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Hurricane Damage and the Law

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Introduction

On 11 September 2004 Hurricane Ivan crossed the western Caribbean and devastated the Cayman Islands. Virtually every structure in the Islands was damaged or destroyed. Total losses ranged from single structure bungalows to entire office blocks. Thousands of trees were uprooted and thrown across roads and buildings, together with hundreds of vehicles and boats. Shoreline, sand and soil were eroded and, in some cases, transported considerable distances by the wind. There was extensive and very serious flooding. Because of climate change and the maritime position of many Commonwealth jurisdictions, Hurricane Ivan provides a convenient case study.[1] Many Commonwealth jurisdictions are susceptible to hurricane or typhoon damage. This article is concerned with the insurance aspects of property losses, whether real or chattel, arising or likely to arise from damage caused by extreme weather events.[2]

The problem

Insurance contracts are term contracts. But, unlike other term contracts, such as leases and charterparties, the parties, or at least one of them, do not expect the terms to be enforced. Insurance insures against risks which are by definition uncertain to occur.[3] Consequently the insured invariably fails to negotiate or even actively consider the terms of the policy – 'I am never going to be involved in a car crash' – while the insurer relies on standard terms, with variations, which are often inappropriate to the risks in question. Add to this the insurer's undoubted vulnerability to fraud and you have a recipe for dispute when the insured event occurs, particularly if it is extreme.

Background

The origins of the modern insurance contract date from practices adopted by Italian merchants in the 14th century. If the Merchant of Venice had insured his ships, as he could

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1 As will the fallout from the Asian tsunami and Hurricane Katrina.

2 Other relevant topics are considered in papers presented to the Hurricane Ivan Conference in the Cayman Islands in January 2005, including *Strata Titles* by Harpum and Duckworth, *Leasehold Law* by Taskis and Radley-Gardner and *Easements, Torts and Professional Negligence Issues* by Brock and Harpum. E-mail brock@falcon-chambers.com for details.

3 Except life insurance where death is certain, but the time of death is not.

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have done in the late 16th century, he would never have been in peril of forfeiting his bond. The centre of the insurance market moved to London in the 17th century and was dominated for several centuries by the insurance of maritime risks, that is the risk of losing ships and cargoes at sea. The market developed around the institution of Lloyd's of London and indeed the standard Lloyd's marine insurance policy was adopted as the statutory form in England by the Marine Insurance Act 1906. In due course, limited companies and mutual insurance clubs proliferated for the provision of insurance against marine and other risks, particularly the risk of fire.

Throughout the development of the insurance industry the English courts built up a jurisprudence, which now forms the basis of insurance law; the first significant developments were provided, in the mid-18th century, by Lord Chief Justice Mansfield who was responsible for many of the seminal judgments in the field.[4] The fact that modern insurance law derives from marine insurance has contributed to the unsatisfactory nature of some of the principles of law that have developed. There is a vast difference between the circumstances surrounding a marine policy and those relevant to a mass-produced standard form property, household or motor policy. The English courts have been slow to intervene to correct long-established marine principles in contrast to the interventionist approach of the US courts, perhaps because the UK has long had a comprehensive social security system providing more protection to consumers than that in the US.[5]

Local law

The law of the Cayman Islands (CI) derives from English law, but from a distant historical base.[6] Accordingly, insurance law, as it relates to the CI, derives from English case law[7] supplemented by the Insurance Law (2001 Revision) as amended, which is mainly concerned with licensing, and other relevant CI legislation. There appears to be no statutory control of insurance policy terms or conditions in the CI which are subject only to the negotiating position of the parties. However, parties to insurance contracts invariably utilise standard printed forms with variations by way of special conditions. These terms are inherently unsatisfactory by comparison with bespoke contracts and inevitably lead to duplication, overlap and confusion. This has led to recent statutory and extra-statutory intervention in the UK,[8] but these provisions do not apply to the CI. A similar position exists in other Commonwealth jurisdictions, the divergence from English law depending on the date of settlement, independence or other deracinating event. As regards property law, many Commonwealth jurisdictions have a system of strata title in addition to freehold and leasehold titles. The CI is a good example.[9]

4 Eg *Carter v Boehm* (1766) 3 Burr 1905, *Pawson v Watson* (1778) 2 Cowp 785 and *De Hahn v Hartley* (1786) 1 TR 343.

5 See Hasson (1984) 'The special nature of the insurance contract: A comparison of the American and English law of insurance', 47 MLR 505.

6 It is understood by the writer that CI law, insofar as it is not codified, derives from English law at the date of settlement, conventionally assumed to have occurred at some point between 1658 and 1734.

