



Inner House, Court of Session

- **Mitchell v Hiscox Underwriting Limited** [2010] CSIH 18 (Avoidance, Misrepresentation)

## Guest article

- The Bribery Act 2010

## Catch up

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## Jewellers Block, Unexplained Loss Exclusion, Condition Precedent, Breach of Warranty

**Widfree Limited (trading as Abrahams & Ballard) v Brit Insurance Limited** [2009] EWHC 3671 (QB)

The claimant was a jewellery shop owned and run by a husband and wife, Mr and Mrs Abraham, which had taken out an insurance policy (the Policy”) with the defendant, dated 15 February 2008.

On 9 October 2008, two women who were behaving erratically came into the jewellery shop. Mrs Abraham showed the women some items of jewellery but they left without purchasing anything.

On 22 October 2008, Mr Abraham tried to find one of the shop’s most expensive items, a diamond ring valued at over £100,000, to show to a customer. A search of the display cabinets and safe revealed that the item was missing. Mrs Abraham thought back to the incident with the two women and concluded that they had stolen the ring. Mr Abraham reported the missing ring to his insurance brokers and the police.

Two police officers attended the shop and watched the security footage from the incident in question. Although the shop had five CCTV security cameras in operation at the time of the incident the officers felt that the footage from only one camera was useful, although this did not clearly show the women stealing the ring. Mr Abraham arranged for this footage to be downloaded from the hard drive, onto a DVD, by the CCTV system operator Nationwide Security. All security footage on the hard drive was retained for a period of at least a week.

The defendant appointed a loss adjuster who visited the claimant on 6 November 2008. The loss adjuster’s report was later shown to contain numerous inconsistencies and inaccuracies. In a letter to the claimant, dated 21 January 2009, the defendant denied liability on the basis of the Fidelity and Unexplained Loss Exclusions in the Policy.

The defendant later accepted that there was no basis for relying on the Fidelity Exclusion but denied that they were liable to indemnify the claimant on three grounds, namely:

1. That the loss of the ring fell within the Unexplained Loss Exclusion in the Policy. This exclusion stated that any insured items which are found to be missing during stocktaking, where the Insured is unable to prove the date and circumstances of the loss will not be covered by the Policy.
2. That there was a breach of a General Condition of the Policy, namely a condition precedent that the Insured provide the Insurer with such information and evidence as the Insurer may reasonably require. The defendant claimed that this Condition had been breached as the claimant had not provided it with security footage taken from all five cameras.
3. That there was a breach of a warranty which stated that a security guard would be in attendance at all times. The security guard had in fact been outside the shop watching through the window. The defendant later abandoned this ground in their closing submissions.

## Held

Mr Peter Leaver QC, sitting as a deputy High Court Judge, held that in relation to the Unexplained Loss Exclusion the definition of stocktaking was to be given its ordinary meaning, a structured and organised process which is undertaken at regular intervals. The defendant's argument that when looking for the missing ring Mr and Mrs Abraham could be described as stocktaking was therefore rejected. Also, it was held that on the balance of probabilities the claimant could prove the date and circumstances of the loss.

In relation to the breach of the General Condition, it was held that the loss adjuster had never asked for the footage from the other cameras and should have known that such footage was not retained indefinitely. It was not for the claimant to attempt to guess what evidence the Insurer might want to see. In light of the advice from the police officers, it was satisfactory that Mr Abraham only downloaded the footage from the one camera.

Judgment in favour of the claimant.

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## Brokers Duty of Care, Directors' and Officers' Liability Insurance, Third Party Rights

In **Crowson v HSBC Insurance Brokers Ltd** (2010) Unreported, Hughes Brickworth Limited ("HBL") had entered into an arrangement with HSBC Insurance Brokers Ltd ("HSBC") who agreed to put into effect insurance policies identical to policies that had been arranged by HBL's previous brokers. The previous insurance policies had included a director's and officer's liability insurance policy which HSBC failed to renew or replace.

HBL's managing director, Mr Crowson, who had sought to rely on the policy, brought a claim against HSBC in his own name for negligence and breach of contract, relying on the Contracts (Rights of Third Parties) Act 1999.

HSBC applied to have the claim struck out on the grounds that it did not owe Mr Crowson a duty of care at common law and that it was not in a contractual relationship with him.

Since this was an application to strike out, the judge only had to assess whether he agreed with HSBC that the case "disclosed no reasonable grounds for bringing the claim".

### Master Bragge held that:

It was at least arguable that Mr Crowson had a valid claim against HSBC even though it was HBL, not Mr Crowson, who had contracted with HSBC.

1. There are two situations where it is arguable that a broker could be liable in tort to a person who had not appointed him, namely:

- (i) Where a broker is instructed to arrange insurance for the person instructing him and for others;
  - (ii) Where a policy is intended to benefit a third party.
2. HSBC knew that Mr Crowson was the managing director of HBL and that he and the other directors required a director's and officer's insurance policy. HSBC also knew that such a policy would be for the benefit of the company and the directors. Mr Crowson gave instructions to HSBC on behalf of HBL and himself and was at least arguably acting as an agent for the other directors. There is arguably a contract between the broker and those for whose benefit the policy is effected.
3. In any event, the situation falls within the Contracts (Rights of Third Parties) Act 1999 and Mr Crowson has a right to enforce the contract on two grounds.
  - (i) Under section 1(1)(b) of the Act as the contract confers a benefit on him, namely insurance as a director; and
  - (ii) Under section 1(3) of the Act as he is expressly identified as a member of a class or answers to a particular description.

The application to strike out Mr Crowson's claim was dismissed.

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## Fraud, Exclusion Clause, Professional Indemnity Insurance

In **Goldsmith Williams (A Firm) v Travelers Insurance Co Ltd** [2010] EWHC 26 QB, the defendant had insured under a professional indemnity insurance policy a firm of solicitors, Joshua & Usman Legal Services Limited ("J&U"), against civil liability arising from its practice.

