Insurance/
Reinsurance

January
2012

# INSURANCE/ REINSURANCE BULLETIN


## Silence and inaction do not amount to estoppel

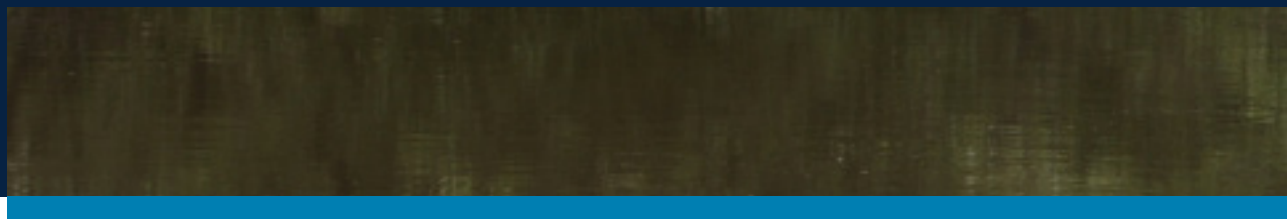
In our April 2011 bulletin (http://www.hfw.com/publications/bulletins/insurancereinsurance-bulletin-april-2011), we reported a decision of HH Judge Mackie QC in *Argo Systems FZE v Liberty Insurance (Pte)* in which insurers were estopped from relying on breach of a 'no hold harmless' warranty as a defence because they had not pleaded it in US proceedings nor indicated they would rely on it for seven years.

The Court of Appeal has overturned that judgement, applying a decision in *"The Leonadis D"* (1985) that silence and inaction cannot constitute an unequivocal representation as to whether a person would not rely on a particular legal right in the future.

Defendant insurers declined a claim from Argo following the total loss of the floating casino Copa Casino. The voyage policy for total loss was subject to English law and contained a warranty of *"no release, waivers or 'hold harmless' given to Tug and Towers"*. However, undisclosed to insurers and in breach of this warranty, the standard towing contract which was used contained a release of the tug owner who would not be liable for any loss or damage sustained by the tow, howsoever caused.

In a letter from the insurers' US lawyers rejecting the claim for total loss, insurers did not refer to the 'no hold harmless' warranty; nor did they seek to avoid the policy, although they reserved *"the right to alter [their] position in light of discovery of previously undisclosed information which would alter the facts and circumstances presently known... without prejudice to all the remaining terms and conditions of the policy, along with any other defences which may be discovered after further investigation."*

The Court of Appeal ruled that Judge Mackie was wrong to hold that the insurers had said they would not rely on other defences, such as the breach of the hold harmless warranty



unless new information came to light. The rejection letter was equivocal and, taken as a whole, indicated that the insurers were reserving rights to rely on other defences that might be discovered after further investigation. The Court of Appeal also ruled that the silence on the defence of breach of warranty until the English proceedings was also equivocal. There were no special circumstances capable of turning insurers' silence and inaction into an unequivocal representation that insurers did not intend to enforce its strict legal rights based on a breach of the 'no hold harmless' warranty. It therefore followed that there was no waiver or estoppel.

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"The rejection letter was equivocal and taken as a whole indicated that the insurers were reserving rights to rely on other defences that might be discovered after further investigation."

## Insurers prejudiced by "loss of chance" because of late claim notification

Insurers cannot usually completely reject late notified claims unless the insured's obligation to notify claims is a 'condition precedent'. Although insurers are entitled to set-off any damages they have suffered because of the late notice, many financial consequences of late notice have generally been considered too remote or too intangible to be recoverable. However, the decision in *Milton Keynes BC v Nulty* apparently opens the door to insurers to claim damages for 'loss of chance' where the delay in reporting circumstances could have prejudiced their ability to investigate the causes of the loss, and perhaps show that the loss was caused by something for which they would not be liable.

The judge found that a negligently discarded cigarette was the most probable cause of a fire at a recycling centre and that a subsequent (more serious) fire was probably caused by incomplete extinction of the first fire. There were, however, other possible explanations for each of the fires and the judge accepted that the late notification of the fires to the liability insurers of the person (now deceased) whose negligence was the "least unlikely" cause of the fires impaired the insurer's ability to investigate the claim thoroughly, and perhaps to demonstrate that one of the other possible causes had a higher probability of being the true cause.

