In brief

Winterthur & TAG claims – following a sample audit of 3,000 files, Winterthur is likely to press ahead with more than 65,000 cases against law firms involved with The Accident Group (TAG). The insurers allege that firms handling claims under the TAG scheme were negligent in failing to vet and monitor cases properly. The firms’ assertion that the files were privileged as against Winterthur failed in April last year (Winterthur Swiss Insurance Co v AG (Manchester) Ltd).

Stress claims – counselling services are not a panacea by which employers can discharge their duty of care in all cases. The claimant’s refusal to use internal counselling services could not be criticised in circumstances where the only way of dealing with her problems
would have been for management to reduce her workload. The claim was upheld (*Intel Incorporation (UK) Ltd v Daw* CA 7 February 2007).

**Effect of Insurance Directive** – the Commercial Court has held that the First Non-Life Insurance Directive was intended to facilitate the development of an open market in the provision of direct (non-life) insurance and was not designed to confer any individual rights. Even if it had been designed to confer individual rights, it would only protect individuals to whom insurers supplied services. Lloyds names could not be equated with insureds in this context (*Poole v HM Treasury*).

**VAT on outsourced services** – PricewaterhouseCoopers’ report following their investigation into the economic effects of the VAT exemption for financial and insurance services recommends extension of the scope of the VAT exemption for insurance-related services. The report has been welcomed by insurers who are anxious to prevent full implementation of the narrow interpretation of the insurance exemption to the 6th VAT Directive favoured by the ECJ in *Arthur Andersen & Co Accountants* (case C-472/03).

**Pre-action admissions** – with effect from 6 April 2007, pre-action admissions will be treated in the same way as admissions made after proceedings begin. This means that a defendant making an admission of liability after it receives a letter of claim will not be able to withdraw the admission without obtaining the permission of the court. This amendment to CPR 14 reverses the effect of the Court of Appeal decision in *Sowerby v Charlton*.

**Insurance**

*Kyle Bay Ltd v Various underwriters* – effect of mistake of law

CA 7 February 2007

An agreement by underwriters to settle an insurance claim on the basis that the insured’s business interruption policy was a gross profits policy subject to the application of average, when in law the policy was declaration-linked and not subject to the application of average, was not void for mutual mistake, as the mistake in question did not render what the parties believed to be the subject matter of the agreement "essentially and radically different" from what it was.

**Comment:** this case illustrates how difficult it is to unscramble a settlement agreement even when both parties have proceeded under a financially significant mistake of law. Here both sides mistakenly thought that the policy was on a gross profits basis rather than a declaration-linked basis, with the consequence that the claimant received about £200,000 from the defendant insurers instead of about £300,000. But because the parties had understood all the other salient points concerning the contract such as the facts giving rise to the claim (a fire at a nightclub), the period of business interruption caused by the fire, the estimated level of gross profits and everything else about the nature of the cover, the mistake was not so radical as to entitle the court to intervene.
Professional indemnity

Zurich Professional Ltd v Karim – condoning dishonesty

Irwin J 15 December 2006

The claimant insurers sought declarations that the claims made under the defendant solicitors’ professional indemnity policy arose "from dishonest or fraudulent acts or omissions committed or condoned by the insured” so that they were not obliged to indemnify the insured. The central issue was whether the son and daughter insureds had condoned the dishonest acts of their mother who also practised from the family firm. The judge concluded that they had condoned the dishonest handling of money and breaches of the Solicitors’ Practice Rules. They must have known that the firm could not sustain the drawings made on it, they knew that funds were being mixed and had divested themselves of any responsibility of how the firm was being run. This was dishonest behaviour and the insurers were not required to pay out under the policy.

Comment: there has been a continuing debate as to whether the civil test of dishonesty requires there to have been subjective dishonesty so that the wrongdoer appreciated that what he was doing was dishonest. The House of Lords confused the issue with conflicting judgments in Twinsectra v Yardley but were taken to have held that the test was subjective. In Barlow Clowes International Ltd v Eurotrust International Inc the Privy Council held that the test did not require subjective dishonesty. The Court of Appeal in Abou-Ramah v Abacha held that the Barlow Clowes approach was right. The judge in the present case also followed the Barlow Clowes approach - whether the individual was aware that his conduct fell below the objective standard is not part of the test. For a more detailed discussion of the test, see Angus Turner’s article on dishonest assistance in the forthcoming Spring edition of Covemote.

