14. *Luxembourg:* Implementing legislation is expected to be adopted in the next two/three months. The Insurance Commissioner has, however, stated that, as of 1st July 1994, EU/EEA insurers will be treated as though the Directives had been incorporated into Luxembourg law.

15. *Norway:* Implementing legislation is expected to be adopted by October 1994.
16. *Spain:* In accordance with agreed transitional arrangements Spain is not obliged to implement the Directives until the end of 1996. In practice legislation may be adopted and come into force by February 1995.

17. *Sweden:* Implementing legislation is being prepared and it is anticipated that it will enter into force in January 1995. Transitional arrangements were agreed by Decision of the EEA Joint Committee of 21st March 1994 in relation to the maximum amount of investments which can be required in negotiable securities under the Third Life Directive.

PAN ATLANTIC INSURANCE CO. v. PINE TOP INSURANCE CO. – THE IMPLICATIONS OF THE DECISION IN THE HOUSE OF LORDS

by Jonathan Gilman, Q.C.

This talk is a sequel to one which I gave earlier this year. For those of you who missed the first instalment, I was invited to speak at a BILA Seminar on "Avoiding Legal Pitfalls" in Managing Claims in May of this year, on the implications of the *Pine Top* decision. There was one slight snag – or pitfall – as far as my lecture in May was concerned, which was that the House of Lords had failed to oblige by delivering their judgment. They eventually did so in late July – and now I have been asked to talk to you about the real thing.

Fortunately, I was careful enough in May not to chance my arm with any very precise predictions, beyond saying that I was fairly sure that avoidance for misrepresentation and non-disclosure would not be made any easier by the House of Lords. That at least is clearly part of the outcome.

Pan Atlantic v Pine Top was expected to be and has proved to be a landmark decision. Its importance has been recognised (which is not always so with important cases, unfortunately) by the Law Reports' editors. You can find it already reported in more than one series. For today's purposes, I will use the W.L.R. reference –

[1994] 3 W.L.R. 677.

In substance, as Lord Mustill's speech confirms (p. 692), the case was an appeal from the *C.T.I.* decision. To set the background, with which I expect you are all familiar anyway, in *C.T.I. v Oceanus* [1984] 1 Lloyd's Rep. 476, the Court of Appeal decided

(i) that it was not necessary to show that the actual underwriter was influenced by the misrepresentation or non-disclosure for which he subsequently avoids the policy, and

(ii) that the test of materiality is whether a prudent insurer (in practical terms, the expert witness called by the Defendant) would take the relevant matters into account as part of the process of forming his underwriting decision – sometimes called the "want to know" test, whether or not the prudent insurer would in fact have reached a different decision.

In rejecting the actual underwriter test, Kerr LJ recanted from his earlier decision in *Berger v Pollock* [1973] 2 Lloyd's Rep. 442 where he had held the opposite. In introducing the "want to know" test, as the sole test, the Court of Appeal in *C.T.I.*, many people think, opened a Pandora's box. This aspect of the decision, in particular, met with a chorus of criticism – Lord Mustill deals with it in some detail. Whether in fact the *C.T.I.* case meant that insurers and reinsurers succeeded in any borderline avoidance cases, where they would not have succeeded anyway, I venture to doubt; I also doubt whether *C.T.I.* was to blame for the fact that avoidance has been more frequently invoked since the mid '80s, which is more obviously due to market circumstances. But it is certainly the case that *C.T.I.* was widely regarded as tipping the balance unduly in insurers' and reinsurers' favour. So the background to the *Pine Top* appeal was that the House of Lords were being asked to rethink the principles governing the right of avoidance in a context where the existing state of law was widely seen as unsatisfactory – including, by the Court of Appeal in *Pine Top* itself.

The menu à la carte for the House of Lords was as follows:–

(i) Should there be an actual underwriter test; and if so, must it be shown that the actual underwriter would probably have reached a different decision, if the material facts had been disclosed, or accurately represented, or would something less than decisive influence be enough?

