

## **Court considers follow the settlements clause and various key issues in relation to reinsurance**

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*RSA v Equitas*<sup>1</sup> will be of interest to the reinsurance market due to the scarcity of case law in this area, and for its consideration of a number of key issues of interest. The judgment addresses a number of areas, including: whether underlying defence costs erode the reinsurance excess; whether the claims co-operation wording circumscribed the follow the settlements clause, and whether the reinsured took proper and businesslike steps in settling.

Whilst some of the law applied and conclusions reached are unsurprising, in other areas there is some pause for thought.

### **Background**

The case concerned a claim under five facultative excess-of-loss reinsurance policies covering the period from 1 October 1981 to 30 September 1985 (the “Reinsurance Policies”). During this period, the Reinsureds provided worldwide general third-party liability insurance to manufacturing company BOC Group Plc and its subsidiaries and associated or affiliated companies (“BOC”). From the mid-1980s, BOC became subject to bodily injury claims in the USA in relation to the use of its products. BOC paid substantial damages and incurred extensive defence costs. BOC sought to claim on its insurance.

The cover provided by the Reinsureds to BOC was up to a limit of £20 million. Defence costs were payable in addition to this limit and without application of the excess. Settlement agreements were reached between BOC and various insurers covering various periods including the Reinsureds’. One of the particular agreements at issue in this claim was referred to as the Toxic Torts Settlement Agreement (“TTSA”), although there were also other settlements and sums claimed.

The Reinsureds claimed a total sum of around £3.8 million from Reinsurers, before interest, in respect of payments to BOC.

### **Issues**

The court was asked to consider four issues:

1. Whether the excess in the Reinsurance Policies was eroded by underlying defence costs in addition to indemnity payments.
2. Whether the Claims Co-operation Clause contained in the Reinsurance Policies circumscribed the Follow the Settlements Clause.
3. Whether the Reinsureds failed to take proper and businesslike steps in settling the claims in breach of the Follow the Settlements Clause.
4. The extent to which the Reinsureds were entitled to interest on any recovery made under the Reinsurance Policies.

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<sup>1</sup> [2025] EWHC 2704 (Comm).

## **Judgment**

Judgment was given by HHJ Keyser KC.

### **The Defence Costs Erosion Issue**

It was common ground between the parties that the Reinsureds' obligation to indemnify BOC in the underlying policy in respect of defence costs was not subject to a financial limit, only a temporal limit, in that it would subsist only while the £20 million indemnity limit in respect of third-party claims had not been reached.

Reinsurers contended that the £4 million excess in the Reinsurance Policies was eroded only by indemnity payments, and the Reinsureds argued that the excess was eroded by both indemnity payments and defence costs.

The judge agreed with Reinsurers for a number of reasons, finding the interpretation of the provisions to be fairly clear. The Reinsurance Policies were back-to-back with the underlying policies: they stated they "*follow original terms, conditions and settlements*", and Reinsurers had seen the "*original policy*". The judge therefore found that the natural reading of the "Limits" provisions in the Reinsurance Policies, in line with the underlying policies, was that the £16 million limit and the £4 million excess related only to the duty to indemnify and not to the additional duty to pay defence costs. The liability to pay defence costs was parasitic on the duty to indemnify. As such, the Reinsurers' exposure to liability for defence costs arose when the £4 million excess for indemnity costs was exhausted and ended when the £16 million limit for indemnity costs was reached.

### **The Claims Co-operation Clause Issue**

The Claims Co-operation Clause (which was agreed not to be a condition precedent) read:

"The primary insurers shall in the event of an occurrence or series of occurrences consequent upon one original cause which may be the subject of a claim under the policy and where the potential cost may exceed £4m, or in the event of the potential cost of such an occurrence or series of occurrences reac[h]ing £4m give notice to re-insurers as soon as practically possible and furnish all available information respecting such occurrence or occurrences if required.

In either such event the course to be adopted by the primary insurers shall be determined by agreement between the primary insurers and re-insurers and the primary insurers shall not without the consent of re-insurers litigate with regard to such loss but such consent shall not be unreasonably withheld.

In the event of a difference of opinion between the primary insurers and re-insurers in respect of an opportunity whereby settlement of a loss can be obtained by the acceptance of a standing judgment or transaction agreed by the claimant reinsurers retain the right to pay to the primary insurers the amount the equivalent to their liability under this policy according to such standing judgment or transaction and shall thereafter be under no further liability under this policy in respect of the loss."

Reinsurers sought to rely on the well-known case of *Scor*<sup>2</sup> and argued that the Claims Co-operation Clause circumscribed the Reinsureds' power to make settlements binding on the Reinsurers, so that they were only bound to follow settlements which had been agreed between the Reinsurers and the Reinsureds.

