European Commission does not favour it and we might see new life being injected into the Commission's proposed Directive on the winding-up of insurers. Negotiations on this proposal have come to a halt since a Commission amendment was proposed in 1989. (Commission Proposals (COM(86) 768) and (COM(89) 394)).

4.2 Supervision of conglomerates

The second area which we can expect to receive attention is the supervision of financial services conglomerates.

"Bancassurance" and **"Allfinanz"** - the offering of insurance and other financial services by banks, insurers and investment houses - have highlighted the need for closer co-operation between bank regulators and insurance regulators.

How does one classify "Bancassurance" for example and who should supervise it - insurance regulators or bank regulators? With banks competing with insurers as distributors of many personal lines products it is possible that this debate will become quite heated and any change in favour of the banks is likely to meet strong resistance from the insurance industry.

3. LEGAL UPDATE ON REINSURANCE CASES

By John Thomas Q.C.

The past year has seen a number of cases dealing with reinsurance topics. I will deal briefly with some of the more important – nothing really new, just a discussion of some old chestnuts.

Use of a Slip in Construing a Treaty

One of the most interesting judgments in the past 12 months was the judgment of the Court of Appeal given in February in *Youell v. Bland Welch. The Super Hulls Case* [1992] 2 Lloyd's Rep. 127 The case concerned the reinsurance of the construction risks of LPG carriers under construction at the Avondale Shipyard and a claim in the 1970s made under that reinsurance by the insurers of the vessels. The detailed facts of the case are of no intrinsic interest and the other part of the case, namely the claim against the brokers for negligence was no doubt dealt with at last year's conference; the appeal against that judgment was compromised during the course of the hearing in the Court of Appeal.

The one point of interest in the case was the argument made by this morning's Chairman (Mr Mance Q.C.) that it was permissible to refer to the slip as an aid to the interpretation of the reinsurance wording. This argument had been unsuccessful at first instance before Phillips J. In the Court of Appeal Beldam L.J. was of the firm opinion that the slip was inadmissible in construing the wording. He made a careful review of the authorities prior to 1906, considered that the law was clear then and the slip remained inadmissible today. Staughton L.J., on the other hand, left the question open. He pointed out that it was somewhat old fashioned to approach the problem in terms of examining the parol evidence rule as the modern approach was to admit (as happened in almost every case in which the Courts were concerned with issues of construction) evidence of the surrounding circumstances. However, he pointed out that the difficulty with respect to a slip lay in the fact that evidence of the parties' negotiations was inadmissible and, a slip, although it represented a concluded agreement between the parties, was a preliminary agreement only and the parties in embodying the agreement in a formal document might alter the meaning in agreeing that formal document. As he did not find the slip of assistance in construing that particular reinsurance treaty, he left the point open.

It is quite clear that if you ask someone in the market to see what the parties agreed even where there is a concluded treaty, he will automatically look at the slip first; if this is what the practitioners do in every day commerce, it is unreal to ignore it. Moreover, it is important to bear in mind that the time and level of ability that is quite often devoted to treaty wordings is not commensurate with their importance and in many cases it is probably a fiction to pretend that either party has consciously tried to improve upon the agreement contained in the slip. It is a great pity that the way in which such wordings are produced is not more widely known and that the slip is treated by many as the document which represents the intention and bargain of the principal persons on each side.

Therefore it seems to me, with respect to Beldam L.J.,that his approach is over-strict and ignores commerical reality; that a court should be able to look at the slip in cases where it may be of assistance. However, as Staughton L.J. rightly pointed out, one must be on one's guard against the parties amplifying or altering the meaning when producing the wording.

There is no doubt that those in the industry should devote more time, as many are now doing, to the accuracy and importance of wordings.

Follow the Settlements and Summary Payments

It is hardly surprising that the year has yet again seen a number of cases where the Courts have been concerned with the circumstances in which a reinsured is entitled to payment from his reinsurer.

I think one must begin by mentioning *Hiscox v. Outhwaite (No. 3)* [1991] 2 Lloyd's Rep 525 and the disquiet in the market over the past year caused by this decision in contrast with what many consider a more commercial approach shown by the American courts in the first instance decision in *Unigard v. North River*. However, no doubt to the disappointment of many in the market, *Hiscox v. Outhwaite* was settled prior to the matter being determined by the Court of Appeal.

