Impairing insurers' ability to rely on a 'technicality' to avoid paying a claim: assessing section 11 of the Insurance Act 2015

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ABSTRACT

This paper assesses section 11 of the Insurance Act 2015. Introduced to redress the imbalance of interests between insurer and assured, its aim is to prevent insurers from avoiding claims in instances where, although the assured is in breach of a term, there is a disconnection between the breach and the loss. The section presents two specific uncertainties which this paper aims to address: (1) identifying the terms which are caught by the provision and (2) applying the relevant test for the link between the term and the loss, as detailed in section 11(3). In respect off (1), this paper focuses both on exclusion clauses, which are considered with reference to similar reforms in New Zealand and Australia, and insurance conditions; more specifically, identifying which conditions are within the scope of the section and examining how ambiguous provisions might be resolved. Finally, in respect of (2), this paper argues that an explicit causation requirement would have been a more appropriate reform.

1. Introducing section 11 of the Insurance Act 2015

The Insurance Act 2015 ('IA 2015') came into force on the 12th August 2016 and is one of the first pieces of comprehensive non-consumer insurance legislation to be adopted in the United Kingdom for over a century. Section 11 details "terms not relevant to the actual loss" which The Law Commissions – The Law Commission (England and Wales) and The Scottish Law Commission, indicated can include exclusions, conditions precedent and warranties.[1] The section, in the spirit of the reform of the Act, is clearly designed to protect the assured: it prevents insurers from avoiding claims in instances where, although the assured is in breach, there is a disconnection between the breach and the loss. The enactment of section 11, as drafted, was unchallenged in Parliament and by the insurance market.[2] While this suggests the provision is unambiguous and uncontroversial it is, however, unclear what the impact of this particular reform will be – it was an extremely controversial provision during the preceding consultations.[3]

Merkin and Gürses identified two principal difficulties: (1) identifying the terms which are caught by the provision and (2) applying the relevant test for the link between the term and the loss as detailed in section 11(3).[4] This paper takes these two difficulties as its focus and makes an attempt to explore them.

This paper therefore begins with a discussion unpicking the precise meaning of a term which "defines the risk as a whole" by outlining The Law Commissions' guidance, and searching for common law guidance. It then progresses, in section 3, to an analysis of exclusions, in an effort to identify whether there is in fact a distinction

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[1] Explanatory Notes to the Insurance Act 2015, para [94].

[2] Robert Merkin and Özlem Gürses, 'The Insurance Act 2015: Rebalancing the Interests of Insurer and Assured' [2015] 78 (6) *MLR* 1004, 1020.

[3] Insurance Bill' (HL) Paper 81 (2014) <https://publications.parliament.uk/pa/ld201415/ldselect/ldinsur/81/81.pdf>accessed August 2017, 5; Robert Merkin and others, Arnould: Law of Marine Insurance and Average (1st supplement, 18th edn, Sweet & Maxwell 2016), paras [1.3-91] – [1.3-94].

[4] (n 2).

between exclusions and terms which define the risk as a whole – courts will have to develop a sense of when a clause defines the risk and when it excludes liability or imposes a condition upon which liability depends.[5] This is contextualised by a comparison with New Zealand and Australian reform, where a distinction has been drawn between exclusions and inherent limitations on coverage, and an analysis of one recent Australian decision, *Pantaenius Australia Pty Ltd v Watkins Syndicate 0457 at Lloyds*,[6] aids this objective. Section 4 then considers which insurance conditions are within the scope of section 11 and how it might change their analysis. Finally, section 5 focuses on the meaning of section 11(3) in the wider context of causation and it is argued that an explicit causation requirement would have been a more appropriate reform.

The UK insurance market is the largest in Europe – the third largest in the world,[7] and contributes £29 billion to UK GDP.[8] The London Market alone is worth approximately £60 billion in gross written insurance premiums (including business managed by but not written in London)[9] and, as such, the insurance industry is a major UK export:[10] the development of insurance in London underpins wider economic growth and means that English insurance law is highly influential worldwide.[11] Put simply, the essence of section 11 of the IA 2015 is to eliminate once specific problem which dominated the London – and UK, insurance markets: the insurers' ability to exclude, limit or discharge their liability for a claim on the basis that the assured was in breach of a term irrelevant to the claim – often in an entirely technical sense. It was generally considered to be nonsensical that an insurer could refuse to pay a claim, for example, in the event of a building burning to the ground simply because the assured was in breach of a term to install and maintain a burglar alarm.[12] Section 11, therefore, works by targeting risk provisions in a policy – ie those provisions which reflect the underwriters' art in assessing the nature and likelihood of particular risks insured. If the assured is in breach of a term which aims to reduce the risk of loss of a particular kind, at a particular location or at a particular time, section 11 prevents an absurdity: if the assured can prove that their non-compliance with the term could not have increased the risk of the loss which actually occurred in the circumstances in which it occurred, the insurer cannot rely on the non-compliance to exclude, limit or discharge its liability under the contract.

[5] Robert Merkin and Özlem Gürses, 'Insurance contracts after the Insurance Act 2015' (2016) *LQR* 445, 458.
[6] *Pantaenius Australia Pty Ltd v Watkins Syndicate 0457 at Lloyds* [2016] FCA 1.
[7] Association of British Insurers, 'UK Insurance & Long Term Savings: Key Facts 2015', 1 <https://www.abi.org.uk/globalassets/sitecore/files/documents/publications/public/2015/statistics/key-facts-2015.pdf>accessed September 2018.
[8] ibid.
[9] M Magnus, A Margerit and B Mesnard,'Brexit: the United Kingdom and EU financial services', EU Parliament Briefing Paper, 9 December 2016, 7 <www.europarl.europa.eu/RegData/etudes/BRIE/2016/587384/IPOL_BRI(2016)587384_EN.pdf>accessed September 2018.
[10] David Hertzell, 'Reforms to UK insurance law: overview of key changes'<https://uk.practicallaw.thomsonreuters.com/6-615-6445?transitionType=Default&contextData=(sc.Default)&firstPage=true&comp=pluk&bhcp=1>accessed September 2018.
[11] ibid.
[12] (n 2).

2. Defining the risk as a whole

2.1. The Law Commissions' guidance

Section 11 of the IA 2015 does not apply to terms which "define the risk as a whole", yet what this means precisely is not clear – the phraseology is novel in the insurance statute law context, although at first glance it supposedly refers to terms which are not linked to a specific risk, but describe the limits of cover as a whole.[13] The Law Commissions indicated that the following are to be considered terms which define the risk as a whole:

- Terms which define the geographical area in which a loss must occur if the insurer is to be liable;
- Terms which define the age, identity, qualifications or experience of the operator of a vehicle, aircraft, vessel or chattel;
- Terms which exclude loss which occurs while a vehicle, aircraft, vessel or chattel is being used for a commercial purpose (cf. private/leisure use).[14]

Section 11 *does* apply to terms which are risk-mitigating for the purposes of section 11(1) – ie terms which tend to reduce the risk of loss of a particular kind, at a particular location or at a particular time. The issue of whether a term can, in some instances, define the risk as a whole and also be aimed at mitigating a risk is an important one which is considered in 4.4 below.

