the IA Directive (IA Directive, Article 1.12).

### 4. The insurer's obligation to ask

The IA Directive must be read in conjunction with the Civil Code.

As we have seen, under the Civil Code, the assured has to disclose material information at the time of placement.

However, this may to some extent be tempered by the IA Directive which obliges the insurer to provide an application form both on placement and renewal (IA Directive, Article 6). This application form must include "*the questions related to the material facts*".

In other words, in the event of a material non-disclosure of information which was not specifically requested, the insurer may be unable to say that the insured breached its disclosure obligations on the grounds that had the information been material, the insurer would have specifically

asked for it. It remains to be seen how effective a "catch all provision" simply asking for all material information would be. Clearly proposal/application forms should be carefully drafted so as to request all material information.

### 5. The insurer's duty extends to claim handling

Under the Civil Code and IA Directive, the insurer is also obliged to exercise good faith in paying claims (Civil Code, Articles 246 and 1034, and IA Directive, Article 2).

It follows that it may theoretically be possible for the assured (i) to claim damages for breach of this duty of good faith when adjusting and settling claims (i.e. this would be similar to the punitive "bad faith" claims one sees in US insurance litigation) and/or (ii) to claim damages for consequential losses flowing from the insurer's breach. We are not aware of any cases in the UAE which have considered these issues and whether this would in fact happen remains to be seen.

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