"The judge found no logical means of quantifying the prejudice that insurers had suffered."

The judge found no logical means of quantifying the prejudice that insurers had suffered. However, he did not consider that it could be assessed at nothing and, based on his impression of the circumstances, assessed the prejudice to the insurer - *"in the form of its loss of opportunity to secure a different result"* at 15%. The insurer was allowed to set-off its claim for damages against its liability to indemnify the assured, effectively reducing the cover available by 15%.

It remains to be seen whether the reasoning in this case will be applied in other factual scenarios or in relation to claims under different types of insurance or reinsurance policy. Nevertheless, the scope for insurers to obtain an effective remedy for breach of notification clauses has clearly increased.

See *Milton Keynes BC v Nulty* [2011] EWHC 2847 (TCC).

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## Australia to adopt a standard "flood" definition

In 2010-11 there were a number of severe floods in Queensland, News South Wales and Victoria. Various briefings by HFW on the implications of these floods can be found at http://www.hfw.com/publications/client-briefings/australian-2010-2011-weather-event-losses.

In Australia, although a number of carriers provide cover for flood, not all carriers do. Those that don't provide cover generally exclude it through specific flood exclusions in their polices. There has been no uniform definition of "flood" in Australia. Previous attempts to arrive at a uniform definition failed to make it past the Government consumer watchdog on the basis that they simply might heighten confusion and possibly even be anti-competitive.

Following the 2010-11 floods, the Government undertook consultations with representatives of consumer groups, the insurance industry and the legal profession. In April 2011 the Government issued a discussion paper 'Reforming Flood Insurance – Clearing the Waters' which supported a uniform definition. In addition, the Government commissioned the Natural Disaster Insurance Review in March 2011 to examine the availability and affordability of natural disaster insurance and this Review Panel also recommended the adoption of the uniform definition.

Part V Division 1 of the *Australian Insurance Contracts Act 1984* (Cth) identifies that certain prescribed contracts of insurance, which include domestic housing contents and buildings policies, must have certain minimum levels of cover. If cover in a prescribed contract is less than the minimum, this must be notified clearly in writing to the insured to be enforceable. The *Insurance Contracts Amendments Act 2011* will introduce a new Division 1A to Part V which stipulates that for prescribed contracts entered into after the transition date (which is the date specified by the regulations when the new definition will come into effect) will have a standard definition of flood applicable to them. Machinery in the new Division specifies that the definition of flood in the regulations will apply even if the contract of insurance seeks to give a different definition of flood.

The draft regulations currently under consideration propose a definition of flood as follows:

*"the covering of normally dry land by water that has escaped or been released from the normal confines of any of the following:*

*A. A lake, river, creek or natural watercourse (whether or not it has been altered or modified).*

*B. A reservoir, canal or dam."*

The definition of 'flood' has been framed in a form that:

- Allows consumers to consider the extent to which the risk exists in their location.
- Is suitable for insurers to express either the inclusion or the exclusion of flood cover.
- Could be adopted without impacting negatively on the extent of flood cover currently provided.

The definition applies to lakes, rivers, creeks and other natural watercourses regardless of whether they have been altered or modified. This recognises that alterations and modifications do not fundamentally alter the nature of such watercourses.

However, the definition does not encompass the release of water from man-made watercourses. Therefore, water damage that results from the release of water from man-made watercourses does not constitute a type of 'flood'. Nor does the definition apply to sea surges, king tides or tsunamis, which although being prescribed insured events for prescribed contracts, are often excluded by most carriers.

It is intended that the standard definition of flood will also apply to policies covering small businesses and strata title residences. Submissions have been invited on the proposed definition of a strata title residence, flood, and small businesses, the latter currently being identified as a business with a turnover of less than $A1 million or with five (or fewer) employees. The closing date for submissions is 3 February 2012.