2.2. Searching for common law guidance

Three cases are informative. In the first, *Brit UW Limited v F & B Trenchless Solutions*, the dispute centred on the exact purpose of a pre-contractual representation, summarised by the underwriter in written evidence presented to the court as follows: "[i]t is just a *risk as a whole* (…) there is inherent risk with tunnelling". The court accepted the submission:[15] the inherent risk involved in tunnelling work appears to have underpinned the entire contract, as drafted, which appears to support the proposition that if a provision details the very essence of the risk, it necessarily defines the risk as a whole. The policy in the second case, *Harding Maughan Hambly v Compagnie Europeenne de Courtage D'Assurances et de Reassurances*,[16] concerned political risk and the issue was whether a broker could be said to have been the effective cause of the policy's placement. Rix J construed the provisions of draft and final documents to identify who the co-assureds were and remarked that the changes in the said documents "*emphasise[d] the difficulty of regarding the risk as a whole as based on the expropriation of* [certain] *assets*".[17] In so doing, Rix J was apparently referring to the essence – the very foundation, of the risk. The third case, "*Ho Feng No 7"*,[18] is a marine cargo case which owes its relevance to the fact that Hong Kong's law of warranties is modelled on the English Marine Insurance Act 1906 (MIA 1906). The insurer successfully

[13] Baris Soyer, 'Risk control clauses in insurance law: law reform and the future' (2016) *CLJ* 109, 121.
[14] Law Commission, *Insurance Contract Law: Business Disclosure; Warranties; Insurers' Remedies for Fraudulent Claims; and Late Payment* (Law Com No 353, 2014) para [18.33].
[15] [2015] EWHC 2237 (Comm), 157 (emphasis added).
[16] [2000] CLC 524.
[17] ibid, 540 (emphasis added).
[18] *Hua Tyan Development Ltd v Zurich Insurance Co Ltd ("Ho Feng No 7")* [2014] HKEC 1489.

relied upon the assured's breach of a deadweight warranty after a vessel sank in bad weather and the cargo was destroyed. However, the vessel might have sunk if the warranty was complied with. The insurer would argue, under the Act, that the deadweight warranty was risk-defining. Yet the assured would argue it reduced the risk of a particular kind. This is one example of many cases which illustrate the increased importance of drafting terms clearly, setting out its requirements and consequence for non-compliance.

Thus, the common law appears to reaffirm the view that a term defines the risk as a whole if it describes the limits of the cover as a whole. The purpose of the insurer's risk-assessment process, which is undertaken prior to a policy of insurance being underwritten, is to determine the nature of the risk(s) insured and the scope of cover; it therefore follows that when this process is rendered dispensable, by the fact of the loss being caused by a risk or activity not contemplated, so too is the policy itself.[19]

3. Defining the risk as a whole: exclusion clauses, inherent limitations on coverage, and lessons from the Southern Hemisphere

3.1. The problem stated

Insurers must be permitted to exclude certain types of loss from cover entirely. Suppose a superyacht insured for private use is used for a commercial purpose, as a chartered superyacht sailing in the Mediterranean; if loss occurs, the insurer is not liable because the loss is not within the scope of cover, regardless of whether the immediate cause of loss was, for example, a collision due to negligent navigation. In a similar vein, if a motor vehicle insured for private use is damaged while operating a chauffeur-driven vehicle hire service, the insurer is not liable for any loss incurred because the loss is not within the scope of cover, regardless of whether the immediate cause of loss was a drunken driver,[20] or the engine having caught fire or an act of criminal damage. The pertinent question to ask at this juncture is whether there is, in fact, a distinction between exclusions and terms which define the risk as a whole in *all* cases, because section 11's application is deceptively difficult – what is one to make, for example, of the following two scenarios?

As illustrated, if the risk is defined in either a vessel's or motor vehicle's policy as use for "private purposes", there can be no recovery for any type of loss incurred when either are being used for commercial ventures; crucially, this is so regardless of whether loss occurs as a result of a vessel's collision due to negligent navigation, or in the case of a motor vehicle, as a result of being driven by a drunken driver,[21] or an act of criminal damage or if the engine catches fire. In short, section 11 is precluded.

If, on the other hand, a policy defines the risk more generally as "sailing" or "driving", with an exclusion for loss(es) incurred while the vessel or vehicle, respectively, was being used for commercial ventures, can it not be argued that the assured remains covered while the vessel or vehicle is used for non-commercial ventures if the loss incurred is unconnected from the breach? Indeed, can the said superyacht's policy indemnify the assured if the vessel collides due to negligent navigation or capture and random by pirates and can the said motor vehicle's

[19] (n 13) 121.
[20] (n 5) 458.
[21] ibid.

policy indemnify the assured if the cause of loss is the vehicle having been driven by a drunken driver or the engine having caught fire or the vehicle having been vandalised in an act of criminal damage?

Taken at face value, these are perhaps the only sensible results in light of the purpose and intentions behind the law reform efforts. Moreover, it is the submission of leading insurance law academics that section 11 should not be precluded in such instances[22] and this author concurs – an interpretation to the contrary risks impeding section 11's effectiveness since it would fail to provide the assured with an indemnity in respect of losses incurred in circumstances where, although the assured was in breach, there was a disconnection between the breach and the loss. Nevertheless, this is a view at odds with The Law Commissions' clear belief that terms operating to exclude loss incurred while a vessel or vehicle – and too an aircraft or chattel – is being used for a commercial purpose are necessarily terms which define the risk as a whole.[23]

To assume another example, suppose a chartered superyacht is insured while sailing in the Mediterranean; the insurer should not incur liability if loss occurs while the vessel is sailing outside of the Mediterranean because it falls outside the scope of cover, even if the immediate cause of loss is capture and ransom by pirates, for example, or negligent navigation by the vessel's Master. Consequently, if the risk is defined in a policy as the vessel "while sailing in the Mediterranean", there can be no recovery for any type of loss incurred outside the Mediterranean irrespective of its type or cause.

If, however, following the reforms, the risk is defined in a policy more generally as "sailing in fair conditions", with an exclusion for losses incurred while the vessel sails outside of the Mediterranean, it is arguable that the assured remains covered for losses incurred while the vessel is outside of the Mediterranean *if* the loss is removed from the breach – in practice, this may include, for instance, if one of the engines fails or if the vessel is sunk by means other than severe weather, eg torpedo. The question to consider is whether the exclusion would, in fact, operate as a term which defines the geographical area in which a loss must occur because The Law Commissions explicitly specifies that such a term defines the risk as a whole.[24] This is where the advantage of standard terms can be keenly observed: when hull and machinery policies incorporate the Institute Time Clauses-Hulls (ITC-Hulls),[25] it is clear precisely which perils the insurer is liable to indemnify the assured for and these include piracy[26] and negligent navigation by the Master.[27]

3.2. Defining the risk as a whole and excluding liability: establishing the distinction

Firstly, it is necessary to consider whether section 11 of the IA 2015, on its wording, applies to exclusions. The language of section 11 indicates that it does – "the insurer may not rely on the non-compliance to *exclude* (…) its liability"[28] – and The Law Commissions clearly intended for it to apply as such.[29] Moreover, it has been observed that the majority of warranties are nowadays more closely related to exclusions, in contrast to their traditional

[22] ibid.
[23] (n 14).
[24] ibid.
[25] 01.10.83 <https://www.cpic.com.cn/cx/upload/Attach/infordisclosure/47141680.pdf> accessed May 2018.
[26] ibid, cl.6.1.5.
[27] ibid, cl. 6.2.3.
[28] Insurance Act 2015, s.11(3) (emphasis added).
[29] (n 1).

function as defining risk coverage;[30] since warranties are clearly within the scope of section 11, it would appear to follow that section 11 was intended to apply to risk-defining exclusions, as well as latter-day warranties.

Significantly, however, the Lloyd's Market Association (LMA) doubts section 11's applicability to exclusions. It suggests that all exclusions are necessarily risk-defining because they delimit the scope of cover under the policy.[31] Indeed, in "*The Aliza Glacial*", which predates the Act, it was noted: "in defining the insured risks (…) it is necessary to have regard both to the perils insured and the exclusions, since together they delimit the risk".[32] The LMA further remarked that because exclusions define that which is not covered, they cannot be terms with which the assured may comply; logically, therefore, they are not within the ambit of section 11(1).[33]

This author acknowledges the strength of the argument opposing section 11's application to exclusions in the strict sense – if the function of an exclusion in a policy is to define the scope of cover, its classification as a term which defines the risk as a whole is surely irrefutable. The answer, at this stage, must be that section 11 may apply to *some* exclusions, depending on the individual term and individual policy in question. As the obiter comment in "*The Aliza Glacial*" illustrates, it is when exclusions are read in the context of an individual policy, together with the insured perils, that – together, they define the risk as a whole.