Limitation

Cattley v Pollard - dishonest assistance claims

Richard Sheldon QC 7 December 2006

The normal primary limitation period of six years applies to claims against a dishonest accessory to a fraudulent breach of trust where the defendant is a stranger who dishonestly participates in the breach of trust and is unaffected by a pre-existing trust relationship. The exception to the normal period of limitation for actions in respect of trust property in s21(1)(a) Limitation Act 1980 only applies to a breach of a trust by an express trustee.

The first defendant, Nigel Pollard, was a solicitor who dealt with the administration of an estate. The second defendant was his wife. Between 1987 and 1996, Mr Pollard misappropriated about £317,000 of estate assets. The trustees brought proceedings against the defendants for this sum and entered judgment against Mr Pollard. They subsequently brought proceedings against Mrs Pollard for damages or equitable compensation arising from her knowingly and dishonestly assisting her husband in the breaches of trust.

The court rejected Mrs Pollard’s defence that the claim against her was time-barred. Whilst the general six year period for fraud applied to the claim against her, s21(3) Limitation Act applied to postpone the running of the primary period of limitation in relation to beneficiaries.
with future interests in the estate and an action by a beneficiary under that section included, at least by analogy, actions brought exclusively on their behalf by trustees who had no personal interest in the outcome. Additionally, s32 also applied to postpone the running of the primary period of limitation until after the date on which the trustees could with reasonable diligence have discovered Mrs Pollard’s dishonest participation in the fraud.

**When can a defendant rely on a laches defence?**

Laches enables the court to refuse to grant equitable relief (eg for specific performance of a contract or an injunction) where delay by the claimant makes it unfair to grant the relief sought. It has a similar effect to a limitation defence so that if the court is satisfied that there has been an unreasonable delay in enforcing an equitable right, it may strike out the claim. Recently in *P&O Nedlloyd BV v Arab Metals Co* (CA 13 December 2006), the claimants sought specific performance of a contract. The Court of Appeal held that the six year limitation period applying to contracts does not apply by analogy to claims for specific performance, although it does to claims for breach of fiduciary duty where claims are also made for breach of contract and damages sought for negligence (*Companhia de Seguros Imperio v Heath*). Where the limitation period does not apply by analogy, defendants may still be able to rely upon a laches defence.

The court went on to consider whether, had the limitation period applied by analogy, it would have operated to exclude the doctrine of laches. They concluded that it would not. Where there is mere delay and the defendant has not altered his position in the meantime, the claim would not be struck out before the end of the limitation period. But where there is unjustified delay coupled with an adverse effect on the defendant or a third party, there is no reason why in principle the court should not be able to strike out the claim for equitable relief on the ground of laches before the limitation period expires. In the light of this conclusion, claimants seeking equitable relief should not assume that they can relax during the limitation period but should be prompt in applying to the court. (See under Jurisdiction below for an example of a refusal to grant equitable relief on the ground of delay.)

**Damages**

*Aerospace Publishing Ltd v Thames Water Utilities Ltd* - reinstatement or diminution in value

CA 11 January 2007

Where a claim is made in respect of a chattel which has been destroyed negligently by a third party, the claimant will only be entitled to the replacement value where it is reasonable to replace the chattel and the cost of replacement is reasonable. In practice, the cost of reinstatement will only be awarded where the claimant intends to reinstate the chattel. The fact that the value of the chattel to its owner is greater than its market value may point to the cost of reinstatement as the proper measure of loss. Where it is appropriate to award damages on a diminution of value basis, the claimant may also be able to claim for future loss of profits.

Thames Water admitted liability for a burst water pipe which flooded the claimant’s premises and destroyed most of its archive of photographs, artwork and reference material relating to aviation. The claimant said that it intended to reinstate the archives and that, given that the
market or resale value was unlikely to be adequate for that purpose, it should be awarded a sum representing the cost of replacement. Thames Water argued unsuccessfuully that the claimant had no intention of replacing the archive and in any event that it would be unreasonable to do so. The claimant recovered more than £2.5 million on a reinstatement basis.

Comment: the claimant also sought to claim for the diversion of staff time, and the retention of two ex-employees on a freelance basis, as a consequence of the flooding. This issue arose last year in R & V Versicherung AG v Risk Insurance and Reinsurance Solutions SA, a case concerning a conspiracy to defraud the claimant company (see February 2006 Insurance Update). Gloster J held that, as a matter of principle, the costs of wasted staff time spent on the investigation and/or mitigation of a tort should be recoverable from the defendant, notwithstanding that no additional expenditure loss, or loss of revenue or profit could be shown. In the present case, to the extent that she disagreed with the decision in Admiral Management Services Ltd v Para-Protect Europe Ltd, the Court of Appeal approved her analysis.