It was alleged that the directors of J&U had either been engaged in or had condoned mortgage fraud and that the defendant was therefore entitled to repudiate liability under the policy. This argument was based on the fact that there was an exclusion clause in the policy which provided that the defendant was not liable in the event of directors' fraud or dishonesty.

The directors of J&U were Mr Atikpakpa and Ms Usman. Mr Atikpakpa had applied to a mortgage provider ("Mortgages 5") for a loan to purchase a property. Mortgage 5 instructed Goldsmith Williams to act in relation to the proposed transaction. Ms Usman had assisted with the documentation for Mr Atikpakpa to obtain the loan.

The loan was granted but Mr Atikpakpa did not purchase the property, instead stealing the money. Mr Atikpakpa's wife subsequently applied for a second loan from Mortgage 5 to purchase a property owned by Mr Atikpakpa. The mortgage company again appointed Goldsmith Williams. Mr Atikpakpa, in his capacity as vendor, appointed J&U. Mortgage 5 advanced the sum of money to Mr Atikpakpa's wife, which was then transferred to J&U, but the transaction was never completed. Mr Atikpakpa stole the money. J&U were subsequently investigated by the Office of the Supervision of Solicitors and struck off the register.

By deed of assignment, Mortgage 5 assigned its claim against J&U to Goldsmith Williams. They in turn proceeded against J&U, claiming the total sums advanced by Mortgage 5. They relied upon their rights as assignee under the deed and the right to be indemnified under the Civil Liability (Contribution) Act 1978.

Goldsmith Williams obtained judgment against J&U (J&U did not defend the proceedings). Goldsmith Williams then brought proceedings against the defendant under the Third Parties (Rights Against Insurers) Act 1930 s.1.

The defendant argued that it was not bound to indemnify J&U and therefore also not liable to Goldsmith Williams. The defendant argued that it was entitled to repudiate liability under the policy based on an exclusion clause which provided that insurers “shall not be liable under the policy in respect of fraud or dishonesty” although “no such dishonesty, act or omission will be imputed to a body corporate unless it was committed or condoned by, in the case of a company, all directors of that body corporate”.

The defendant argued that the evidence established Goldsmith Williams’ claim against J&U arose from the dishonest and fraudulent acts of Ms Usman and Mr Atikpakpa.

Goldsmith Williams did not dispute that Mr Atikpakpa had acted dishonestly or fraudulently but denied that Ms Usman had condoned the activity and therefore argued that the exclusion clause did not apply.

**Mr Justice Wyn Williams, finding in favour of the Defendant, held that:**

1. The defendant was correct in its submission that Mr Atikpakpa was guilty of extensive dishonesty and fraud during his time as director.
2. There was evidence that Ms Usman had made fraudulent mortgage applications in her own right. She had additionally helped a further colleague to engage in fraudulent applications. It was not credible that Ms Usman was engaged in mortgage fraud herself but yet had known nothing of the other fraudulent activities going on in and around J&U. On the evidence Ms Usman had known of Mr Atikpakpa’s mortgage fraud and had aided and abetted Mr Atikpakpa's crime and had condoned his dishonest and fraudulent mortgage application, enabling him to obtain the loan.
3. If an insured condoned a course of conduct which was dishonest or fraudulent and that course of conduct led to or permitted the specific acts or omissions upon which the claim was founded, the insurer was entitled to repudiate liability (**Zurich Professional Ltd v Karim** (2006) EWHC 3355 (QB)).
4. The claim in respect of the first mortgage fraud had arisen from Ms Usman’s dishonesty in conducting the fraudulent acts on the part of Mr Atikpakpa.
5. Ms Usman had known of Mr Atikpakpa’s fraud relating to the second mortgage fraud (the apparent sale of Mr Atikpakpa's property to his wife). The fraud would not have taken place had Ms Usman not condoned the fraud. Therefore both Ms Usman and Mr Atikpakpa had engaged in or condoned dishonest or fraudulent activity.
6. The defendant was therefore entitled to repudiate liability under the exclusion clause.

## Notification, Date of Material Damage

### **Loyaltrend Limited v Brit UV Limited [2010] EWHC 425 (Comm)**

The claimant, a fashion retailer, brought a claim for property damage and business interruption under an insurance policy arising from subsidence affecting its retail premises in Notting Hill (“the Shop”).

Structural problems with the Shop arose from mid 2003 and continued until at least 2006. During this time the claimant’s brokers arranged insurance coverage which, unbeknownst to the claimant, was with three separate companies who each insured the premises over separate periods.

The claimant discontinued the proceedings against the companies who had insured it at the beginning and end of this period and decided to pursue only the defendant, Brit UV Limited (“Brit”), which had insured the claimant from 11 December 2003 to 10 December 2004.

The main issue in dispute was when the event causing damage had occurred.

Signs of subsidence were first reported to the Shop’s landlord in the summer of 2003 while the claimant was insured by Creechurch Dedicated Limited. The landlord’s agent, Farley, inspected the Shop and found cracks to the front of the building and movement to the public pavement in front of the shop. By November 2003 the situation had deteriorated significantly. The landlord’s insurer, AXA, was notified but the claimant did not notify its own insurer.

Over the next three years the subsidence continued to worsen and led to considerable water damage and dampness within the Shop. Various repairs were undertaken to the exterior by the landlord and to the interior by the claimant.

In August 2004, the claimant made a claim under the Brit insurance policy for the repairs to the Shop interior, business interruption loss and damaged stock. Brit denied liability due to a breach of a condition precedent by the claimant namely General Condition 5 which provided that the claimant must, “give immediate notice to the Insurers... on the happening of any injury or damage in consequence of which a claim is or may be made”.