3.3. Inherent limitations on coverage and exclusions: establishing the distinction

Over a century ago, the MIA 1906 was a pioneering development which influenced Commonwealth jurisdictions to an enormous degree. Nevertheless, it was New Zealand and Australia at the forefront of reforming its perceived archaic inadequacies and The Law Commissions drafted their proposals with these reforms in mind.[34] Section 11 of the IA 2015 finds its counterpart in New Zealand in section 11 of the Insurance Law Reform Act 1977 (ILRA) and in Australia, in section 54 of the Insurance Contracts Act 1984 (ICA). Put very broadly, all three provisions were implemented to provide that in cases where there is a degree of disconnection between the breach and the loss, the insurer cannot rely on the assured's breach to avoid paying the claim.

In New Zealand and Australia, the courts have drawn a distinction between inherent limitations on coverage and exclusion clauses,[35] although notably the Australian ICA 1984 does not apply to marine insurance and reinsurance.[36] It goes without saying that case law from Commonwealth jurisdictions is persuasive precedent and may inform the interpretation of section 11 of the IA 2015, particularly as section 11 of the IA 2015 was drafted to avoid the difficulties encountered by the New Zealand and Australian provisions.

[30] (n 5) 455.
[31] Lloyd's Market Association, 'The Insurance Act 2015: A practical guide to changes in UK Insurance Law' (6 October 2016) <www.lmalloyds.com/act> accessed 19 September 2017, paras [70] - [71].
[32] "*The Aliza Glacial*" [2002] EWCA Civ 577, [2002] CLC 1227, [24].
[33] (n 31) para [71].
[34] (n 5) 448.
[35] (n 5) 461.
[36] Insurance Contracts Act 1984, s.9.

3.3.1 New Zealand

Section 11 of the ILRA 1977 was introduced to allow the assured to recover its loss if it could prove, on the balance of probabilities, that the loss was not caused or contributed to by non-observance of the risk-mitigating term found in the policy.[37] It was implemented with the aim of defeating so-called "whilst" cases.[38] The view that section 11 "is designed to deal with those kinds of exclusion clauses which provide for circumstances likely to increase the risk of a loss which the policy actually covers",[39] has fallen out of favour. Instead, conditions which prevent modifying the insured subject-matter are not risk-defining.[40]

New Zealand Insurance Co Limited v Harris [41] is a good starting point. A tractor suffered irreparable damage by fire while out on hire and the policy contained an exclusion stipulating that cover was inapplicable while the tractor was on hire to a third party. The question was whether the provision operated to exclude liability for fire in particular circumstances or whether it described the risk. In an influential Court of Appeal of New Zealand judgment, it was remarked that section 11 was intended to counter the practice adopted by insurers of putting temporal (ie while certain facts are in existence, cover is not available), as opposed to causative, exclusions in policies.[42] Thus, section 11 of the ILRA 1977 was interpreted to prevent insurers from denying liability for loss(es) suffered to equipment during commercial use, when the policy covered private use only. In a similar vein, in *State Insurance Ltd v Lam*,[43] a motor vehicle policy insured the assured as the named driver and contained an exclusion stipulating that there was no cover if the vehicle was driven by a person under 25 years of age. However, the insurer was required to pay for the loss when the vehicle was being driven by a different, underage driver – the vehicle was damaged when a drunken driver collided into it when it was legally parked on the road; significantly, the fact that the premium was reduced because only one driver was insured was apparently irrelevant.

The argument that the case law tipped the balance too far in favour of assureds is a fair one. It is the task of the underwriter, as part of their risk-assessment process, to consider the likelihood of a loss occurring or not occurring and on which basis to either accept or not accept risk; the interpretation of section 11 in *Harris* and *Lam* does not accommodate the extent to which an exclusion may be drafted in a policy with this risk-assessment of the loss's statistical likelihood in mind.[44] Indeed, the flawed approach extended to comparable implications for exclusions concerning a requirement that a driver has a licence and not be in breach of its terms and higher deductibles for under-age drivers.[45]

Consequently, reviewing the law in 1998, the New Zealand Law Reform Commission (NZLRC) did not approve of imposing liability on insurers despite the assureds' breach of a term which defined the risk as a whole. Their proposed solution was to preclude section 11's application vis-à-vis certain risk factors, according to those the

[37] Australian Law Reform Commission, *Insurance Contracts* (Australian Law Com No 20, 1982) para [233].
[38] Robert Merkin and Maggie Hemsworth, *The Law of Motor Insurance* (Sweet & Maxwell 2015) para [2-109].
[39] *Barnaby v South British Insurance Co Ltd* (1980) 1 ANZ Ins Cas 60-401.
[40] (n 5) 460.
[41] *New Zealand Insurance Co Limited v Harris* [1990] 1 NZLR 10.
[42] ibid, 15.
[43] *State Insurance Ltd v Lam* (CA, 10 October 1996).
[44] New Zealand Law Commission, *Some Problems of Insurance Law* (New Zealand Law Com No 46, 1998) para [43].
[45] *Daly v Electronic Navigation Ltd* [1992] DCR 379; *Flight v State Insurance Office* [1972] DLR 781; *State Insurance Ltd v Electronic Navigation Ltd* (1992) 7 ANZ Ins Cas 77,542; *Allied Mutual Ltd v Crofts* (1992) 7 ANZ Ins Cas 77,711.

insurer might consider pertinent when underwriting the policy – so-termed "increased risk exclusion" terms, because there comes a point where the activity generating the loss is so far removed from the activity covered by the policy that the policy should not apply at all.[46] However, it was conceded that this paradigm in fact had the potential to apply arbitrarily. In a marine policy, for example, a provision excluding a vessel from cover whilst in the English Channel would define the risk as a whole, yet a provision stipulating a vessel must retain its classification would require a causal connection.[47]

Evidently, The Law Commissions took note and it is therefore unsurprising that while such terms featured in the NZLRC's proposed new wording of section 11, they feature only in the guidance for use with section 11 of the IA 2015. As with any guidance or suggestion, it can ultimately be disregarded because it is not strictly binding on English courts; this frees the English judiciary from any associated difficulties in the Southern Hemisphere. It is of course a double-edged sword: allowing a selective approach has the potential to result in the very same strained interpretations it seeks to avoid.

In *Hall v FP North Ltd*,[48] which followed in 2009, an exclusion in a public liability policy – insuring the assured's work as an investment advisor – excluded cover for loss related to company insolvency. It was held to be risk-defining because it operated to qualify the scope of the cover, as opposed to events which affected liability which was otherwise covered. While a straightforward matter vis-à-vis the scope of cover,[49] admittedly, the judgment renders drawing the distinction between a term which defines the scope of cover and one which applies a limitation or exclusion within that cover, somewhat unclear. Yet were insurers to argue that the correct interpretation is that the term is necessarily – inherently, risk-defining, it would be a tenuous argument indeed. In *Nelson Forrest v Three Tuis*,[50] the policy in question covered business liability on a farm. Cabins in the grounds were rented to tourists and a forest fire started when the grates from one cabin were not disposed of correctly. The term defined the risk the insurers had subscribed to and tourism ventures were not within the risk contemplated. It indicates a more limited interpretation of section 11, although while the Court of Appeal of New Zealand upheld the judgment, the section 11 issue was not reconsidered.[51]

3.3.2 Australia

Australian reform did not follow New Zealand's example for the reason the NZLRC later identified: it failed to take into consideration the "statistical likelihood factor".[52] The Australian Law Reform Commission (ALRC) attempted to rebalance the interests of the parties with two objectives in mind: proportionality and contribution to the loss.[53] The result, section 54 – titled "Insurer may not refuse to pay claims in certain circumstances", is