There were, however, during the year two cases where the more general problem that frequently arises on the "follow the settlements" clause was considered. In the first of these *Charman v. G.R.E.* 3 July 1991Webster J. held that where there is a follow the settlements clause in a contract, the burden of proof lies upon the reinsurer to displace the reassured's right to rely as against him upon the settlement agreed; therefore, if the reinsured proves the settlement or compromise of an original claim against him, this binds the reinsurer unless the reinsurer can prove either that the compromise was dishonestly arrived at or that the reassured has failed to take all proper and businesslike steps to have the amount of the loss fairly and carefully ascertained. The rationale for this decision was that Webster J. considered that the essential element of a follow the settlements clause was that the reinsurer has put his trust in the reassured, that there was a presumption that he had carried out that trust and the burden lay upon the reinsurer to displace it.

This is a useful case for reinsureds. In the second case, *Württembergische* 4 July 1992, where the clause of the reinsurance treaty was somewhat different and required the reinsured to prove that there was liability under the terms of the original policy, Evans J. held that nonetheless the burden was prima facie discharged by proof of settlements made in the ordinary course of business. In an eminently practical judgment, Evans J. said that although the reinsurer was entitled to put the reinsured to proof of their claims, the reinsured discharged the evidential burden of proof by producing the records and claims in proper form, the burden then shifting to the reinsurer to challenge the accuracy of the records or the good faith of the settlement or the liability of the reinsured to the original assured:

In October 1991, Hoffman J. had to consider an attempt to present a petition to wind up a reinsurance company which had not paid a claim under a reinsurance but which contended that it was entitled to inspect the documents under the inspection clause prior to payment. *In Re a Company ex p.N.D. Pritchard* (October 1991). Financial Times, November 22 1991 the Judge held that it would be wrong, where there was a bona fide desire to exercise rights under the inspection clause to compel payment prior to that inspection.

Finally, in another case in the Chancery Division In Re a Company No. 00. 13734 of 1991 [1992] 2 Lloyd's Rep. 415 Mr Roger Kaye Q.C. was faced with a petition to wind up a reinsurer who had not paid a claim made by a reinsured which was under the winding-up order of the Bermudian court. The principal point taken by the reinsurer was that the reinsured was not entitled to be paid unless he had himself paid on the original claim. Mr Kaye was, in my view, rightly prepared to accept that under the type of clause used in that treaty which had been considered by Hirst J. in *Home v. Mentor* [1989] 1 Lloyd's Rep. 473 at 480 and in by Sterling J in the last century in *Re Eddison Marine Insurance* [1892] 2 Ch. 423 if it was sufficient for the reinsured to be able to claim from his reinsurer payment if he was liable to pay, not that he had in fact paid. However Mr Kaye refused to allow the petition to wind up the reinsurer to proceed because he considered that there were other and complex issues unsuitable for determination on an interlocutory matter of that kind.

The interest of the case is, therefore, the clear indication again that under the types of clauses most commonly found, reinsurers are bound to pay an insolvent reinsured even though the latter have not actually paid the original assured.

Arbitration

No doubt the extremely important Judgment in *Harbour Assurance v. Kansa* [1992] 1 Lloyd's Rep. 81 was considered at last year's conference. It is again unfortunate that the very important issue as to the effect of illegality on an arbitration clause was not considered by the Court of Appeal as this case was also compromised prior to the hearing of the appeal. However, as the Judgment, which contains the clearest possible analysis of the problem, was undoubtedly correct in setting out the classic position in England law, there can therefore remain little doubt that, unless the Court of Appeal feels it was able to reform English law (which in this respect would be highly desirable) the decision in the case will stand as the exposition of English law on this matter.

One can only hope that this defect in English law will be addressed in any legislation on arbitration that may come before Parliament. Quite clearly from a survey of arbitration clauses undertaken by A.R.I.A.S. this year, there was unanimity in the view that it was highly undesirable that parties to a contract should have to have disputes determined both in court and in arbitration and the position in English law in compelling resort to the courts in cases of illegality was deplored.

Of much less importance (!) was the decision in *Pan Atlantic v. Hassneh* [1992] 2 Lloyd's Rep. 120 where one of the parties to an arbitration tried to prevent the President of this Association (Mr John Butler) hearing an arbitration because he had retired from his office at the Mercantile & General. Although taken to the Court of

Appeal, the attempt failed. In giving judgment in the Court of Appeal Leggatt L. J. stressed that the purpose of the clause restricting the appointment to "executive officials of insurance or reinsurance companies" was to ensure that the right sort of person sat as arbitrators, rather than to ensure that those appointed kept their hand in.

