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In this week's Insurance Bulletin:

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1. REGULATION AND LEGISLATION

EU warns insurers to prepare for hard Brexit

The EU's insurance regulator has issued an opinion paper warning insurers and financial services regulators to make "sufficient and timely" preparations to ensure continuity of service after Brexit for cross-border insurance risks. The paper, published by the European Insurance and Occupational Pensions Authority (EIOPA) on 21 December 2017, stresses that the insurance industry and regulators should not assume that any particular trade deal between the UK and EU will be negotiated. They should therefore take responsibility for fulfilling their insurance obligations as part of the sound and prudent management of their business, whatever the post-Brexit landscape might look like.

Most insurers will already be aware of their options for restructuring after Brexit, but these are set out in EIOPA's paper and include:

- The transfer of insurance contracts of UK undertakings with policyholders in the EU27 to an insurance subsidiary established in an EU27 Member State;
- The transfer of insurance contracts of EU27 undertakings with UK policyholders to an insurance subsidiary established in the UK;
- The establishment of a third country branch in the UK or in the EU27 Member State of the policyholder; and
- With regard to UK undertakings in the legal form of a European company, the change of domicile of the company to an EU27 Member State.

According to EIOPIA chairman Gabriel Bernardino: *"It is essential that insurance undertakings consider all eventualities, including the possibility of no political agreement at the date of withdrawal"…"I call on all insurance undertakings and national supervisors to plan effectively and take the necessary steps in good time to ensure that policyholders and beneficiaries are not exposed to unnecessary uncertainty regarding the status of their contracts."*

EIOPA's paper serves as a reminder that the post-Brexit landscape for insurers remains uncertain and that insurers should not make any assumptions about the kind of trade deal that will be reached. In particular, it is unclear whether a free trade deal will be agreed between the UK and EU in respect of financial services specifically. UK financial services regulators anticipate that there will be a transition period after the UK's formal exit from the EU, during which firms could continue to benefit from 'passporting' rights. However, the EU's chief negotiator Michel Barnier has stated that any trade deal after Brexit would not include financial services and that the UK will lose passporting rights as a result of its decision to leave the EU. Barnier has spoken of *"the red lines that the British have chosen themselves. In leaving the single market, they lose the financial services passport"*.

EIOPA's paper is here.

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2. COURT CASES AND ARBITRATION

Australia: "Accidental" damage and the importance of causation

The decision in *Sheehan v Lloyds Names Munich Re Syndicate Ltd*[1] provides guidance on defining accidental damage and the importance of causation in the context of insuring clauses and exclusion clauses in insurance policies.

The insured commenced proceedings in the Federal Court of Australia against his insurer seeking indemnity under a policy of insurance for 'accidental' loss and damage to the starboard engine of his motor yacht.

The damage occurred on 17 September 2015 approximately one day after the insured vessel had been

1 [2017] FCA 1340.

serviced. The vessel was operated for approximately five minutes before an alarm activated and the speed of both engines slowed down automatically to a 'limp' mode. Approximately eight minutes later, the starboard engine shut down completely and a subsequent mechanical inspection revealed extensive and irreparable damage.

A jointly-appointed expert referee considered that the damage was 'a direct result' of overheating and seizure of the engine due to loss of lube oil pressure, but also faulty design of the sealing arrangement between the lube oil cooler and the engine block.

The insurer declined indemnity on the basis that:

(a) the insured's failure to read the vessel manual, know about the operation of alarms, recognise their significance and act reasonably means the damage was not 'accidental'; or alternatively,

(b) certain exclusions in the policy were triggered including, amongst others, loss and damage arising from (i) faulty design; (ii) inherent defect; and (iii) structural design.

The Court accepted the insured's evidence that, despite the vessel manual stating that the alarm would trigger a warning on an LCD screen that the engine oil pressure was low, no such warning was displayed. The insured's evidence was that if it did, he would have turned off the engine. The Court held that the insured was not aware of the risk of damage to the engine by continued operation, and therefore could not have chosen to take that risk. Accordingly, the damage was 'accidental' within the meaning of the policy.

However, the Court also found that, notwithstanding the insured's failure to turn off the starboard engine as being a possible cause of the damage, the single proximate cause was the failure of the gasket due to its faulty design. Therefore, although the *Wayne Tank* principle (whereby when there are multiple proximate causes and one is excluded under the policy, the insured will be unable to recover) did not apply, the damage was nevertheless excluded under the policy.