[46] (n 44) paras [47] - [48].
[47] Law Commission, *Insurance Contract Law: Misrepresentation, Non-disclosure and Breach of Warranty by the Insured* (Law Com CP No 182, 2007) para [8.37].
[48] *Hall v FP North Ltd* (2010) ANZ Insurance Cases 61-631.
[49] (n 5) 459.
[50] *Nelson Forrest v Three Tuis* [2010] NZHC 2178.
[51] *Nelson Forrest v Three Tuis* [2011] NZCA 576.
[52] (n 44) para [228].
[53] (n 31) para [113].

conceded not to be without fault: subsection 2 is to be read before subsection 1 and the latter has given rise to many complex issues.[54] It is helpful to reproduce the text here:

> (1) Subject to this section, where the effect of a contract of insurance would, but for this section, be that the insurer may refuse to pay a claim, either in whole or in part, by reason of some act of the insured or of some other person, being an act that occurred after the contract was entered into but not being an act in respect of which subsection (2) applies, the insurer may not refuse to pay the claim by reason only of that act but the insurer's liability in respect of the claim is reduced by the amount that fairly represents the extent to which the insurer's interests were prejudiced as a result of that act.
>
> (2) Subject to the succeeding provisions of this section, where the act could reasonably be regarded as being capable of causing or contributing to a loss in respect of which insurance cover is provided by the contract, the insurer may refuse to pay the claim.[55]

The test it stipulates is: "but for" an act or omission, there would otherwise be coverage under the policy. The distinction is drawn as follows:

> '[T]he actual claim made by the [assured] is one of the premises from which consideration of the application of [s.54] must proceed. [It] does *not* operate to relieve the [assured] of restrictions or limitations that are inherent in that claim.[56]'

Contrary to Gürses' suggestion that a mechanism to distinguish between risk-defining terms and terms which remove liability in certain circumstances was needed, it was conceded that such a distinction "might not be of much help".[57] Indeed, in *FAI General Insurance Co Ltd v Australian Hospital Care Pty Ltd*, a High Court majority remarked:

> '[T]*he distinction between "cover" (...) and "condition or exclusion" (...) is a distinction that depends on the form of the contract and not on its substantive effect.* No distinction can be made, [vis-à-vis] s.54, between provisions of a contract which define the scope of cover, and those provisions which are conditions affecting an entitlement to a claim. *The substantive effect of the contract can be determined only by examination of the contract as a whole*.[58]'

The matter arose again in *Stapleton & Anor v NTI Ltd* .[59] In brief, the facts were that a motor vehicle policy excluded cover in the instance where a loss was incurred while the vehicle was operated 450km from the assured's base of operations. Although the judge acknowledged the complexity of establishing the distinction, ultimately the exclusion was held to be an inherent restriction in a claim: the 450km reference comprised part of the definition of the event which was insured under the policy. The fact of use past the stipulated 450km radius might or might not, in the language of section 54, cause or contribute to the loss; thus, whether the insurer is permitted to avoid the claim depends upon the "act" having caused or contributed to the loss.

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[54] Özlem Gürses, 'Reform of construction of insurance contract terms' (2013) *JBL* 39, 42.
[55] Insurance Contracts Act 1984, s.54.
[56] *FAI General Insurance Co Ltd v Australian Hospital Care Pty Ltd* (2001) 204 CLR 641, [41] (emphasis added).
[57] (n 48) 44.
[58] (n 49) para [33] (emphasis added).
[59] *Stapleton & Anor v NTI Ltd* [2002] QDC 204.

All that being said, the New South Wales Court of Appeal subsequently attempted to outline precisely what constitutes an inherent restriction or limitation:

> '[The insured peril] may be an accident which results in personal injury or property damage; [or the aforesaid result per se] (…) These descriptions of themselves are *not sufficiently specific to define the event covered* by a particular type of policy. *The accident will have to be of a specific kind, or arise out of or in the course of a specified activity.* The injury or damage will usually have to happen in the course of or in connection with a particular activity.[60]'

Moreover, the statement in *Australian Hospital* – that in construing the policy, the focus is one of substance and the form is disregarded – was not echoed in *Stapleton*.[61] The result is inconsistent case law, with perhaps the only identifiable guiding principle being that whether a restriction is part of the definition of the insured risk is not dependent on where in the policy the said clause is placed.[62]

The two most significant cases vis-à-vis section 54 are well-known – *Johnson v Triple C Furniture & Electrical P/L* [63] and *Maxwell v Highways Hauliers Pty Ltd*,[64] but need repeating here. In *Johnson*, a private aircraft was involved in an accident which resulted in a death. The policy in question stipulated that pilots were, two years prior to any flight, to have completed a flight review. The Queensland Court of Appeal was clear in holding that this term was an inherent limitation in the coverage of the policy – there was no relevant act or omission for the purposes of section 54 and the exclusion clause in the policy operated to the benefit of the insurer. In *Maxwell*, two separate accidents occurred. Despite the motor policy requiring a PAQS driver profile score "of at least 36" – 'PAQS' being defined in the policy to refer to 'People and Quality Solutions Pty Ltd – both drivers involved had not taken the test. Furthermore, the drivers were non-approved for the purposes of an exclusion clause. Corby J in the High Court of Australia was resolute in distinguishing *Johnson*, on the basis of a complex analysis: the result in *Johnson* was based on applying section 54 to the particular facts, as opposed to regarding the correct construction of section 54 – the obiter argument regarding subsection 2 was also disregarded. The "act" was the use of the vehicles by those who did not satisfy the requirements of the policy, rather than the non-accreditation of the drivers, emphasising the substance of the policy. On this view, the exclusion clause imposed an obligation to submit declarations as appropriate and therefore did not operate to impose an obligation that the drivers take the PAQS test. Therefore, section 54(1) was interpreted to provide the assured with a right to indemnification.

Plenty of cases have followed the approach in *Maxwell*, illustrating the judiciary's preference for an interpretation which favours the assured, using section 54 to negate the impact of exclusions. A recent example is *Pantaenius*[65] which concerned cover under the policy for a yacht – the Froia II. Although a policy for a yacht appears, at first glance, to be a marine insurance contract, section 9A of the ICA excludes the application of the Marine Insurance Act 1909 to marine insurance contracts for "pleasure craft". For this purpose, a "pleasure craft" is defined a vessel which is used, or intended to be used, "wholly for recreational activities" and which is owned legally and beneficially by one or more individuals. While the application of the ICA is not explicitly addressed in the

[60] *Prepaid Services Pty Ltd v Atradius Credit Insurance NV* [2012] NSWCA 252, [134] (emphasis added).
[61] (n 54) 45.
[62] ibid.
[63] *Johnson v Triple C Furniture & Electrical P/L* [2010] QCA 282.
[64] *Maxwell v Highways Hauliers Pty Ltd* [2014] HCA 33.
[65] (n 6).

judgment, it is clear is that the Froia II was owned by one individual and it is implicit from the judgment, and indeed the conduct of both parties, that the yacht was a pleasure craft for the purposes of the ICA.