The claimant argued that it did not have a duty to notify Brit until the subsidence damage became serious and had the potential to cause loss. It claimed that this did not occur until August 2004 and at this time Brit was informally notified.

### **Judge Mackie QC held that:**

1. The test for whether a claim ‘may be made’ was objective.
2. There was no evidence to support the claimant’s assertion that notice was given to Brit in August 2004.
3. In any event the claimant’s obligation to notify Brit arose in November 2003 as the seriousness of the damage was apparent at this time.

4. Brit was not liable under the insurance policy as the claimant had failed to comply with the condition precedent as to notice.

Judgment for the defendant.

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## Non-Disclosure, Brokers Duty of Care, Causation

### **Nicolas G Jones v (1) Environcom Limited (2) Environcom England Limited and Miles Smith Insurance Brokers [2010] EWHC 759 (Comm)**

Environcom Limited (“Environcom”) was in the business of recycling white goods, mainly refrigerators. Part of this recycling process involved the extraction of CFC chemicals which are used as a coolant in refrigerators, although more modern refrigerators use alternative chemicals to CFCs including pentane which is highly flammable.

The first stage of the refrigerator recycling process involves the removal of the compressors which contain the coolant chemicals. On occasions, when the nuts and bolts attaching the compressors to the bottom of the refrigerators are difficult to remove, they are cut off using plasma cutters. The plasma cutters heat metal to a high temperature, causing it to melt before a high velocity gas is applied which removes the melted part.

There was an inherent risk that when using plasma cutters, the sparks or molten metal could ignite pentane refrigerators.

In early 2004, Environcom approached Miles Smith Insurance Brokers (“MS”) to arrange insurance cover. During the initial discussions, Environcom’s business was described as being concerned with the recycling of ozone depleting substances and a plant for degassing CFCs. No mention was made of other chemical coolants nor the method or tools used to remove the compressors.

MS arranged coverage with Woodbrook which commenced on 24 May 2004. On the proposal form the business was described as, “Recycling White Goods” but no description of the recycling process was required. There was also a declaration which was signed by Environcom’s chairman which stated:

“I have not withheld any material facts. I understand that non-disclosure of a material fact will entitle the Underwriters to void the insurance.

(N.B A material fact is one likely to influence acceptance or assessment of this proposal by Underwriters)”

At Woodbrook’s request, a survey was carried out at Environcom’s premises.

In November 2004, Mr Hamilton (“Mr H”), an employee of Environcom, became responsible for the company’s insurance matters and approached MS for a summary of cover. Mr H also reported a break-in during which a generator and plasma cutter were stolen.

A few days later, MS wrote to Mr H to discuss the renewal of Environcom's insurance policy. The letter focused on the need to update the description of the business to take account of any acquisitions or developments and included the following provision:

"Material Facts

You are under a continuing obligation to notify Insurers of any material alterations to risk, for example:

- Change in business activities / acquisitions or disposals
- Additional premises / Risks / Insurable Items"

On 27 October 2005, a fire broke out on the recycling line causing the line to be shut down. Woodbrook instructed a specialist forensic fire investigation firm which found that the fire was caused by the ignition of pentane, although the source of ignition was unclear.

The insurance policy was renewed annually. Several site visits and risk assessments were carried out over the years. None of these noted the use of plasma cutters. In March 2006, Environcom produced a description of the recycling process in which, the use of plasma cutters was not mentioned. There were several fires at the recycling plant although Environcom only reported the most serious of these, neglecting to report any fires that it did not make a claim in respect of.

In May 2007 Woodbrook informed MS that it did not intend to renew Environcom's policy due to the experience of adverse claims. MS eventually persuaded Woodbrook to renew the policy; however, this was on more onerous terms than previously offered.

There was another small fire on 6 September 2007 which Environcom did not report. This was followed by a more serious fire on 16 September 2007 for which Environcom made a claim under the policy. Woodbrook declined the claim on the grounds of material non-disclosure relating to the use of plasma cutters and small fires which had occurred.

Woodbrook commenced proceeding seeking a declaration of non-liability. Environcom counterclaimed for an indemnity under the policy and joined MS as a third party on the ground that they had acted negligently in the brokering of the policy.

In November 2009 there was a mediation during which the dispute between Environcom and Woodbrook was settled.

**In the claim by Environcom against MS, Mr Justice David Steel held:**

1. There was no dispute as to the broker's duty, namely has a duty to:
  - advise clients of their duty to disclose all material circumstances;
  - explain the consequences for failing to disclose;
  - give an indication of what matters ought to be disclosed;
  - take reasonable care to elicit matters which the clients might not think are necessary to mention;
  - ensure that the policy is suitable for the clients' needs.

2. On the facts MS had breached its duty as it had failed ensure that Mr H understood the disclosure obligation and had provided no explanation of what might be material or the consequences of any failure to disclose.
  3. Where an incomplete explanation is given by a broker to its clients in relation to their obligations there is a higher standard of care on the broker when eliciting material information for disclosure.
  4. However, even if MS had complied with its obligations the use of plasma cutters would probably have not been disclosed by Environcom, although the small fires probably would have been disclosed.
  5. If full disclosure had been made, the chances of Environcom obtaining insurance cover, or adequate insurance cover, or accepting the terms of that insurance cover, were remote.
  6. Accordingly, despite the breach of duty by MS, Environcom's claim was dismissed as not being causative and the loss claimed was not of the kind or type which MS ought fairly to accept liability.
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## XOL Reinsurance, Follow Settlements, Burden of Proof

### **IRB Brasil Resseguros SA v CX Reinsurance Company Ltd** [2010] EWHC 974 (Comm)

The Commercial Court was asked to consider the appeal from the award ("Award") of an arbitration tribunal (the "Tribunal") in relation to six different individual cases concerning various reinsurance claims arising from the participation of IRB Brasil Resseguros SA ("IRB") in an excess of loss reinsurance programme. All of the underlying claims concerned class actions against US companies and related to US liability insurance.