They went further to assist claimants by concluding that where the claimant has adequately established the diversion of the time of a significant number of its employees, and where there can be no sensible challenge to the conclusion that the business was disrupted, the court will be entitled to infer that the employees have been diverted from revenue-generating activities which would have generated revenue for the claimant in an amount at least equal to the costs of employing them during that time. In such circumstances, the burden of disproving this inference will in practice rest upon the defendant. An award of £31,520, significantly reduced from the sum originally claimed, was upheld by the Court of Appeal. Where there has been substantial staff disruption following tortious damage, insurers should expect awards of damages in such cases to increase and reserves should be revisited to take this possibility into account.

Jurisdiction

Markel International Co Ltd v Craft – effect of arbitration clause
Morison J 12 December 2006
Mr Craft died after abandoning ship on his return from a drilling rig to the port of Tunis. A Tunisian statute gave his family a right to claim damages directly from the shipowners’ insurers, Markel. The family began proceedings in Tunisia and Markel applied for an anti-suit injunction to restrain them on the ground that the insurance policy contained an exclusive arbitration clause.

The court refused to grant the injunction. Where an injured party has a right conferred by a foreign statute to bring a claim directly against the insurers of the tortfeasor who has injured him, he is not bound by an arbitration clause in the tortfeasor’s contract of insurance and can bring proceedings in the foreign country. It is only where the claimant is seeking to enforce his rights in accordance with the terms of the insurance contract that he is bound by all its terms, including any arbitration clause (Through Transport Mutual Insurance Association v New India Assurance Association Co Ltd).
Comment: the judge noted that even had Markel been legally entitled to the injunction, he would not have granted it in the exercise of his discretion because of Markel’s delay in applying for the relief. The “arbitration point” was only taken after the Tunisian proceedings had been running for over a year. The application should have been made promptly and the judge was not impressed with the argument that there has been greater delay in other cases. See under Laches above for a discussion of the circumstances in which the courts will deny an applicant equitable relief on the ground of delay.

Abolition of payments into court
The existing Part 36 of the Civil Procedure Rules (CPR) will be replaced on 6 April 2007 with a completely new CPR 36 setting out the rules for making offers of settlement. The principle change, and one which was surprisingly not foreshadowed in the consultation paper on Part 36, is the abolition of payments into court.

Under the present Part 36, a defendant who wishes to settle a money claim must make a payment into court. During the past few years, this rule has been subject to exceptions devised by initially by NHS Trusts and subsequently extended with the approval of the courts with the effect that any defendant who is deemed to be “good for the money” can make a Part 36 offer instead of a payment into court.

The abolition of payments into court will not be of much significance to organisations which were already able to avoid the present requirement because they were obviously “good for the money”. But for those defendants of less self-evident size and solvency, the new rule is excellent news. Where they would have had problems proving that they were “good for the money” and so unable to avoid making a payment in, they will now be able to hold on to the funds in question where their offer is rejected instead of having to leave the money in court until the end of the action. Under the new regime, if a defendant makes an offer which is accepted and then fails to pay the sum in question within 14 days, the claimant will be entitled to enter judgment and the defendant will lose the costs protection the offer would normally achieve.

EU Regulation
European competition inquiry
The European Commission has published its interim report on the inquiry into the business insurance sector. Market fragmentation is a serious issue and the report highlights several factors that may adversely affect competition. These include lack of transparency in brokers’ fees, standardisation of terms between reinsurers, prohibition of commission rebating by insurers and brokers' conflicts of interest. The insurance block exemption is likely to be subject to detailed scrutiny by the Commission in the next stage of its investigation. Comments on the report are invited before 10 April 2007. The final report is due this summer.

What is Solvency II?
The European Commission, jointly with Member States, is carrying out a fundamental review of the regulatory capital regime of the insurance industry (the Solvency II project). Its
objective is to establish a solvency system that is better matched to the true risks of insurers enabling supervisors to protect policyholders' interests as effectively as possible. A draft Solvency II directive had been expected last year but this has been put back to July 2007. Implementation of the directive by EU member states is scheduled for 2010, assuming adoption of the directive in 2008. The Treasury and the FSA have recently published a joint discussion paper of the proposals. For further information see The Treasury's page on EU financial services.

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