The cover in question was limited to damage incurred while the vessel was in Australian territorial waters. The clause in dispute functioned to suspend coverage from the time the yacht was cleared by customs – leaving Australian waters, until it was cleared again upon return. The insurer, Nautilus, refused to pay when the vessel was wrecked off Cape Talbot: while the yacht was in Australian waters, it was sailing from Indonesia and had not cleared customs at the time the loss occurred. Nautilus argued that there was no act or omission within the ambit of section 54(1): cover was suspended and, when the loss was incurred, cover had not been reinstated because the vessel did not clear customs on its return. Were the clause a warranty, and within the jurisdiction of the English courts, this argument would have succeeded. Yet in Australia, it was rejected. The clause was held to be an exclusion, not an inherent limitation (operating as one of the contractually prescribed elements of the geographical limits on the scope of cover itself). Reading the exclusion in light of the underlying purpose of the policy, Foster J held its purpose was to extend the yacht's coverage for the time it was in Australian waters and the assured's claim was within the ambit of section 54, ie clearing customs was an "act". This is because, following *Maxwell*, the claim was within the scope of the policy: section 54 focuses on the effect of the insurance upon which a claim has been made, as opposed to its application being limited to a claim for an insured peril. The Federal Court helpfully articulated how an inherent restriction is to be identified:

> 'The process of understanding what are the restrictions or limitations that are inherent in the claim is one that involves the construction of the policy, not merely as to what its constituent words mean, but in a broad sense so as to characterise as a matter of substance what is the essential character of the policy. Once that essential character is decided upon, the restrictions or limitations that necessarily inhere in any claim under such a policy (…) and the restrictions or limitations that do not necessarily inhere in any claim under such a policy (…) can be ascertained.[66]'

3.4. Lessons from the Southern Hemisphere

The overriding point to take away is that the judiciary in the Southern Hemisphere has been so committed to interpreting the law in a manner which strives to benefit the assured, upholding "[t]he intention of the legislature",[67] that this has sometimes been at the expense of cogent interpretation. It is submitted that it would be inappropriate to always view exclusions as inherently risk-defining: it is arguable that certain exclusions aim to reduce the risk of loss. For example, an exclusion regarding the assured's insolvency; or AVN 1/D – which replaces AVN 1/C in one of the Standard Aircraft Liability policies in the London Market – which excludes cover when the aeroplane is operated by an unauthorised pilot. If the IA 2015 applies, cover under the latter liability

66 *Watkins Syndicate 0457 at Lloyds v Pantaenius Australia Pty Ltd* [2016] FCAFC 150, para [40].
[67] (n 6) para [107].

policy would not be excluded if the pilot was qualified – the insurer will be off-risk when the subject matter of the exclusion concerns the risk even if, overtly, the clause does not state its purpose is to avoid certain risks.[68]

Moreover, the result might be to encourage courts to be more liberal in finding that a disputed exclusion clause is in fact a restriction or inherent limitation on cover, and strained interpretations fly in the face of commercial certainty. Indeed, the distinction between exclusions and inherent limitations is a distinction which is now definable and workable: English courts are spared much of the uncertainty which follows the implementation of new legislation by relying on tried-and-tested persuasive precedent. Furthermore, this approach emphasises the role of the underwriter in framing the scope of the risk covered by non-consumer policies, reinforcing the view that underwriting insurance is a collaborative process between all parties involved.

It is foreseeable that in practice there will be a divide in the said approach between non-consumer and consumer policies, owing to the presumed greater understanding of risk and familiarity with insurance policies assumed of those operating in the commercial sphere compared with the consumer assureds' limited position to negotiate and consequent reliance on standard terms. Alternatively, and more appropriately in this author's view, there might instead be a divide in the approach between tailored – more specialist, individual policies and standard, 'off-the-shelf' policies – so often bought online.

In *Wood v Capita Insurance Services Ltd*,[69] the Supreme Court re-emphasised the importance of considering the policy as a whole in contractual interpretation and underlined that in the case of a complex commercial agreement, which has been negotiated and drafted with the input of lawyers, a textual analysis attributes more weight to the specific language used rather than a contextual analysis which favours the policy's factual background and practical implications. The reason for this is simple: the policy is the result of a negotiated compromise, although the court must be aware that one party may have agreed to something which, in hindsight, was not in his interest.[70]

Therefore, without being too esoteric, in bespoke policies which are tailored to insure a particularly high-risk, one-off venture; or a particularly complex liability policy, an expression that particular terms are agreed to be risk-defining – either by clearly stating this in the text specific term, or its inclusion under a heading in the policy labelled 'risk-defining terms', will probably be taken at face value.

In the case of off-the-shelf policies, which heavily rely on standardised terms, *Wood* may provide assureds' with scope to challenge a term's function as a risk-defining provision by means of a contextual analysis if this produces a result more consistent with business common sense. Lord Hodge SCJ highlighted that in ascertaining the objective meaning of contractual language, regard must be had to the nature of the policy, its formality and the quality of its drafting – attributing a greater or lesser weight to these aspects, in an assessment of its wider context, as relevant on the facts of each particular case.[71] Thus, if a policy does not reflect the underwriters' art in framing the scope of the risk – perhaps it is silent re matters of great importance in the type of policy in question; or it contains many superfluous terms, for example a public liability policy which makes inconsistent references to

[68] 'Insurance Act 2015 Shaking up a century of insurance law' (2016) <https://www.clydeco.com/uploads/Files/Admin/CC010256_Insurance_Act_2015_26-07-16-web.pdf> accessed September 2017, 25.
69 [2017] UKSC 24, paras [12] – [14]; *Rainy Sky SA v Kookmin Bank* [2011] UKSC 50; *Arnold v Britton and others* [2015] UKSC 36.
[70] ibid, paras [11] – [12].
[71] (n 69) para [10].

property losses; or has been amended by in-house compliance professionals rather than lawyers, a more demanding process of construction rooted in the policy's factual background and practical implications may be necessary. (Although the caveat is that assureds lacking the ability to negotiate a policy's terms in the first instance may lack the ability to litigate the point.) To this end, the questions the court might consider when construing a policy could include the following:

- Was the policy an 'off-the-shelf' policy, applying in a straightforward fashion to straightforward and accepted risks within the specific sector in question?
- If a standard policy was amended, for which reason(s) were the amendments made?
    - What was their objective purpose?
    - Did the assured appreciate the difference(s) in coverage offered?
- If the policy in question is a specialised, tailored policy:
    - Which risk(s) did the assured think they were obtaining cover for?
    - How could, and indeed how did this impact the underwriters' assessment of the risk? (Eg the impact on the premium.)
    - What was the objective purpose of the policy and the disputed term in question?
- Determining the objective purpose of the term in question is achieved by examining the insured perils, together with policy's exclusion(s), in the context of the policy as a whole.

As one final point, it is worth highlighting that the comments in "*The Aliza Glacial*" were both obiter and in the context of an Institute War Clauses policy: as a very specific type of cover, insurers may find that it is not particularly persuasive in cases concerning different classes of insurance cover.

4. Conditions

4.1. Overview

In insurance law, conditions are not defined as in ordinary contract law: an insurance condition – also termed a 'bare' or 'mere' condition, can be distinguished from a condition precedent. Conditions are analysed in the same way innominate terms are analysed in contract law: a breach confers upon the innocent party either the right to repudiate the contract as a whole, or a right to damages, depending on the seriousness of the breach. The question to ask is: does the breach go to the "root" of the contract?[72] In other words, is the innocent party deprived of the benefit they were expecting to gain as a party to the contract? If answered in the affirmative, the innocent party can repudiate the contract as a whole. It is important to note that the common law does not recognise the concept of repudiation of a claim; it is not possible, therefore, for the insurer to repudiate the claim when the assured is in breach of a provision which is not drafted as a condition precedent. Consequently, prior to the IA 2015's

[72] *Hong Kong Fir Shipping Ltd v Kawasaki Kisen Kaisha* [1962] 2 QB 26; *Friends Provident Life & Pensions Ltd v Sirius International Insurance Corp* [2005] EWCA Civ 601.

implementation, conditions precedent were of great value to insurers because the assured's breach enables the insurer to reject the claim per se.[73] The question now is in which ways the IA 2015 has changed this analysis?