The first two claims related to bodily injuries suffered due to silicon breast implants manufactured by AHS and 3M.

The third and fourth claims, against Baxter and Revlon, concerned the production of products derived from blood contaminated by HIV and Aids.

The fifth claim was against Corning, a company engaged in the use of asbestos.

The last claim, against Stauffer, a manufacturer of chemical and agricultural products involved an environmental pollution claim.

Each of these claims was settled by the insurer, CX Reinsurance Company Ltd (CX Re), by way of a compromise agreement.

The Tribunal considered whether the sums paid under the compromise agreement were recoverable by CX Re against IRB as reinsurer. The Tribunal found against IRB who appealed on the ground that the Tribunal had erred in law in their Award.

The four questions for the court to consider were:

1. What is the standard of proof necessary for a reinsured to prove their case under a “double proviso” follow settlements clause? Is it on the balance of probabilities or arguability? This question arose in respect of the claims against AHS, 3M, Baxter and Revlon.
2. When considering whether, under a follow settlements clause the proof of loss of a compromised settlement, is it appropriate to look at the underlying facts of the original claim or simply to look at the basis of the claim as compromised? This question arose in respect of the claims against AHS, 3M, Baxter and Revlon.
3. In relation to a reinsurance contract containing a follow settlements clause, what is it necessary to prove in relation to a “losses occurring during” clause? This question arose in relation to the claims against AHS, 3M, Corning and Stauffer.
4. What is the test for determining whether a loss ‘arises out of’ an event? This question only arose in relation to the claim against Corning.

The first two questions involved the policies’ “NOTICE OF LOSS CLAUSE”, effectively a “double proviso” follow settlements clause. The two provisos of the clause being:

- (i) that the insurer must settle losses within the terms and conditions of the underlying policies, and
- (ii) the settlement must be within the terms and conditions of the reinsurance.

The third question related to the policies’ “Period” clause, which stated:

“This reinsurance covers all losses as herein defined occurring during the period commencing with ..... and ending with ....., both days inclusive...”

The clause relevant to the fourth question was the “EACH AND EVERY LOSS” clause, which stated:

“... The term “each and every loss” shall be understood to mean each and every loss and/or occurrence and/or catastrophe and/or disaster and/or calamity and/or series of losses... arising out of one event.”

**Mr Justice Burton held that:**

1. Compliance with both provisos in the “double proviso” follow settlements clause had to be proven on a balance of probabilities. Although the Tribunal may have expressed itself erroneously in the award, it had in fact applied the correct burden of proof.
2. The evidence required to discharge the burden of proof varies from case to case. Where there is a compromise settlement, the relevant facts are those on which the compromise was reached, not the facts of the loss as it happened.
3. It was not necessary for the Tribunal to spell out the Period clause in their award. Under US law the “triple trigger theory”, by which once a defect has been identified liability can be found on one of three

different occasions, brings into play different periods of cover. Under this theory, it was possible that the insurers could have been found liable for 100% of the loss. The insurers had reached a settlement compromise by calculating what percentage of losses could be attributed to their period of cover. This was a mere mathematical calculation but there was nothing to stop a court or arbitrator from relying on such to reach a conclusion. The Tribunal had reached a reasonable and business decision and had made no error of law.

4. To determine whether a loss 'arises out of' an event it is necessary to consider the contractual context, including the type of peril insured against and the loss in question. The Tribunal was right to conclude that the single event was the decision of the company, Corning, to engage in business involving the use of asbestos.

The Tribunal had not erred in law in reaching their conclusions.

Appeal dismissed.

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## Business Interruption, Causation, 'But For' Test

**Orient-Express Hotels Limited v Assicurazioni General S.p.A (UK Branch) Trading as Generali Global Risk**  
[2010] EWHC 1186 (Comm)

The claimant, Orient- Express Hotels Limited ("OEH") owned a luxury hotel in New Orleans (the "Hotel"), which suffered significant wind and water damage due to Hurricane Katrina and Hurricane Rita in 2005.

The Hotel was forced to close during September and October 2005 and re-opened, although not fully repaired, on 1 November 2005. The area of New Orleans surrounding the Hotel was also devastated. A mandatory evacuation of the city was ordered on 28 August 2005 and the city was not re-opened until the end of September 2005.

OEH claimed under its combined property damage and business interruption loss policy (the "Policy") with the defendant ("Generali"). There followed a dispute as to OEH's right to indemnity for the business interruption loss under the Policy which was referred to arbitration.

The arbitration tribunal (the "Tribunal") applied the "but for" test of causation and held that under the Policy's Insuring Clause OEH could only recover in respect of business interruption loss which it could show would not have arisen had the damage to the Hotel not occurred. This involved a hypothetical analysis of putting OEH in the position of "an undamaged hotel in an otherwise damaged city".

The Tribunal held that even if the damage to the Hotel had not occurred, the Hotel would have still suffered the same loss, as the city was closed and no one would have been able to visit it. It therefore followed that OEH was not entitled to an indemnity from Generali for business interruption loss under the Policy's Insuring Clause.

OEH did recover an indemnity under the Policy's Prevention of Access ("POA") and Loss of Attraction ("LOA") clauses but this was for a significantly lower amount than would have been recovered under the Insuring Clause.

OEH appealed against the decision of the Tribunal under section 69 of the Arbitration Act 1996 on two questions of law:

1. whether the Policy provided cover in respect of loss which was concurrently caused by both the physical damage to the property and the loss of attraction of the surrounding area; and
2. whether the same event(s), which gave rise to the business interruption loss, were also capable of giving rise to 'special circumstances', allowing an adjustment of the business interruption loss within the scope of the Trends clause?