However, the Judge noted that the decision in *Scor* was on the particular form of claims co-operation clause in that matter. The Judge distinguished the wording of the Claims Co-operation Clause at issue here, which did not expressly prohibit the Reinsureds from entering into settlement agreements without consent, but only from litigating without the consent of Reinsurers. The only provision made within the clause for a situation without agreement was where the Reinsured wanted to litigate and the Reinsurer wanted to settle. A situation where the Reinsured wanted to settle was not addressed, and the Judge found that was an indication that the clause was only intended to restrict Reinsureds' freedom to litigate and not to settle.

The Judge therefore held that this particular form of Claims Co-operation Clause could be read consistently with the Follow the Settlements Clause. This meant that Reinsurers were in principle bound by the Follow the Settlements Clause whether or not they had approved settlements entered into by the Reinsureds.

The Judge went on to find that Reinsurers had agreed to the course to be adopted in any event. The Judge found that references in the correspondence to Reinsurers "*reserving their rights*" meant only that, although Reinsurers approved the course being taken by Reinsureds, they were not committing themselves to accepting a liability to indemnify.

### **The Proper and Businesslike Steps Issue**

It is established law, following *Scor*, that the effect of a follow the settlements clause is that Reinsurers are bound by settlements entered into by the Reinsured, provided that the claim recognised by the Reinsured falls within the risks covered by the reinsurance as a matter of law, and provided that the Reinsured has acted honestly and taken all proper and businesslike steps in making the settlement. If the Reinsured discharges the burden of showing that the claim settled falls within the risks covered by the policy of insurance, then the burden moves to the Reinsurer to plead and prove that the Reinsured failed to take proper and businesslike steps (*Gan v Tai Ping*<sup>3</sup>).

The Reinsurers in this case challenged whether the Reinsureds had taken all proper and businesslike steps. Reinsurers argued that, in entering into the settlements, the Reinsureds had taken an unreasonable interpretation of the New Jersey law that applied, and had entered into the TTSA prematurely without considering all relevant information.

The Judge considered the relevant law and noted that an allegation of failure to take proper and businesslike steps is tantamount to an allegation of professional negligence, referring to Field J's decision in *Tokio Marine Europe Insurance Ltd v Novae Corporate Underwriting Ltd*,<sup>4</sup> in which it was held that if a proposed settlement figure already represented a good deal, the failure to investigate or raise points that would not have affected that figure did not constitute improper or unbusinesslike conduct.

Prior to the TTSA, the Reinsureds had obtained legal advice from a New Jersey lawyer, Mr Miller, who reviewed relevant authorities on allocation methodologies in continuous trigger liability cases and advised that the proposed settlement was

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<sup>2</sup> *The Insurance Co. of Africa v Scor (UK) Reinsurance Co. Ltd* ("*Scor*") [1985] 1 Lloyd's Rep. 312.

<sup>3</sup> [2002] EWCA Civ 248.

<sup>4</sup> (No. 2) [2014] EWHC 2105 (Comm).

advantageous. The Reinsurers argued that Mr Miller had recommended an unreasonable level of payment not based upon an appropriate allocation methodology as a matter of New Jersey law.

The Judge held that the Reinsureds bore responsibility for the advice they relied upon in entering into the TTSA and considered whether that advice was “*such as no careful lawyer, reasonably competent in the law of New Jersey, could have given, so as to make the decision to settle on the basis of it a failure to take proper and businesslike steps*”<sup>5</sup>.

The Judge, having heard expert evidence on New Jersey law and having considered all the legal advice given by Mr Miller, concluded that the legal advice the Reinsured received was not negligent. He found that Mr Miller reached a reasonable interpretation of the relevant authorities on a question where opinions may differ, and formed a view on the Reinsureds’ prospects of success. Significantly, the Reinsureds’ views were made known to Reinsurers who were content with how the matter was handled. Further arguments around an alleged lack of verification of policy details and the timing of the settlement were also rejected.

Reinsurers were therefore bound by the Follow the Settlements Clause.

### **The Interest Issue**

At issue was the date of commencement of an award of interest and the rate at which it should be awarded.

### **Timing**

The Judge found that the Reinsureds’ interest should run from the date of the respective losses. The Reinsurers contended that it should run from a date no earlier than when the Reinsureds had particularised the quantum of the claim. This was argued on the basis that a discretionary approach is appropriate in reinsurance claims, as the Reinsurers would have no idea of the existence of a loss, but would be dependent on the presentation of a claim and the data relied on in support. In addition, the Reinsurers needed a reasonable period of time to consider the same.

The Judge found that interest would run from the date of the loss. This reflected the established position that the (re)insurer agrees to hold the (re)insured harmless, and is in breach of this obligation from the date of loss. Any delay in payment keeps the (re)insured out of its money and preserves it in the hands of its (re)insurer. The previous authorities in this area pointed to a restrictive approach to disallowing interest from the date of loss. Further, uncertainty in the quantification of the claim was not a reason to disallow interest.

### **Basis of calculation of interest**

The Judge found that the Reinsured was entitled to simple interest at the rate of 2% above the Bank of England base rate from the date of each respective loss. The Judge considered the decision in *Sempra Metals Ltd*<sup>6</sup> and noted that insurance markets are an area in which losses can be more commonly reflected by compound interest than some other areas of activity.