It is first helpful to outline the three different types of condition precedent. The first is to the validity of the policy, ie the condition must be satisfied before the parties can be treated as having a contract at all – an example includes that the assured will obtain the Salvage Association's approval.[74] The second is to the attachment of the risk: a valid contract is presupposed but the risk does not attach until the condition(s) are satisfied.[75] Examples include that the subject matter insured be inspected and any subsequent recommendations be complied with; that the provision of further information be provided by the assured; payment of the premium or the implementation of security measures. The third, and most common, type of condition precedent is to the insurer's liability: it prevents the assured from bringing a claim for loss to which the condition relates; for instance, the insurer faces no liability unless the assured has submitted a claim within a fixed or reasonable time of the date of the loss.[76]

Therefore, in answer to the question posed, section 11 of the IA 2015 applies to conditions in three cases, providing they relate to risk: (1) conditions precedent to the insurers' liability for a claim, (2) the latter, when it in fact functions as a 'bare' condition in a policy and (3) 'conditions precedent' to the attachment of the risk which also properly function as 'bare' conditions. It follows that section 11 applies neither to conditions precedent to the validity of the contract – because a breach precludes the formation of a binding policy – nor conditions precedent to the attachment of the risk – because such a breach repudiates the policy, with the exception of such terms which are in fact found to operate as 'bare' conditions.

There is a case to say that the reforms missed the opportunity to redress the imbalance in the parties' interests in a more comprehensive fashion in respect of claims provisions drafted as conditions precedent – and, by extension, other non-risk provisions in policies.[77] A claims co-operation clause requires the (re)assured to notify the (re)insurers of the occurrence of circumstances likely to give rise to a claim and to provide information to (re)insurers.[78] A claims control clause is wider in its affect – it takes the settlement out of the (re)assured's hands and confers upon the (re)insurers the right to negotiate with the assured;[79] they are most commonly used in policies where the (re)assured has acted as a front for the reinsurers and has reinsured the vast bulk of, or all of, the risk.

On the one hand, claims provisions are 'true' conditions precedent in that they are so fundamental to the performance of the contract that it cannot be considered an abuse of drafting to afford them this status. Indeed, The Law Commissions expressly stated that they did not intend to preclude insurers from including conditions which they regarded as so fundamental that, upon breach, their liability should be discharged.[80] On the other hand, the appropriateness of such a stringent remedy can be questioned given that it applies indiscriminately,

[73] *Cornhill Insurance PLC v D.E. Stamp Felt Roong Contractors Limited* [2002] EWCA 395, para [19].
[74] *Zeus Tradition Marine Ltd v Bell (*"*The Zeus V*") [2000] 2 All ER (Comm) 769.
[75] ibid.
[76] *MJ Harrington Syndicate 2000 v Axa Oyak Sigorta AS* [2007] Lloyd's Rep IR 60.
[77] (n 2) 1019.
[78] *Insurance Co of Africa v Scor (UK) Reinsurance Co Ltd* [1985] 1 Lloyd's Rep. 312; *Gan Insurance Co Ltd v Tai Ping Insurance Co Ltd* [2002] EWCA Civ 248.
[79] *Eagle Star Insurance v Cresswell*[2004] EWVA Civ 602.
[80] (n 14) para [13.22].

irrespective of both prejudice to the insurers[81] and in cases where the assured's conduct and breach is trifling.[82] This result is arguably draconian yet it generally escapes the same criticism levelled at the old law governing warranties.[83] This is a comprehensive argument, however, and one beyond the scope of this paper.

4.2. Pre -2015: a "tendency" to interpret conditions precedent obligations narrowly

An extensive body of case law advocates a cautious approach to construing provisions as conditions precedent which safeguards them from abuse. For example, in *Heritage Oil and Gas Ltd & Anor v Tullow Uganda Ltd*, Beatson LJ refused to construe a notification clause as a condition precedent to a tax indemnity claim.[84] Specific insurance law examples include *Eagle Star Insurance v Cresswell*[85] and *Aspen Insurance UK Ltd v Pectel Ltd*.[86] In *Eagle Star*, the dispute centered around a term in a liability quota share reinsurance contract entitled 'Claims Co-Operation' clause; it was held that because the clause detailed the negotiation and settlement of any claims, its proper interpretation was that it resembled more of a 'Claims Control' clause.[87] The Court of Appeal was unanimous in ruling that the clause was a condition precedent but emphasised the caveat that such a classification of a term in a policy must be "clearly spelt out"[88] – "questions of construction are best dealt with without restrictive rules which may distort the attempt to find the parties' true meaning".[89]

Furthermore, when courts do indeed interpret a provision as a condition precedent, Merkin notes a "tendency" to interpret them narrowly because their obligations are often onerous for assureds – although this is not universally followed.[90] For example, in *Milton Furniture Ltd v Brit Insurance Ltd,* the Court of Appeal disagreed with Jay J that the two overlapping security provisions were to be read together, with the wider of the two being read down to match the other.[91] Instead, Gloster LJ held the two provisions were to be construed independently, ruling that "General Condition 7" was, in fact, a condition precedent.[92] By way of further example, in *Royal and Sun Alliance Insurance v Dornoch* [93] a liability policy required insurers to notify the reinsurers within 72 hours "upon knowledge of any loss or losses which may give risk to claim under this policy". "[L]oss or losses" was held to refer to established losses meaning there was no obligation to notify the reinsurers until judgment. Consequently, the insurers – the reassured's, were not in breach, despite the provision presumably being drafted to avoid this precise scenario.

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[81] Özlem Gürses, *Reinsuring Clauses* (Taylor & Francis 2013), para [9.54].
[82] (n 2) 1022.
[83] Robert Merkin and Jenny Steele, *Insurance and the Law of Obligations* (Oxford University Press 2013), para [3.3.4.4].
[84] *Heritage Oil and Gas Ltd & Anor v Tullow Uganda Ltd* [2014] EWCA Civ 1048, [33] – [42].
[85] [2004] EWCA Civ 602, [2004] 1 CLC 926.
[86] [2008] EWHC 2804 (Comm), [62].
[87] [2004] 1 CLC 926, [20].
[88] ibid, [23].
[89] ibid.
[90] Robert Merkin, *Colinvaux's Law of Insurance* (11th edn, Sweet & Maxwell 2016) para [8-032].
[91] *Milton Furniture Ltd v Brit Insurance Ltd* [2014] EWHC 965 (QB).
[92] *Milton Furniture Ltd v Brit Insurance Ltd* [2015] EWCA Civ 671.
[93] [2005] Lloyd's Rep IR 544.

4.3. Does the 2015 Act signal a change in judicial approach?

This interpretive approach remains relevant in respect of insurance policies predating the 12th August 2016 and, subsequently, those postdating the IA 2015 if section 11 is contracted out. In respect of all other conditions precedent the uncertainty is two-fold, whether (i) the cautiousness in construing provisions as conditions precedent, and subsequently whether (ii) the interpretive "tendency" to construe its obligations narrowly, will survive. The answer would appear to be in the affirmative insofar as non-risk-mitigating terms are concerned – which prospectively is likely to be only legitimate claims provisions. For those which are risk-mitigating, section 11 of the IA 2015 circumvents the hardship where section 11(3) is satisfied and the need to classify the provisions' status as a condition precedent or otherwise is removed: the *form* no longer matters but the *substance* does. Consequently, answering (ii) is redundant and the prevailing question regarding risk-mitigating provisions after 12th August 2016 is whether the assured can satisfy section 11(3).[94]

4.4. Defining and/or mitigating the risk: classifying ambiguous conditions

A difficult point arises when a condition or condition precedent is, on the face of it, both risk-defining and risk-mitigating. An example is a condition in a credit risk policy that there will be "no material change to Covered Transaction". It is probably risk-defining, but an assured could argue that a material change, such as altering the repayment currency, for example, aims to reduce the risk of loss of a particular kind, ie loss arising from currency fluctuations, meaning the insurers were on-risk for losses unrelated to currency fluctuations.[95] This raises two questions: (i) whether the distinction between risk-defining and risk-mitigating terms is inherent or a matter of good drafting[96] and (ii) whether a term can indeed be both risk-defining and risk-mitigating for the purpose of section 11?