The Policy contained the following clauses:

The Insuring Clause:

"... The Insurers... agree... to indemnify the Insured...

b) under the Business Interruption Section against loss due to interruption or interference with the Business directly arising from Damage..."

Damage was defined as "direct physical loss destruction or damage" and the cover for business interruption loss was defined as "loss due to interruption or interference with the business directly arising from the Damage".

The Trends Clause:

"... Adjustments shall be made as necessary to provide for the trend of the Business and for variations in or special circumstances affecting the Business either before or after the Damage or which would have affected the Business had the Damage not occurred so that the figures thus adjusted shall represent... the results which but for the Damage would have been obtained during the relevant period after the Damage."

**Justice Hamblen held that:**

1. The Tribunal had not excluded the recovery of losses caused concurrently by damage to the Hotel and damage to the vicinity. It had only excluded losses which would have been suffered despite the damage to the Hotel as such losses should not be regarded as caused by the property damage.
2. The Tribunal was right to apply the "but for" test for causation in the way that it did. This is although OEH had not raised this issue during the arbitration which made it difficult for the court to determine whether the Tribunal had erred in law.
3. The same event, which gave rise to the business interruption loss, was also capable of giving rise to "special circumstances", allowing an adjustment of the business interruption loss within the scope of



the Trends clause. However, the Tribunal's interpretation and application of the Trends clause was correct. It was not necessary "to go behind the Damage and consider whether the event which caused the Damage also caused damage to other property in the City."

Appeal dismissed.

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## Third Parties (Rights Against Insurers) Act 1930, Breach of Condition By Insured A Bar To Third Party Claims

**Clare Horwood & Others v Land of Leather Limited (in Administration), Zurich Insurance PLC & Others**  
[2010] EWHC 546 (Comm)

In September 2007, Land of Leather Limited ("LOLL") received a number of complaints from customers who had suffered skin allergies from sofas which had been supplied to LOLL by Linkwise. LOLL sought compensation from Linkwise and in November 2007 the two companies reached an oral agreement (the "November Agreement"). The terms of the agreement stated that Linkwise would give LOLL USD900,000 in credit against future orders.

LOLL sent its product liability insurer, Zurich Insurance PLC ("Zurich"), a copy of an invoice prepared for Linkwise outlining the terms of their agreement. LOLL stated that it would be made clear to Linkwise that any payment did not include compensation in respect of the impending personal injury claims. Zurich confirmed that the wording in the invoice was fine.

LOLL sent the invoice via email to Linkwise outlining the terms of their agreement and stating that the invoice was for "Immediate settlement". Linkwise replied summarising the key points of the agreement as follows:

"The payment of \$900,000 was in full and final settlement of all matters relating to alleged allergic furniture problems.

Linkwise to issue a credit note for \$900,000, payment to be made over 6 months at the rate of \$150,000 per month starting December.

Land of Leather to guarantee \$20,000,000 of purchases over the 12 months from 1 Dec 2007."

LOLL replied to this stating that the terms of the settlement were on the invoice and that LOLL did not want to guarantee the purchases from Linkwise.

On 16 November 2007, Linkwise issued a credit note to LOLL. However, credit was refused when LOLL made its next payment for sofas supplied by Linkwise. This refusal of credit occurred at a difficult time for LOLL which had suffered damage to its reputation and a 50% drop in its share price. The need for the USD900,000 became more pressing.

In February 2008, LOLL made demands on Linkwise to honour the November Agreement but Linkwise wanted to renegotiate. A second agreement was reached (the “February Agreement”) which included the following provision:

“Land of Leather also confirm they will make no further claim on Linkwise in respect of alleged allergic reactions to their products...”

LOLL went into administration which led its customers to bring their personal injury action directly against Zurich under the Third Parties (Rights Against Insurers) Act 1930.

Zurich argued that it was not liable to indemnify LOLL, and was therefore not liable to the claimants, as the general words of release in the February Agreement were in breach of General Condition 3 of the policy.

General Condition 3 stated that:

“The Insured shall not, except at his own cost, take any steps to compromise or settle any claim...”

Zurich further argued that the February agreement was in breach of an implied term of the policy to act reasonably and in good faith with due regard to Zurich’s interests.

The customers counter-argued that:

1. The words “no further claim” in the February Agreement had to be read in their context as “no further claim of the type identified in the invoice” and as Zurich had agreed to the wording of the invoice there had been no breach of General Condition 3 or breach of an implied term of the policy.
2. The prohibition on settling claims under General Condition 3 of the policy only applied to claims against the insured and not claims by the insured.
3. There was no consideration given for the February Agreement which meant that it was not a valid contract.

**Mr. Justice Teare held that:**

1. The February Agreement was a complete statement of the parties’ respective rights and should not be read with reference to the invoice. Likewise a reasonable person would not think that the February Agreement should be interpreted as referring to the invoice.
2. The prohibition under General Condition 3 of the policy relates to both claims against and by the insured.
3. The February Agreement did provide a commercial benefit to LOLL in that prior to this agreement it did not know when it would receive payment. This was satisfactory consideration and therefore the February Agreement was a valid contract.

The personal injury claim by the customers was dismissed.

## Double Insurance, Damage to Property Between Exchange and Completion

**The National Farmers Union Mutual Insurance Society Limited v HSBC Insurance (UK) Limited** [2010] EWHC 773 (Comm)

This case concerned a property (the “Old Hall”), which was sold for £1.81 million. The seller and the buyer exchanged written contracts on 10 October 2007 and completion was scheduled for 7 November 2007. A clause of the sale contract provided that the risk of damage to or destruction of the Old Hall passed to the buyer on exchange.

The seller had an insurance policy with HSBC Insurance (UK) Limited (“HSBC”) and before exchange the buyer took out a policy with the National Farmers Union Mutual Insurance Society Limited (“NFU”).

There was a fire at the Old Hall on 27 October 2007, between the dates of exchange and completion, where under the terms of the sale contract the Old Hall was at the risk of the buyer.