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England and Wales: Broker seeks bank disclosure to assist in tracing missing premiums

This case[1] illustrates some of the difficulties encountered in interpreting inter-broker agreements for the run-off administration of existing risks.

According to the evidence cited by broker Miles Smith Broking Limited (MSB), MSB is being pursued for substantial unpaid premiums by the reinsurer on a 2001 excess of loss treaty which MSB placed. Some time after placing the treaty, MSB had entered into a broking "run-off" agreement with another broker, Square Mile Partnership Limited (SMP), which later collected the premium from the reinsured, but failed to pass it on to the reinsurer. It is not clear what became of the premium and SMP has since been dissolved, rendering it an unappetising target for a claim.

The reinsurer claims that the effect of the run-off agreement was that SMP acted as MSB's agent in collecting the premium and so MSB remained primarily liable for the failure to pay it over. On the other hand, MSB's position is that the run-off agreement made SMP and not MSB the broker which was liable to collect and pay sums due under the treaty.

MSB sought a *Norwich Pharmacal* order against SMP's bank, requiring disclosure of documents relating to SMP's bank account, in order to ascertain what had become of the premium and who at SMP was responsible for this. As is usual for *Norwich Pharmacal* applications, the application was not opposed by the subject bank, and MSB's evidence was unchallenged in the application, so Master Clark made no findings of fact.

On the assumed basis (which SMB denies) that SMP acted as its agent, as alleged by the reinsurer, SMB would itself be able to claim against those responsible for any misapplication of the premiums. Whilst the normal

1 *Miles Smith Broking Limited v Barclays Bank PLC* [2017] EWHC 2228 (Ch.)

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"...the Court also found that, notwithstanding the insured's failure to turn off the starboard engine as being a possible cause of the damage, the single proximate cause was the failure of the gasket due to its faulty design. Therefore, although the *Wayne Tank* principle (whereby when there are multiple proximate causes and one is excluded under the policy, the insured will be unable to recover) did not apply, the damage was nevertheless excluded under the policy."

position is that monies held in an Insurance Broking Account are not held on trust, there were features of the run-off agreement (including reference to a "sub-trustee") which caused Master Clark to find there was a good arguable case that MSB had a proprietary interest in the premiums in SMP's account (notwithstanding that the cedant or the reinsurer may have been the ultimate beneficial owner of the premiums). MSB was therefore in a position to complain of wrongdoing by SMP in misapplying the premiums, and had a good arguable case against the persons who procured mispayments to be made from the account (for e.g. inducing breach of trust) and those persons were likely to be SMP's directors. Master Clark found a *Norwich Pharmacal* order was needed since it would or may enable MSB to identify the persons responsible for instructing the bank to pay away the premiums and may enable MSB to defend the reinsurer's claim and he also said "the bank was mixed up in so as to have facilitated the wrongdoing", if any, and so the necessary elements were present to enable him to make the *Norwich Pharmacal* disclosure order, which he duly did, whilst pointing out that any right to confidentiality of its accounts which SMP may once have had no longer exists, since SMP no longer exists. Master Clark also found that MSB's proprietary interest in the premiums would entitle it to trace the premiums and that it is entitled to seek disclosure under Banker's Trust principles.

It remains to be seen which direction this matter takes after the relevant documents have been disclosed.

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3. HFW PUBLICATIONS AND EVENTS

France: HFW Paris Office Insurance team top tier ranking

We are delighted to announce that HFW Paris office insurance team has been ranked as a top tier law firm in the latest edition of the "Risk Management and Insurance" guide, published by Décideurs Leaders League.

The HFW Paris team, led by Guillaume Brajeux and Olivier Purcell, is described as being "at the forefront of innovation" and "very strong at managing complex and high profile cases." For further details please see the report here.

UK: Andrew Bandurka

We are delighted to announce that Andrew Bandurka has recently qualified as an accredited mediator, a Member of the Chartered Institute of Arbitrators, and a member of the ARIAS(UK) panel of experts/ arbitrators.

ANDREW BANDURKA
PARTNER

"Whilst the normal position is that monies held in an Insurance Broking Account are not held on trust, there were features of the run-off agreement (including reference to a "sub-trustee") which caused Master Clark to find there was a good arguable case that MSB had a proprietary interest in the premiums in SMP's account (notwithstanding that the cedant or the reinsurer may have been the ultimate beneficial owner of the premiums)."

MENAIR INSURANCE AWARDS 2017 WINNER

UK CAPTIVE 2017 SERVICES AWARDS WINNER LAW FIRM

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