It is necessary to consider the precise wording of section 11(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 (…)'

It appears to suggest that in the event that a term is both risk-defining and risk-mitigating, the former interpretation expressly excludes it from application. This is an analysis supported by subsection 2 which specifically stipulates that a breach of a risk-defining term will not cause the insurer's liability to be excluded, limited or discharged in respect of other types of loss.[97]

In practice, undoubtedly, practitioners will advise insurers to identify clearly which provisions in their policies they deem to be risk-defining, but if insurers can ensure that a risk-mitigating provision is drafted to indubitably

[94] *See* 5 'Section 11(3) and "Causation"'.
[95] (n 68) 56.
[96] (n 5) 455.
[97] David Kendall and Harry Wright, 'A practical guide to the Insurance Act 2015' (Taylor & Francis Ltd (2017), Chapter 7.

take effect as a risk-defining provision, they are at liberty to circumvent section 11's operation with relative ease and there may be a case to say that the balance tips in favour of the insurer.

Indeed, "[t]here is no obvious solution other than judicial good sense".[98] Therefore, as suggested above, it is submitted that in practice a distinction will emerge between the interpretation of ambiguous terms in the more bespoke policies and 'off-the-shelf' policies. In respect of bespoke, negotiated, commercial policies, legal certainty is of paramount importance in commercial law and any other approach surely flies in the face of commercial common sense. Significantly, *Pilkington United Kingdom Ltd v CGU Insurance Plc* continues to provide a vital safeguard: provisions in a policy stated to be conditions precedent should not "be treated as a mere formality which is to be evaded at the cost of a forced and unnatural construction of the words used in the policy" – they should be "construed fairly to give effect to the object for which they were inserted, but at the same time so as to protect the assured from being trapped by obscure or ambiguous phraseology".[99] Furthermore, it is a commercial reality that arbitration, particularly in international commercial disputes, has the potential to be extremely expensive and challenging arbitral awards even more so:[100] as a common means of dispute resolution, a certain approach which minimises disputes in commerce is difficult to convincingly challenge.

With regard to standardised policies, the court may be persuaded by a contextual/purposive argument to the effect that a provision is risk-mitigating if this is what the parties intended, assessed through the eyes of a reasonable person "having all the background knowledge which would have been available to the parties" and based on their understanding of the contractual language, in its documentary, factual and commercial context, at the time the contract was entered into.[101] This is the advantage of a system of precedent reliant on interpretation; while admittedly it may detract from predictability initially, clarity, and in turn certainty, will be achieved on a case-by-case basis as the criteria which is taken into consideration in the courts' reasoning becomes apparent.

It is important to consider the reforms in the wider context of the current insurance market. The IA 2015 allows non-consumer parties to contract out of section 11 and a 'soft' market favours assureds. Consequently, insurers are unlikely to abuse any margin of bargaining power they exercise over a minority of assureds and it is therefore submitted that, in this respect, the IA 2015 pays sufficient heed to the interests of the insurer while simultaneously promoting the interests of the assured.

4.5. *Looking forward: will there be an increase in the use of conditions precedent?*

It is clear that conditions precedent which define the risk as a whole (in addition to risk-defining warranties and risk-defining exclusions) retain their value for insurers after the IA 2015: their breach will continue to result in the insurers' automatic discharge of liability per se, even if the breach is trivial. This is in addition to breaches of conditions precedent which, on a technical analysis, mean the insurer may never come on risk at all and so, in the strict sense, the insurer is not subsequently discharged from liability; for ease of reference, this includes as above, conditions precedent to the validity of a contract, to the attachment of the risk, and to the liability for a claim – to

[98] (n 5) 459.
[99] *Pilkington United Kingdom Ltd v CGU Insurance Plc* [2004] EWCA Civ 23, [2004] 1 CLC 1059, para [65].
[100] Stephen Ware and Ariana Levinson, *Principles of Arbitration Law* (West Academic Publishing 2017), 144.
[101] (n 69); *Arnold v Britton* [2015] UKSC 36 paras [14] – [20].

the extent that the provision relates to the risk.

It is therefore easy to see why Song and Hjalmarsson predicted an increase in the use of conditions precedent following the reforms.[102] It is true that insurers have lost much of their previous armour which enabled them to avoid liability on the basis of a 'technicality' – namely breach of warranty, section 33 of the MIA 1906 having been replaced by sections 10 and 11 of the IA 2015; it is not improbable to assume, therefore, that insurers will be incentivised to maximise their chance of escaping liability in this way in all instances which do not concern section 11. Indeed, there is already a perceived increase in their use in certain markets.[103] Furthermore, so far as provisions which are both risk-defining and risk-mitigating are concerned, there may be instances in which the risk-defining element can be regarded as a tenuous effort at best by insurers to replicate their position under the former law relating to warranties; or colloquially, to 'try their luck'.

However, when section 11(3) applies, the assured is empowered to avoid the 'dramatic impact' of a breach of condition precedent if it can be proven that their non-compliance with the provision did *not* increase the risk of loss in the form it occurred in. This, prima facie, strikes a congruous balance, redressing the former imbalance of interests to the detriment of the assured; whether it will succeed in reality is another matter – the subsection is not straightforward to apply.

Moreover, it must be remembered that the market, at the time of writing, is a 'soft' one: premiums are low and capital is high – it is very much an assured's market (although it cannot remain so indefinitely[104]). Additionally, the perceived increase of conditions precedent in policies is countered by persuasive advice from the likes of *Airmic* to their members that they be both expressly stated and – crucially, kept to a minimum.[105] This is in keeping with the overriding aims of the Act – to redress the rights of both parties and to promote an increased understanding of the risk between them.

5. Section 11(3) and Causation

The market objected to a causal requirement and so The Law Commissions were at pains not to express a causation element at all: the test is whether non-compliance could not have increased the risk of that loss, as opposed to whether non-compliance *caused* the loss.[106] Looking forwards from when the risk was underwritten[107] rather than backwards, it emphasises the centrality of the risk-assessment process with the aim of increasing the parties' understanding of the risk(s). The reasons for rejecting a causal link between the breach and the ultimate loss were three-fold: (i) the costs involved, (ii) uncertain outcomes and (iii) difficulties with proof.[108] However, these

[102] Mexian Song and Johanna Hjalmarsson, 'The Insurance Act 2015 and marine insurance' (2016) *Shipping and Trade Law* 1, 3.
[103] 'The Insurance Act: more work needed, warns Airmic' (*Airmic.com*) <www.airmic.com/news/guest-stories/insurance-act-more-work-needed-warns-airmic>accessed 6 June 2017.
[104] Simon Cooper, 'What are the current trends in and future prospects for the insurance and reinsurance market in your jurisdiction?' (Ince & Co LLP Market Spotlight, *Lexology.com*) <www.lexology.com/navigator#!results/446/view> accessed 13 June 2017.
[105] 'The Insurance Act 10 months on' (*Airmic.com* 12 June 2017) <https://www.airmic.com/technical/library/insurance-act-2015-10-months>accessed June 2017
[106] (n 1) para [96]; (n 5) 452 (emphasis added).
[107] (n 5) 465-466.
[108] (n 1) para [94].

difficulties will likely be encountered in any event because satisfying section 11(3) will not always be a straightforward task – it is unequivocally "convoluted".[109]

Suppose a building is damaged by fire when the assured was in breach of a provision in a Commercial Combined Insurance policy to maintain a burglar alarm.[110] Objectively, the insurer is liable. There will be borderline cases, that much is agreed. Yet what highlights how deep the uncertainty surrounding the provisions' application runs is that academics appear to disagree, at first glance at least, how this seemingly straightforward scenario is to be reconciled in some instances. While Soyer argues the term reduces the risk of a break-in *and* related events such as arson and vandalism,[111] Merkin and Gürses reject this interpretation – using the test rejected in *Harris*,[112] because otherwise section 11 would have "a very narrow ambit" indeed.[113]

In *Harris*, a wide causation test was rejected – "refined analysis in terms of metaphysical inquiries into causation should be eschewed",[114] in favour of the immediate cause of the loss – the fire, which was removed from the hiring. Strikingly, Merkin and Gürses question whether the reasoning would differ under the IA 2015.[115] For only by using the test rejected in *Harris* does section 11(3) of the IA 2015 produce a different result.[116] What exacerbates the uncertainty further is that The Law Commissions would expect the insurer to be liable in a *Milton Furniture* scenario, yet section 11 of the IA 2015 supposedly does not apply to a term which excludes loss which occurs while a vehicle is being used for a commercial purpose – as per *Harris*.