The sale was finally completed on 21 March 2008. The buyer made a claim under its policy with NFU. NFU sought a contribution from HSBC on the basis that at the time of the fire the buyer was covered by both the NFU and HSBC policies and therefore there was an issue of double insurance. HSBC denied liability on the basis that on the proper construction of their policy the buyer was not covered by HSBC at all.

The terms of the HSBC policy stated:

“WHAT IS COVERED

The buildings for physical loss or physical damage... the insurance also covers ... anyone buying your home...until the sale is completed.”

“WHAT IS NOT COVERED

We will not pay... if the buildings are insured under any other insurance.”

The NFU policy contained the following clause:

“Other insurance

If when you claim there is other insurance covering the same accident... we will only pay our share.”

The trial focused on three preliminary issues, namely:

1. Did the HSBC policy provide cover to the buyer for damage due to fire?
2. Did the NFU policy contain only a general pro rata clause where there is other insurance covering the same damage?
3. Was the cover for buyers in the HSBC policy limited to assisting in the event that the buyer did not complete?



Mr Gavin Kealey QC, sitting as a deputy High Court Judge, held that on the proper construction of the two policies the HSBC policy did not extend to cover the buyer pending completion of the sale.

The Old Hall was only covered by the NFU policy and therefore no question of double insurance arose.

HSBC were not liable to make a contribution.

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## Pure Economic Loss, Beneficial (Not Legal) Owner

### **Colour Quest Ltd v Total Downstream UK Plc [2010] EWCA Civ 180**

On 11 December 2005, there was a huge explosion at the Buncefield Oil Storage Terminal caused by the negligent overfilling of a fuel storage tank which led to the creation of a hydrocarbon vapour cloud which ignited.

Part of the Buncefield site was occupied by Hertfordshire Oil Storage Limited (“HOSL”), a joint venture company owned 60% by Total Downstream UK Plc (“Total”) and 40% by Chevron Ltd (“Chevron”).

Substantial claims by a number of claimants, including Shell UK Limited (“Shell”), were brought against HOSL and Total. Total, in turn, brought Part 20 proceedings against Chevron.

In October 2008, there was a trial of preliminary issues in the Commercial Court, the main focus of which was the dispute between Total and Chevron as to who was the relevant defendant liable for the negligence and the division between the two companies under the Part 20 proceedings. Justice David Steel held, amongst other things, that:

1. Total and not HOSL was vicariously liable for the negligence.
2. Total was not entitled to a contractual indemnity against HOSL or Chevron as the relevant agreements did not provide for Total to be indemnified in respect of its own negligence.
3. Chevron was precluded from claiming for property damage and consequential economic loss against Total under the terms of the agreements between the two.
4. Shell, who had suffered damage to neighbouring tanks and pipelines as a result of the explosion, could not claim damages for consequential economic loss. This was because Shell was deemed not to have the necessary legal ownership or right of possession of the pipeline, which was held, for its benefit, on trust in a vehicle company.

An appeal was brought by Total, Chevron and Shell in relation to the following issues.

1. Total appealed on the applicability of the indemnity provisions arguing that it did have a right to be indemnified even where the loss was caused by its own negligence.

2. Chevron cross-appealed on Total's role arguing that at the time of the explosion Total was not a "participant" within the meaning of the relevant agreements and therefore Chevron was not precluded from making a claim against Total and Total was excluded from relying on any indemnity between the parties.
3. Shell appealed on the ground that while the right to sue for negligent damage to property was confined to the person who had legal ownership or a possessory title to the property, this did not exclude the equitable owner if they joined the legal owner in the proceedings as Shell had.

**Held:**

Lord Justice Walker, Lord Justice Longmore and Lord Justice Richards in the Court of Appeal held that Total was not entitled to an indemnity under any of the provisions on which it sought to rely, therefore Total's appeal failed.

Total was a "participant" within the meaning of the relevant agreements and therefore Chevron's appeal also failed.

However, Shell's appeal was successful as it was held that a duty of care was owed to the beneficial owner just as much as it was owed to the legal owner. In joining the legal owner in the proceedings Shell could recover as beneficial owner for economic losses regardless of whether it was in possession of the property.

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## Avoidance, Misrepresentation

### **Mitchell v (1) Hiscox Underwriting Limited (2) Syndicate 33 at Lloyd's, managed by Hiscox Syndicates Limited [2010] CSIH 18**

The defenders ("Hiscox") appealed against the decisions of the Sheriff and the Sheriff Principal that they were not entitled to avoid a policy with the Pursuer ("Mitchell") on the basis of misrepresentation.

Mitchell had entered into a contract of insurance with Hiscox in respect of a motor boat called the "Dot Dash". As part of the insurance application process Mitchell made a number of representations which were later proven to be false, namely:

1. That the purchase price of the boat was £25,000. It was in fact less than this.
2. That he had a no claims bonus of 5%. Mitchell had not actually had his own insurance policy prior to this and had only been covered as a driver for the boat for third party liabilities on a policy in the name of his then girlfriend.

In July 1999, the Dot Dash was stolen from the marina where it was moored. Hiscox refused to make payment under the insurance policy.



The Sheriff held that although the misrepresentations of the purchase price and the no claims bonus were both material, they had not induced Hiscox to enter into the contract of insurance.

The Sheriff did find, however, that the misrepresentation about the no claims bonus had induced Hiscox to adjust the premium to be paid.

Despite this it was held that Hiscox were not entitled to avoid the policy.

Hiscox appealed to the Sheriff Principal who refused their appeal.

Hiscox appealed to the Inner House of the Court of Session on the basis that there was a contradiction in the finding that the misrepresentation of the no claims bonus had induced Hiscox to adjust the premium to be paid but had not induced them to enter into the contract of insurance.