The importance of the case is to remind the market of the difficulties which can be today work simply do not have the time, there is available the expertise of those who are recently retired from the industry but who keep closely in touch with what goes on.

Subrogation

Although of importance both in direct insurance and reinsurance, it is worthwhile briefly mentioning the important decision of the Court of Appeal in July in *Napier v. Kershaw* (9th July 1992) Court of Appeal, The Times, July 17, 1992. This case arose out of the settlement of the litigation brought by the Names against the Outhwaite agency at Lloyd's. On the settlement of that litigation the stop loss reinsurers of the Names sought to be subrogated to the recoveries. Two points were dealt with – whether the monies collected by the solicitors for the Names were the subject of a trust in favour of the stop loss reinsurers and the way in which the excess under the stop loss policy operated. It is the first of these points that is of great general importance and on which the text book authority was conflicting. Saville J. and the Court of Appeal both decided that the recoveries were not subject to a trust. Quite apart from being, in my view, correct as a matter of authority, it must be right in principle that insurers and reinsurers are, in the case of an insolvent insured or reinsured, in no better position than the general body of creditors. I understand the matter may proceed to the House of Lords and it will be interesting to see what the House of Lords makes of this and the other, though less important, point.

Illegality

The issues decided by the Court of Appeal in *Phoenix v. Halvanon* [1988] QB 216 have been the subject of so much unhappiness in the market that it is hardly surprising that whenever an opportunity arises to re-litigate that unfortunate decision a chance is not taken to see if it can be reversed.

The current year has seen an important further attempt – *D.R. Insurance V. Seguros America Banamex* 30th July 1992, Adrian Hamilton Q.C. sitting as Deputy Judge. This matter arose out of claims by the Plaintiffs as assignees of Elkhorn Insurance Company under internal retrocessions made of risks accepted in the name of Elkhorn by the Stetzel Thomson pool in Great Britain. The Defendant retrocessionaires

claimed that the policies written by the pool and the pool retrocessions were illegal and void under the Insurance Companies Act 1982. In very brief outlines, the Stetzel Thomson pool had used that system commonly used in London in the 70's and early 80's where the managers of the pool had "reserved a line" for the pool participant, communicated the details of that reservation to the pool participants and only communicated the acceptance of the risk to the broker when they had heard from the pool participant. However, Adrian Hamilton Q.C. (sitting as a Deputy Judge) held that each of the pool participants was carrying on insurance business in Great Britain even though the final decision to underwrite the insurance was taken overseas as the contracts were effected in Great Britain and also carried out there. He held that the extent of the managers' activities on behalf of the pool participants was so extensive and important as to constitute the carrying on of insurance business in London by each of the pool participants.

Given that conclusion of fact (which seems on the findings in the judgment to have been plainly correct) Adrian Hamilton Q.C. was much troubled by the fact that Elkhorn (who he found had never intended to break the law and who had behaved innocently) would be unable to recover on the internal pool retrocessions. Careful consideration of *Phoenix v. Halvanon* and the decision of Knox J. in the *Cavalier Insurance* [1989] 2 Lloyd's Rep. 430 case led him to the conclusion that *Phoenix v. Halvanon* was correct and he specifically found that the principles decided in these cases applied to reinsurance. The important judgment also reviews the many other arguments (incidentally also advanced in this case by today's Chairman, Mr Mance Q.C.) that had been raised in other cases in relation to the legislative history of the Insurance Companies Act and in particular the effect of the European directives. He held that these made no difference to the conclusion in *Phoenix*.

However there was one new issue, that has often been raised at seminars and conferences that Mr Hamilton had to consider - whether Section 132 of the Financial Services Act was retrospective. Unless a court, and one probably at a high level, was prepared to be exceptionally bold, it would be very difficult to say that Section 132 was retrospective. That indeed was the decision of Adrian Hamilton Q.C. and, speaking entirely for myself, I doubt very much whether a court would be prepared to depart from this orthodox decision. It is of little comfort to the industry that Mr Hamilton concluded his judgment by very much regretting the conclusion he had reached but considered it "inescapable"-but the remedy lies only in Parliament, unless your chairman for today proves me wrong!