A further difficulty is encountered in respect of two competing causes of loss. Suppose a fire was caused by arson, or an electrical fault, and the assured was in breach of a condition requiring inspection of electrical installations – how is the subsection satisfied? Moreover, if the fire was caused by arson, but the electrical fault contributed 40% to the loss, is this immaterial?[117]

The difficulty regarding two concurrent causes of loss is settled in English law both in non-marine insurance, as per *Wayne Tank v Employers Liability Insurance Corp*,[118] and in marine insurance, as per *"The Cendor Mopu"*.[119] Nevertheless, *Wayne Tank* is not a decision without criticism. Indeed, the Canadian Supreme Court chose not to follow *Wayne Tank* in *Derksen v 539938 Ontario Ltd* in the absence of a persuasive argument as to why the exclusion should be preferred in such an instance;[120] rather, such an intention is a matter of clear drafting.[121] It is useful to consider the Australian decision of *McCarthy v St Paul's International Insurance Co Ltd.*[122]

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[109] (n 13) 118.
[110] (n 14) para [18.61].
[111] (n 13) 255; Baris Soyer, 'Beginning of a new era for insurance warranties?' (2013) *LMCLQ* 384, 390.
[112] (n 41).
[113] (n 5), 468.
[114] (n 5) 465.
[115] (n 2), 1022.
[116] (n 3) 466.
[117] (n 68), 48.
[118] [1974] QB 57.
[119] *Global Process Systems Inc and another v Syarikat Takaful Malaysia Berhad ("The Cendor Mopu")* [2011] UKSC 5; MIA 1906, s.55.
[120] [2001] 3 SCR 398, para [48] – [49].
[121] ibid, paras [46] – [47].
[122] [2007] FCAFC 28.

The Federal Court distinguished between interdependent and independent concurrent causes of loss. In the case of interdependent losses, the loss would not have occurred if only one of either of the two causes was operative at the time of loss – the insurer can avoid the claim because "the non-response of the policy can be comfortably and logically accepted as the intended result of the revealed agreement of the parties".[123] In the case of independent losses, either of the two causes would have caused the loss incurred in the absence of the other – the policy must be construed in order to ascertain the parties' contractual intentions; it is not simply a case of relying on the *Wayne Tank* principle.

These authorities have most recently been considered by the Court of Appeal of New Zealand in *AMI Insurance Ltd v Legg*[124] which confirmed that in the instance of two competing concurrent causes of loss, the exclusion takes precedence. However, since the decision concerned two interdependent concurrent causes, there is scope for an argument to the effect that independent concurrent losses can be distinguished from the principle set out in *Wayne Tank*.[125] This would mean, in the above example of a fire caused by arson or an electrical fault, that the assured could, in theory, recover their loss(es) from their insurer; indeed, it will be difficult to maintain the position that an exclusion prevails and that a type of loss or extent of loss which falls within the ambit of a policy's coverage is secondary given that the purpose of section 11 of the IA 2015 is to redress the imbalance of interests between insurer and assured.

5.1. Lord Hoffmann – The language of causation[126]

The raison d'etre of subsection 3's formulation is that it is immaterial both (i) what the cause of the loss was and (ii) that compliance with the obligation would not have made any difference – the chance that it could have made a difference will suffice.[127] While the phrasing deliberately frees the English judiciary from adopting the more difficult persuasive precedents, this author acknowledges the strength in the argument that the subsection is "pure causation" by means of the back door.[128] It is submitted that a more appropriate reform would have explicitly required a causal link (not necessarily a complete chain of causation) for one simple yet fundamental reason: it would have been a transparent and accountable means of applying the law.

Causation can usually be subdivided into two stages: (i) establishing factual causation, ie the causal link and (ii) consideration of remoteness of damage.[129] Lord Hoffmann writes that when judges speak of applying common sense, they appeal to moral notions of what would fairly delimit the events for which a person is responsible.[130] He terms this 'standard criteria' which works well when liability is based on fault.[131]

[123] ibid, para [103].
[124] [2017] NZCA 321.
[125] (n 118) paras [67] – [68] (Lord Denning MR), para [69] (Cairns LJ), paras [74] – [75] (Roskill LJ).
[126] Leonard Hoffmann, 'Causation' [2005] 121 *LQR* 592.
[127] (n 5) 466.
[128] (n 5); (n 13).
[129] (n 126), 598.
[130] (n 126), 594.
[131] (n 126), 598.

However, when liability is to be based on something other than fault, the standard criteria may be departed from and the answer depends on the extent of liability the judges think Parliament intended to impose.[132] Yet the final draft of the subsection was subject to minimal Parliamentary discussion:[133] what are judges to do? This is a question of law which may result in a difficult policy choice, which is unhelpful if not fully explained; it is then a question of fact whether the claimant has satisfied the requirements of law. Moreover, in respect of the remoteness of damage issue, an overt causal link requirement would have ensured that sufficient heed was paid to the requirement that the loss occurred was of a foreseeable kind.[134]

On one level, as formulated, it is not hyperbolic to suggest that section 11(3) will prove to be far more expensive, uncertain and difficult to prove than any causal link requirement – perhaps a case of better the devil you know. To a large extent in practice, it will come down to an issue of construing the policy wording, with the only way for insurers and assureds alike to mitigate the uncertainty being to carefully draft their terms. In doing so, the Act will accomplish its aim: to foster the tripartite relationship between the parties – by means of collaboration, and an increased, more sophisticated, understanding of risk.

6. Conclusion

Section 11 of the IA 2015 is curious: it will be some time before its "practical significance or value to assureds", or lack thereof, becomes apparent.[135] Regarding its interpretation, on the whole, "[t]here is no obvious solution other than judicial good sense".[136] For now, persuasive precedents from the Southern Hemisphere provide an insight into how the English judiciary might attempt to draw the distinction between terms which define the risk as a whole, exclusions and inherent limitations on coverage. It is this author's submission that it might be appropriate for the judiciary to develop a dual approach with regard to interpreting policies in line with the aims of the Act, drawing a distinction between standard, off-the-shelf policies on the one hand; and tailored, more specialist, individual policies on the other.

In respect of insurance conditions, section 11 does impair the insurer's ability to rely on the assured's breach to avoid paying a claim in instances where the breach is removed from the loss, but only in the case of risk-mitigating provisions. This means that trivial yet technical breaches of non-risk provisions drafted as conditions precedent will continue to defeat otherwise legitimate claims. Therefore, while the reform is a welcome one, there is more to be done in the wider realm of rebalancing the interests of insurer and assureds – the task of The Law Commissions does not stop at the Insurance Act 2015.

As regards section 11(3) and the issue of causation, it will be interesting to see how the courts apply the subsection – it is not unthinkable to suppose that The Law Commissions may well be tasked with reviewing it in the near future.

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[132] *Fairchild v Glenhaven Funeral Services Ltd (t/a GH Dovener & Son)* [2002] UKHL 22; *Gregg v Scott* [2005] UKHL 2.
[133] (n 3).
[134] *Hadley v Baxendale* (1854) 9 Ex 341.
[135] Robert Merkin and others, Arnould: Law of Marine Insurance and Average (1st supplement, 18th edn, Sweet & Maxwell 2016), para [1.3-126].
[136] (n 5) 459.

It will be some time before the precise parameters of section 11's scope and application are determined, but it can be said with certainty from the outset that the English judiciary is esteemed for its commerciality and any decision of an English court will be in accordance with the understanding that the purpose of commercial law is to facilitate, rather than frustrate, commerce.