Hiscox submitted that the correct test was that a policy can be avoided if a misrepresentation induced the insurer to enter into the policy on the terms which it did, in particular as to the premium.

The Court of Session opinion, allowing the appeal, was delivered by Lord Osborne who stated that:

1. The appropriate test was whether the misrepresentation led to different terms being offered by the insurer. If so, that was sufficient to avoid the policy.
2. The Sheriff had misdirected herself in law and therefore her decision was flawed.
3. The contract of insurance was induced in the relevant sense by the misrepresentation about the no claims discount.

Hiscox were entitled to avoid the policy for misrepresentation.

## Guest article

We are delighted to have a guest article in this edition from Euros Jones, an Associate in our London based Regulatory Team. Euros' article takes a look at The Bribery Act 2010 and some of the implications for company directors, officers and their insurers.

### **The Bribery Act 2010: are you ready for it?**

#### **Introduction**

The UK's most recent piece of anti corruption legislation, The Bribery Act 2010 ("the Act") received its' royal assent in April 2010. The Act signifies a move to consolidate the law on corruption and is a very wide, tough piece of legislation designed to facilitate the prosecution of corrupt practices. The previous Government's stated intention, with cross party support, of combating corrupt practices moved a step closer with it.

Whilst the current Government has recently delayed the coming into force of the Act until April 2011 so as to allow for a consultation process to be held with the intention of assisting companies to understand what action should be taken to ensure compliance with this new law, it is important that action should be taken now by companies and senior company officers to begin the process of compliance.

#### **Recent enforcement action**

This stated aim by Government is being supported by the recent increase in enforcement action by enforcing bodies. It is clear that the Serious Fraud Office ("SFO") is looking to enforce more as can be seen from recent enforcement action it has taken. For example, take the prosecution of Mabey and Johnson in 2009. That company agreed to pay £5.6m following a plea bargain agreement with the SFO which included the requirement to pay fines and reparations.

Another example is the civil recovery order obtained by the SFO in 2008 against Balfour Beatty Plc under the Proceeds of Crime Act 2002. In those proceedings, Balfour Beatty Plc agreed to a settlement payment of £2.5m together with a contribution towards costs and the agreement to the introduction of certain compliance systems that were to be externally monitored.

Richard Alderman, Director of the SFO commenting on the Balfour Beatty Plc case at the time said:

"This is a highly significant development in our efforts to reform British corporate behaviour. We now have a range of enforcement tools at our disposal, and a major factor in determining which of those tools is deployed will be the responsibility demonstrated by the company concerned."

The Financial Services Authority ("FSA") is also looking to crack down on corrupt practises. Traditionally, the FSA has looked to enforce against individuals accused of insider dealing and market abuse. However, in 2009 the FSA took the step of taking enforcement action against Aon Limited ("Aon"), imposing a fine of £5.25m on it "for failing to take reasonable care to establish and maintain effective systems and controls to counter the risks of bribery and corruption associated with making payments to overseas firms and individuals"

Margaret Cole, the FSA's director of enforcement, said:



"This is the largest financial crime related fine imposed by the FSA to date. It sends a clear message to the UK financial services industry that it is completely unacceptable for firms to conduct business overseas without having in place appropriate anti-bribery and corruption systems and controls."

"The involvement of UK financial institutions in corrupt or potentially corrupt practices overseas undermines the integrity of the UK financial services sector. The FSA has an important role to play in the steps being taken by the UK to combat overseas bribery and corruption. We have worked closely with other law enforcement agencies in this case and will continue to take robust action focused on firms' systems and controls in this area."

"Aon assisted the FSA throughout its investigation and secured a 30% reduction on the financial penalty under the FSA's settlement discount scheme as a result. The FSA said that "the pro-active determination of Aon Ltd's current senior management to identify past issues and improve the firm's systems and controls in this area is a model of best practice that other firms may wish to adopt".

The above, together with additional recruitment of staff into the FSA's enforcement division demonstrates that this regulator is taking steps to strengthen its role in stamping out corrupt practices.

In seeking to do so, the Act is the newest weapon in these enforcement bodies' armouries.

### **Is it a simplified law?**

Until recently the substantive law governing bribery in the UK was, according to the Organisation for Economic Co-Operation and Development ("OECD"), full of "complexity and uncertainty".

The Act is designed to simplify matters. Both companies and company officers need to be aware of its existence and to take adequate steps to ensure that there is compliance with its provisions as failure to do so could lead to a criminal prosecution.

The Act has extra jurisdiction application and is more far reaching than the US' Foreign Corrupt Practices Act 1977 in that it will apply to both public and private sector corruption. Interestingly, unlike the US legislation, facilitation payments are banned and there is a potential grey area of what is acceptable as corporate hospitality. The Act also introduces a number of new offences that have application to all areas of business.

### **The offences**

The Act's primary offences are those of bribing another person (Section 1) and of being bribed (Section 2). The Act also introduces an offence of bribing a foreign public official (Section 6) and a new corporate offence of failing to prevent an associated person from committing bribery (Section 7).

### **The basic offences**

An offence is committed under Section 1 if a person offers, promises or provides a financial or other advantage to another where as a result, that other person performs a function improperly.

An offence is committed under Section 2 if a person requests, agrees to receive or accepts a financial or other advantage from another where as a result that person performs a function improperly.



These two offences have an extra jurisdictional application and the provisions of Section 3, 4 and 5 assist in the interpretation of these offences. A person improperly performs a function if he/she breaches an expectation that the function would be performed impartially, in good faith or as a result of a position of trust.

However, the two offences that have caused the most interest are those contained in Section 6 and Section 7 of the Act.

### **The offence of bribing a foreign public official**

Section 6 creates an offence of bribing a foreign public official. Such an offence is committed if a person pays or offers an advantage to a foreign public official with the intention of influencing that official so as to obtain or retain business as a result and when that official is not allowed or required to be influenced by that payment or advantage under local law.