7 And English statutes prior to 1 George II C 1. See s 40 of the Interpretation Law of the CI.

8 See the Unfair Terms in Consumer Contracts Regulations 1999, the relevant provisions of the Financial Services and Markets Act 2000 and the establishment of the Statements of Practice and the Insurance Ombudsman Bureau.

9 See the Cayman Islands Strata Titles Registration Law (1996 Revision), which was closely modelled on the New South Wales Conveyancing (Strata Titles) Act 1961. See also the paper by Harpum and Duckworth referred to in fn 2 above.

Basic principles

Insurance involves the management of risk. The first and principal distinction to be made is between first party insurance under which the insured[10] insures a personal life, property, goods, vehicles or the like and third party or liability insurance, where the insured insures against personal potential liability in law to pay damages to a third party. First and third party insurances may well be combined in the same policy. This article will be concerned only with first party insurance. Insurance today may be provided by underwriters at Lloyd's, limited companies or by mutual undertakings. Insurers may reinsure. This article is not concerned with reinsurance.

Somewhat surprisingly, there has never been any legal definition, either in case or statute law, of the meaning of a contract of insurance. As judges have pointed out, it is not an easy matter to define.[11] Like the elephant, it may be easier to say that one knows a contract of insurance when one sees one,[12] not least because insurance law has its own peculiar principles, such as the doctrine of utmost good faith and the special importance of warranties, which do not apply to general contract law.

A reasonable definition may be as follows: a contract of insurance is any contract whereby one party assumes the risk of an uncertain event, which is not within his control, happening at a future time, in which event the other party has an interest, and under which contract the first party is bound to pay money or provide its equivalent if the uncertain event occurs.[13] An insurance contract involves at least the following essential elements:

(1) There must be a binding contract and the insurer must be legally bound to compensate the other party.

(2) There must be uncertainty as to whether or not the event insured against will occur.[14]

(3) The insured must have an insurable interest in the property the subject of the insurance.

(4) The event insured against must be outside the control of the party assuming the risk.

(5) The insurer must undertake to pay money or money's worth on the occurrence of the uncertain event.[15]

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10 In this article, the person taking out the insurance cover will be referred to throughout as 'the insured' and the person providing the insurance as 'the insurer'.

11 *Department of Trade and Industry v St. Christopher Motorists' Association* [1974] 1 All ER 395; *Medical Defence Union v Department of Trade* [1979] 2 All ER 421 at p. 429.

12 By contrast, for example, with a contract of guarantee. See *Seaton v Heath* [1899] 1 QB 782.

13 This definition is taken from the excellent and recently revised study by Birds (2004) *Modern Insurance Law*, 6th edn, p. 14. Prof. Birds is also the senior editor of the standard text (2003) *MacGillivray on Insurance Law*, 10th edn. Other more discursive texts are *Ivamy on Fire & Motor Insurance* and *Clarke on The Law of Insurance Contracts*.

14 The exception to this principle is life insurance where death is inevitable, but the uncertainty involves the time when it will occur.

15 Various cases, such as *Hampton v Toxteth Co-operative Society* [1915] 1 Ch 721, suggest that there may be other essential elements to an insurance contract, but the above will suffice for present purposes.

Insurable Interest

Principles

In England the unsavoury practice of gambling on the prospect of the death of unconnected third parties resulted in s 1 of the Life Assurance Act 1774 which required the insured to have an insurable interest in the life insured. Section 2 of that Act required the names of persons interested to be inserted into the policy and s 3 required a declaration that the insured could recover no more than the amount of the value of his interest. This Act was followed by s 18 of the Gaming Act 1845 which rendered all contracts by way of gaming and wagering in England void. At common law, which probably applies to the CI, there is authority for the proposition that the insured must have an insurable interest in the relevant property insured, both at the date of the contract and at the date of the loss.[16] For present purposes we can assume that this remains the case.

In England, controversy has raged as to whether the Life Assurance Act 1774 applies to insurances of real property. See the conflicting statements of the Court of Appeal in *Re King* [1963] Ch 459 at 485 per Lord Denning MR and *Mark Rowlands v Berni Inns* [1986] QB 211.[17] More recently, in *Siu Yin Kwan v Eastern Insurance* [1994] 1 All ER 213, the Privy Council held that s 2 of the 1774 Act did not apply to a policy of liability insurance.