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<sup>5</sup>Paragraph 69 of the judgment.

<sup>6</sup> *Sempra Metals Ltd v Inland Revenue Commissioners* [2007] UKHL 34.

However, the Judge declined to award interest on a compound basis due to the fact that the Reinsureds had failed to particularise and prove this loss. They had simply pleaded an entitlement to it.

## Comment

The issue of whether the reinsurance limits and excess include underlying defence costs has not been considered in England previously, as far as we are aware, in any case (other than *Scor* on a different aspect). There was for many years a controversy over limits in the US as a result of the *Bellefonte*<sup>7</sup> decision, finding that the reinsurance limit was treated as costs inclusive. That decision has now been overruled, on the basis that it is a matter of construction in each case – and industry practice is to treat the limit as costs exclusive where the ceded risk is written on such basis. The decision here makes obvious sense in light of the back-to-back nature of the cover as to the excess (as it would have done to the limit had the limit been relevant).

The judgment does appear to produce one unsatisfactory result. Had the underlying settlements breached the £4m excess, Reinsurers would then have become liable for defence costs thereafter – but those costs would already have been incurred. This is a common issue in underlying layered liability programmes written on a defence costs exclusive basis, and wording is usually seen generating a retrospective re-allocation of defence costs amongst the impacted layers, proportionate to the indemnity settlement. There does not seem to have been any express wording in the reinsurance to address this issue.

In relation to the Claims Co-operation Clause, the judge appears, in our view, to have correctly distinguished the wording from *Scor* in that consent to settlement was not required by the policy wording at issue here. That makes sense more generally, as a follow the settlements clause and a settlement consent clause are inconsistent.

There has historically been limited authority on the application of the proper and businesslike manner test, not least because the market generally prefers to arbitrate rather than litigate reinsurance disputes. Originally, it might be said that this looked to the cedant's claims process<sup>8</sup>, with the Reinsurer agreeing to follow settlements provided the cedant continued to approach claims as it would/should do absent reinsurance. This focus on process came into sharp relief in the *Novae* case where there was no process because the underlying insured offered a deal (for reasons unrelated to its claim) that was more favourable on any view than the usual adjustment process could produce. Faced with an argument by reinsurers that the process needed to be undergone anyway, the cedant argued that the test was equivalent to that of professional negligence and that it was not negligent to accept such a favourable offer. The Judge in *Novae* simply accepted that submission, and the test of professional negligence now seems to have become entrenched in English law, – the point not being argued in this case.

There may not often in practice be much of a difference between a test of proper/business-like steps and professional negligence. But there could have been here. The Reinsured's claims manager relied on professional US legal advice in settling, which was argued to have been negligent. It was not suggested that there had been some relevant error in the instructions, or that the claims manager should have appreciated a problem with the advice. While negligence of the US lawyers was not found in the case, one might ask that if there had been, whether that is really the sort of situation that the parties (or the market) would objectively intend should remove the follow settlements clause protection? Surely the reinsurer would expect to be bound, and take the benefit of any subsequent recoveries from the negligent lawyer.

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<sup>7</sup> *Bellefonte Reinsurance Co. v. Aetna Cas. & Sur. Co.*, 903 F.2d 910 (2d Cir. 1990).

<sup>8</sup> *Charman v GRE* [1992] 2 Lloyd's Rep 607.

As regards interest, the starting point is usually the legal fiction that an insurer is in breach from the moment of an underlying property loss, or liability incurred by the insured, for failing to prevent that loss or liability from being incurred. At reinsurance level, it now seems established that the Reinsurer is in breach upon the Reinsured's own settlement with the insured, regardless of the nature of the underlying risk. Interest is discretionary and compensatory, but should in principle run from that moment.

That said, there have been insurance cases where interest has been delayed for one reason or another. Most recently, in the context of the Russian Aircraft Litigation, Butcher J found that the court should exercise its discretion to allow insurers some time to consider their position after a loss, before interest will run following *Quorum v Schramm (No 2)*<sup>9</sup>. So, in other words, there is some inconsistency in the court's position here and it will depend on the precise circumstances of each case.

Another relevant aspect is that there has also been a decision on the implied term to pay claims within a reasonable time, that such period may be up to a year in *Quadra v XL*<sup>10</sup>. Following *RSA v Equitas* this presents a perhaps unusual situation where an insured may not reasonably expect a claim payment until, say, a year post-loss, but will be treated as entitled to such from the date of the loss for interest purposes.

Although not new law, it is also noteworthy that compound interest could potentially have been recovered had proof of loss on this basis been put forward and it highlights the need to ensure that any claim for compound interest is properly supported by evidence and not simply pleaded. It is not clear however, why the Commercial Court ordered a rate of 2% over base, rather than its usual award of 1% over base. The reason is not evident from the judgment, and the issue does not appear to have been argued.

Note that permission to appeal was granted in the case on 27 March 2026.

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<sup>9</sup> [2002] All ER (Comm) 179.

<sup>10</sup> [2022] EWHC 431 (Comm).