Companies therefore have to be careful when dealing with foreign public officials, not least as facilitation payments are banned under the Act. Whilst it is acknowledged that there may be concerns with the competitiveness of companies in the global market who are linked with our jurisdiction as a result of this provision in the Act, this clear approach is intended to demonstrate that there will be zero tolerance of bribery moving forward.

### **The offence of failing to prevent bribery**

Section 7 creates the new corporate offence of failing to prevent bribery. Such an offence is committed if a person associated with a company, performs a service on behalf of the company and that person bribes another with the intention of obtaining or retaining business or an advantage in the conduct of that company's business. The offence is made out if the company is then unable to make out the defence of having in place "adequate procedures" which are designed to prevent associated persons from engaging in bribery. An associated person includes an employee, agent or subsidiary (See Section 8). This list is by no means exhaustive.

A company linked to the UK through its' business activities can therefore be prosecuted here for the acts of its associated persons abroad. This has serious implications for that company and its officers, not least as the maximum sentence for a company convicted of this offence is an unlimited fine.

### **What are adequate procedures?**

It is therefore important to ensure that a company with business links with the UK has in place adequate procedures to ensure that bribery does not take place through the company's acts or that of its associates.

Unfortunately, the Act does not define what "adequate procedures" are and the position is not made any easier by the fact that the Government has not published its Guidance on the matter. This is a concern given that the Act is to come into force in April 2011 and that companies will be expected to have these procedures in place before then. The Government's recent decision to postpone the implementation of the Act until April 2011 should assist companies to some degree. This decision was made to allow for a consultation to be launched in September 2010 which will look at what companies need to do to ensure that they comply with the law. A statement on the Ministry of Justice's website states:

"In September the Government will launch a short consultation exercise on the guidance about procedures which commercial organisations can put in place to prevent bribery on their behalf."

Whilst a number of companies will have procedures in place to comply with the Foreign Corrupt Practices Act 1977, those procedures will have to be reviewed in light of this legislation and other companies will have to start from a lower base.

### **How detailed will the Guidance be?**

The Guidance is unlikely to be detailed, focussing more on a generic set of principles for companies to follow. It will not be prescriptive in nature, and each company will have to adapt its' own procedures to its' own specific business and associated risks.

### **When will the Guidance be published?**

"This will be published early in the New Year to allow businesses an adequate familiarisation period before the Act commences." – Ministry of Justice

### **What can companies therefore do in the interim to ensure they are compliant with the legislation?**

As the publication of the Guidance in the New Year will not allow for much time to implement procedures before the Act comes into force, there are other sources available from which indicators can be taken of what could be adequate procedures within the context of the Act. Examples include:

The Serious Fraud Office's guidance on self reporting of corrupt practices;

The US sentencing guidelines for breaches of the Foreign Corrupt Practices Act 1977; and

The Financial Services Authority's report on "Anti bribery and corruption in corporate insurance broking" issued in May 2010.

This latter report is a good indicator of what procedures should be adopted in the insurance broking context and concluded "that many firms are not currently in a position to demonstrate adequate procedures to prevent bribery".

### **Immediate action to demonstrate adequate procedures**

What is clear from the above indicators is that there should be acceptance and proactive development of anti bribery procedures within companies and those procedures should be implemented from Board level downwards.

The Board should develop an anti bribery culture, and have a stated company ethics policy.

Directors and senior managers should take a lead on implementing and reviewing that policy and the company should conduct a risk and vulnerability assessment of the likely difficulties to be encountered in its' business line so as to identify and manage those risks and prevent bribery.

Other suggested actions include the implementation of financial and management controls and procedures to limit the possibility of bribery together with the publication of clear policies on topics such as gifts and corporate hospitality.

Other procedures include staff training on anti corruption policies and procedures, implementation of whistle blowing procedures and the vetting of representatives and agents, particularly those operating in different jurisdictions.



If not already doing so, companies need to start work on these issues as soon as possible and seek professional assistance in doing so.

### **What of senior officers?**

Company senior officers must be active in ensuring that the company is complying with the Act. This is important because if it is shown that an offence under Section 1, 2 or 6 of the Act was committed with the consent or connivance of a senior officer or a person purporting to act in such capacity then that senior officer may also be guilty of an offence (Section 14). The importance of this is highlighted by the fact that the maximum sentence for an individual convicted of an offence in such circumstances could be a period of imprisonment of 10 years, putting to one side ancillary action following conviction, such as the imposition of confiscation and directors disqualification orders.

A senior officer is defined as a director, manager, secretary or any other similar officer of a body corporate.

### **Conclusion**

In summary therefore, not only does the Act simplify the law but it also has wide reaching effect. It will impact on all areas of business and both companies and corporate officers will have to be alive to its provisions and ensure that safeguards are implemented to ensure compliance by the company and its' associates. Only then will potential criminal sanction be avoided. Preventative action must be taken now as there will be little time to do so between the publication of the Government's Guidance in the New Year and the Act coming into force in April 2011.

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## Catch up

The London Market Team would like to thank those who attended our 'Update on Leading (Re)insurance Cases' seminar at Lloyd's on 24 March 2010. If you were unable to attend and would like a copy of our seminar handout or would like to be added to our mailing list for future events please contact Sarah Oldham at [sarah.oldham@weightmans.com](mailto:sarah.oldham@weightmans.com). Our next seminar at Lloyd's is likely to be in the autumn.

You will be able to catch up with members of the London Market Team at the following forthcoming events:

- Monte Carlo Rendez-Vous, 12-15 September 2010
- 'Deepwater Horizon Catastrophe', BILA lecture at Lloyd's, 17 September 2010
- AIRROC, New Jersey, 18-20 October 2010
- IACP/XSLCA European Conference, France, 17-18 November 2010



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