(ii) Should the prudent insurer test be reformulated, as a decisive influence test, or remain its *C.T.I.* form as a want to know test?

It was common ground in the arguments before the HL that the "increased risk" formulation which you will find in Steyn LJ's judgment in *Pine Top* in the C.A. meant the same as the *C.T.I.* test; and it was not suggested that the prudent insurer test should be done away with altogether – it could not be at least in Marine insurance, because it is in the 1906 Act; the points at issue were how the prudent insurer materiality test should be formulated, and whether an actual underwriter test – a second fence to jump – should be required as well, as Kerr J. had originally held in *Berger v Pollock.*

It is fairly remarkable in this day and age that such fundamental questions should still have been open to debate. In fact, it is apparent from Lord Mustill's review of the authorities and of the early insurance textbooks that the issues at the heart of the debate in *Pine Top* genuinely were open to question; they were confronted more clearly in the textbooks than in any of the cases before *Berger v Pollock* and *C.T.I.*, but the authors of the classic 19th century textbooks were divided. Lord Mustill's speech contains an interesting historical account – for any of you who are interested in such things. Arnould, I'm happy to say, has throughout been on what is now the winning side and in the absence of a new edition (no questions please on when to expect one!) you will find that Arnould contains a pretty accurate account of what is now the established law, at least as regards the actual underwriter requirement.

The House of Lords unanimously decided that an insurer or reinsurer can only avoid where the actual underwriter was induced to accept the risk, or to do so on the terms that he or she did, by material misrepresentation or non-disclosure on the part of the assured or reassured or their brokers. Inducement is not defined, and some debate has already been generated as to what this test means. For myself, I do not see that it presents any great difficulty. Nor evidently did the House of Lords, as they were content to say that the test was the same as the common law test of inducement which applies generally to misrepresentation in the field of contract.

The fact that there is no general common law equivalent to avoidance for non-disclosure does not, as it seems to me, give cause for any real uncertainty about what "inducement" should mean, in relation to non-disclosure. It is pretty clear, I think, that the law now is that an avoidance can only be upeld where it can be found as a fact or as an inference of fact that the actual decision to accept the risk or as to

the rate or other terms on which it was accepted was influenced by the material misrepresentation or non-disclosure complained of; causation is required; the decision must have been materially affected, the misrepresentation having played a real and substantial part leading to what on a balance of probabilities was a different decision from that which would otherwise have been made.
In reaching the unanimous conclusion that causation, an actual underwriter test, was required the House of Lords adopted a fairly creative approach to statutory interpretation (the 1906 Act makes no reference to the actual underwriter, only to the prudent insurer, but the House of Lords was able to conclude that the test was implied in the 1906 Act). I was not sure beforehand that the H.L. would be able to find a way round the wording of the 1906 Act, and was concerned that the case might open up distinctions between marine and non-marine.

The House of Lords decided by a majority (Lords Goff, Mustill and Slynn – the minority comprising Lords Templeman and Lloyd) that the prudent insurer materiality test did not require it to be shown that a prudent insurer would have reached a different decision. The majority rejected the decisive influence test for materiality, taking the view that a "decisive influence" requirement would be contrary to the natural and ordinary meaning of the provisions in ss. 18 and 20 of the 1906 Act, which reflect the common law; on this point, there was no room for implying terms into the statute; these Sections refer to circumstances which would influence the judgment of a prudent insurer in fixing the premium or in determining whether he will take the risk. "Influence the judgment" is not the same as "change the mind" (per Lord Mustill, at p. 695). Secondly, the majority considered that so long as there was also an actual underwriter requirement, to retain (in effect) the *C.T.I.* test for materiality would have no adverse consequences and some practical advantages. Those of you who attended my previous lecture may recall that my preference would have been for the Lloyd view rather than the Mustill view, which has prevailed.