The regulations will come into force two years after they are made, thereby providing a two year transitionary period to enable carriers to make necessary alterations to their business.

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## Australian High Court upholds judgment that all material exposure to asbestos causes mesothelioma

In a December 2011 judgment which is consistent with that of the House of Lords in *Fairchild v Glenhaven*, the Australian High Court has held that the underlying NSW Supreme Court was correct to accept:

- That all material exposure to asbestos causes mesothelioma.
- That prospective risk of contracting mesothelioma increases with the period of significant exposure ("the cumulative effect mechanism").

HFW will be producing a fuller analysis of *Amaca v Booth* [2011] HCA 53 in January 2012. However, our preliminary view is that this decision is likely to have wide ranging implications, in NSW in particular, for the defence of mesothelioma claims which arise from incremental asbestos exposure attributable to multiple defendants. Unless the defendant(s) in question can produce evidence of an alternative operative cause, it will be difficult to deny liability.

"The case also raises the possibility that insurers (and reinsurers) may seek to re-allocate losses, pro rata, across the period(s) of exposure."

The case also raises the possibility that insurers (and reinsurers) may seek to re-allocate losses, pro rata, across the period(s) of exposure. Based on the principles that injury occurs on exposure and that, having negligently allowed exposure to asbestos, policy holders could only be liable for causing that injury once (per *Orica v CGU* and *Vero v Power Technologies*), many liability insurers of NSW risks have previously allocated common law liabilities for asbestos losses to the policy period covering the first negligent exposure. In light of *Amaca v Booth*, dependent upon their policy language, those insurers may seek to allocate loss across different (subsequent) policy years and, insofar as applicable, to insurers of different defendants who are also found to have exposed victims in breach of their obligations.

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## Digital satellite revisited

This case concerned the FSA's consideration of the warranty cover provided by Digital Satellite Warranty Cover Limited and another company and it highlights the FSA's interest in ensuring that regulated activities are conducted only by authorised or exempt persons.

In the High Court, the FSA argued successfully that these businesses had entered into contracts of insurance, a regulated activity, without authorisation and in breach of the general prohibition in the Financial Services and Markets Act 2000.

In November, an appeal by the companies against the decision to make winding up orders against them failed.

The companies provided "extended warranty contracts" in relation to satellite television equipment under which they repaired equipment or replaced that equipment. There was no obligation on the companies to pay money.

The judge, in agreeing there was a breach of the general prohibition, concluded that the contracts were insurance falling within the "Miscellaneous Financial Loss" category at schedule 1 of the Act.

The companies now argued that the original directive which the Regulated Activities Order implemented did not include benefits in kind insurance which is in fact what they were providing. The closest correlation was with class 18 of schedule 1 ("Assistance "), which could only be regulated in relation to assistance for persons who were travelling. They asserted that they were not providing insurance.

The Court of Appeal held that a risk covered by a contract providing for the repair and replacement of equipment, and one which provided an indemnity for the costs involved, was essentially the same. In both cases the risk was ultimately a breakdown of the equipment which would lead to expense on the part of the insured, or financial loss


attributable to incurring unforeseen expense or other risks. It was therefore within class 16 of schedule 1.

Going further, the Court held that the directives only laid down a minimum regulatory framework and did not exclude any government's right to extend regulation to a wider class of benefits in kind insurance.

Ultimately, it is absolutely clear that what is and is not "insurance" will be a question of fact in each case. We recommend that where the intention is to avoid carrying on a regulated activity, contracts are carefully constructed before being marketed (and that the marketing process itself is assessed), given the increased FSA scrutiny of such contracts.

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## Conferences & Events

Mining Claims Forum
London
(30-31 January 2012)
Paul Wordley

LexisNexis Webinar: Solvency II - what will it mean?
London
(9 February 2012)
Paul Wordley

2nd Energy Insurance Middle East Forum
Dubai
(14-15 February 2012)
Paul Wordley

World Space Risk Forum
Dubai
(28 February - 1 March 2012)
Nick Hughes, David Greves and Edward Newitt

If you are interested in receiving more information about any of these events, please contact events@hfw.com

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