It is sensible to assume that in the CI and in many other Commonwealth jurisdictions the old common law principles and/or the 1774 Act do impose a requirement that the insured has an insurable interest in the relevant property at the date of the contract as well as at the date of the loss. The insured has to have an insurable interest at the date of the loss because a contract of insurance, by its very nature, is only a contract to indemnify an insured against a loss actually suffered.[18] As regards the CI, it would be surprising if s 3 of the 1774 Act applied to limit the insurer to recovery of no greater sum than the amount of the value of the insured's interest. This would mean that a tenant who insures the tenanted property and names the landlord as an interested party would be limited in recovery to the value of the tenant's interest which may be much less than the value of the property or the sum insured.[19]

Relevant elements

Assuming that an insurable interest is required at the date of contract and at the date of loss, the identification of the insurable interest is of real importance for present purposes because it identifies the interest of the insured which may be different depending on whether the relevant party is a freehold owner, a strata title corporation, a proprietor of a strata title, landlord or tenant, mortgagor or mortgagee, trustee or beneficiary or other limited owner.

16 *Sadler's Company v Badcock* (1743) 2 Atk 554.

17 There seems to be complete confusion in the text books. Compare *MacGillivray* at para 1–161 to 162, *Ivamy* at para 175–81 and Clarke at para 4-4A.

18 *Macaura v Northern Assurance* [1925] AC 619.

19 A point not considered in *Re King* because the tenant had covenanted to repair and accordingly had an interest in the whole value of the property demised.

An insurable interest is 'a right in the property, or a right derivable out of some contract about the property, which in either case may be lost upon some contingency affecting the possession or enjoyment of the party'.[20] In *Lucena v Craufurd* (1806) 2 B&PNR 269, the Crown Commissioners insured a number of enemy ships captured by the Royal Navy on the high seas. They had statutory power only to take charge of such ships when they reached British ports. Some of the ships were lost at sea before reaching port. The House of Lords held that the Commissioners could not recover under the insurance policy because they had no present proprietary right to the ships when they sank.

Accordingly, as the law stands in England and the CI, a mere expectation or even a moral certainty of loss should a particular property be destroyed, is not enough to create an insurable interest. There must be a present right to a legal or equitable interest or a right under contract. A person with a contingent interest, or a beneficiary of property under a will of a dying testator, has no insurable interest because the contingency may not happen. A turnpike company that insured a bridge spanning a stream connecting two parts of its road, but with no interest in the bridge itself, had no insurable interest in it. The risk that a person might become liable for negligently causing damage to someone else's property does not of itself give an insurable interest in that property as opposed to an interest in their potential liability.[21]

In *Macaura v Northern Assurance* [1925] AC 619 the sole shareholder of a limited company, who was also a substantial creditor of the company, insured in the sole shareholder's own name timber owned by the company. The timber was destroyed by fire but the House of Lords held that the sole shareholder had no insurable interest in it. He was a shareholder but he had no right to property owned by the company, which was a separate legal person, even though it was obvious that the shares would have diminished in value proportionately to the destruction of the timber. The sole shareholder could have put matters right by arranging for the company to insure the timber, but he did not do so.

This principle remains a serious trap for the unwary. *Macaura* has been distinguished and criticised,[22] but must be assumed to be good law. It is to be assumed that the courts of the CI will do their best to protect the insured's interest where possible. See, for example, *Glengate-KG Properties v Norwich Union* [1996] 1 Lloyds Reports 614, where the English Court of Appeal held that 'the interest of the insured' in a policy covering the owner of a building against consequential loss following an insured peril included the value of lost architects' plans, although the plans were owned by the architects and not by the insured. However, it may be said that the claim in that case was within the definition of expressly insured consequential loss.

Limited interests

Accordingly, it follows that in order to recover the insured's indemnity, the insured must have a proprietary or contractual right to, or possession of, the property in question with a legal liability for it, such as that of a bailee. Persons with limited interests in property, such as a mortgagor, mortgagee, landlord, tenant, trustee and beneficiary, will have a sufficient

20 Per Lord Eldon in *Lucena v Craufurd* (1806) 2 B&PNR 269; and see *Glengate-KG Properties v Norwich Union* [1996] 1 Lloyd's Reports 613 at p. 624.

21 *Deepak Fertilisers & Petrochemical Corporation v ICI Chemicals & Polymers* [1999] 1 Lloyd's Reports 387 at pp. 399–400.

22 *The Moonacre* [1992] 2 Lloyd's Reports 501; *Feasey v Sun Life Assurance of Canada* [2003] Lloyd's Reports IR 637 at pp. 657 and 674. It has been disapproved in other jurisdictions, eg by the Supreme Court of Canada in *Constitution Insurance of Canada v Kosmopoulos* (1987) 34 DLR (4th) 208.

proprietary interest in property to insure it up to its full value, but *prima facie* such a person may recover only sufficient to indemnify himself as regards the value of his interest.