The decision on materiality leaves the position as it was before. The insurer or reinsurer must find an expert witness to say, at least, that the circumstances giving rise to the dispute were material in his opinion in the sense that he would have taken them into account when forming an underwriting judgment on the risk (if it had been offered to him), even if he might have made the same underwriting decision. In practice of course, no defendant in his right mind would let an avoidance case get to court unless he could produce an expert who would have reached a different decision; an expert who would merely have wanted to know would be unlikely to

impress.

At two points in his speech, Lord Mustill refers to there being a "presumption of inducement" once materiality is established (at p. 705; and at p. 712). This is not developed, but it is a point of some potential importance. In most avoidance cases, the actual underwriter or at least the leading underwriter gave evidence anyway; not to call him when he was available to be called, might suggest lack of merit in the case. As Kerr J. said in *Berger v Pollock,* except in the most obvious cases the underwriter should be called. The practical importance of a presumption – which can plainly only be a rebuttable presumption, or a factual inference to be drawn – is that it caters for those cases where the underwriter cannot be called or where he has no recollection (which is more common). It would, I think, be unwise for any prospective defendant to rely on the presumption in a case which was in any way borderline as an excuse for not calling an available witness; but that is not to say that there will not be cases which ultimately turn on a presumption or inference, materiality having been proved by expert evidence, of what the actual underwriter's attitude would have been.

Although the *Pine Top* decision has largely settled the law, for at least the foreseeable future, it will be clear from what I have said that I do not think that the restoration of the actual underwriter equipment coupled with the retention of the *C.T.I.* test for materiality will make a great deal of practical difference to the way in which avoidance disputes are actually handled and litigated in practice.

One difference may be that it will be necessary now to call underwriting witnesses from the following market as well as the lead syndicate; plaintiffs may now be less inclined to simplify the task for defendants in cases of this type by an agreement to be bound or a representative action, and may find it to their advantage to put the Defendants through the hoop of having to call numerous underwriters. Apart from that factor, I would summarise the effect of *Pine Top* as being that the legal requirements for a valid avoidance have been tightened in what I regard as a satisfactory way, but restricting avoidance to cases where the actual underwriting decision was affected by misrepresentation or non-disclosure, but that the practical considerations which any insurer or reinsurer should take into account before embarking on the serious step of avoidance, and before taking the serious decision to stand and fight in Court with all its attendant publicity remain essentially the same as they were before. If any insurers are now deterred from avoiding in unmeritorious cases, where they merely made a bad underwriting decision which

they would have made anway, that is no bad thing; but most cases have more substance to them, or at least the insurers sincerely believe they were misled before they resort to avoidance, and the *Pine Top* decision should not discourage meritorious cases or make them more difficult for insurers. In practice, an insurer who has a proper case should not notice the difference.

UNFAIR CONTRACT TERMS DIRECTIVE
by Keith Long, DTI

You have invited me to speak to you today on the Unfair Contract Terms Directive. This directive was adopted in April last year and is due to come into force at the end of this year. The directive has, I know, provoked a good deal of concern amongst insurance companies, for whom legislation in this field is something new.

What I want to do now is not to explain the ins and outs of the Directive itself – I assume you will all have read the two consultative documents published by the Department in October 1993 and September this year – nor to give a detailed Government reaction to the responses that the Department has received to the second Consultative Document – after all, the closing date for comments was only last Monday – but to give you some thoughts on the underlying reasoning for why insurance is included in the directive and what the implications may be.

The purpose of the Directive is to change the balance between suppliers and consumers in consumer contracts by "eliminating unfair terms", that is, terms that act unfairly towards consumers.

In the European Commission's own Explanatory Memorandum in 1990 explaining their proposal, the problem of unfair contract terms had already been recognized by a number of member States. Since 1974 most States have adopted unfair contract terms legislation. The Commission noted specifically that "British law differed from the law of other member States in that it excludes contracts of insurance from the application of the Unfair Contract Terms Act 1977, whereas insurance is not excluded by the law of other countries". The Commission did not refer to the alternative of the voluntary ABI Statement of Recommended Practice that has stood alongside the UCTA, but even if it had it is doubtful whether this would have altered their position. It was always the Commission's intention therefore that the