For example, a tenant of property has an insurable interest in it and can therefore insure it up to its full value, but that does not mean that there can be recovery for that value.[23] If the tenant is merely a weekly tenant with no obligation to insure or repair, his recovery is limited to the value of the tenant's insurable interest which will extend only to the minimum period of a permissible notice to quit.[24] If the tenant has a fixed term lease under which there is liability to pay full rent regardless of the destruction of the property,[25] the tenant will have an interest at the time of loss to the full extent of the rental liability. If the tenant is under an obligation to insure and/or to repair the demised property, the interest will be to the full value of the property.[26] By contrast, a landlord's reversionary interest appears to extend to the full value of the property in any case, even where the tenant is liable to repair, because of the risk of the tenant failing to comply with the tenant's obligation. However, in that event the insurer may have subrogation rights against the tenant.

Similarly, a mortgagee will recover only the value of the outstanding debt[27] while a vendor of land may recover nothing if the vendor can still enforce the contract of sale against the purchaser. If the limited owner has the expectation of profits or other advantages beyond a proprietary interest in the property, such as the expectation of profits to be made from ownership or occupation of the property, there is an insurable interest in that expectation, but the usual indemnity policy on property will not indemnify against consequential losses so that the limited owner must insure such losses separately.

It is common for persons with a limited interest in property to insure their own interest and the interest of third parties, whether by joint insurance or by noting on the policy. For instance, a policy taken out by a mortgagor of property that is expressed to insure the mortgagee's interest will cover both. Such policies may be construed as containing, in effect, separate contracts of insurance between the insurer and each co-insured.[28]

As regards real property insurance,[29] the position appears to be[30] that the third party's interest will be sufficient to allow the insured to recover for the benefit of a third party or to allow the third party himself to sue on the policy so long as the contract, properly construed, reveals an intention to cover the third party's interest.[31] In addition, the insurance will obviously have to cover the full value of the property rather than merely the interest of the insured as limited owner. A policy will be more readily construed to this effect where the parties are trustee and beneficiary[32] or mortgagor and mortgagee.[33] This is because in

23 The basis of the tenant's interest is best analysed in *MacGillivray* at paras 1–43ff.

24 In England, four weeks is the minimum period for notice to quit residential property by virtue of s 5 of the Protection from Eviction Act 1977.

25 Unlikely, because any well drafted commercial lease will contain an abatement of rent provision in the event of damage by insured risks.

26 As in the leading English case of *Re King* [1963] Ch 459.

27 *Westminster Fire Office v Glasgow Provident* (1888) 13 App Cas 699.

28 See *Arab Bank v Zurich Insurance* [1999] 1 Lloyd's Reports 262 and *FNCB v Barnet Devanney* [1999] Lloyd's Reports IR 43.

29 Different considerations may apply to the insurance of goods, as to which see Birds at pp. 61–72.

30 The position in England is clouded by the unsettled question as to whether the relevant provisions of the Life Assurance Act 1774 apply to real property insurances, but this question is probably irrelevant to the CI.

31 *Hepburn v Tomlinson* [1966] AC 451.

32 *Davjoyda Estates v National Insurance of New Zealand* (1967) 65 SR (NSW) 381.

33 *Hepburn v Tomlinson* [1966] AC 451 at pp. 481–82.

the first case the interests of the parties are similar and in the second there is likely to be a noting of both interests on the policy. The position is likely to be similar in the case of insurance by strata title corporations in respect of the interests of strata title owners in the CI.

This is less likely to be the case where the interests of the parties are more distinct, as in the case of vendor and purchaser[34] or landlord and tenant. In *Re King* [1963] Ch 459 the tenant was held to have an insurable interest to the full value of the property because he was subject to a covenant to repair. He was not insuring for the benefit of the landlord even though the latter was named in the policy. The landlord's interest was to control the receipt of the insurance monies and insist on reinstatement, but he could not sue on the policy as co-insured.[35]

Repudiation of Policies and Liability

It is not intended in this article to consider the consequences of fraudulent or exaggerated claims or misrepresentations and misdescriptions inducing cover. Nor will consideration be given to the avoidance of policies on the grounds of public policy or statutory intervention in respect of unfair terms in other jurisdictions.[36] However, this article will consider the extent of the insured's duty of utmost good faith which is, in effect, an absolute duty and not dependent on intentional wrongdoing. Some consideration must also be given to the nature and effect of warranties and conditions.

Utmost good faith

The consequences of deliberate fraud and misrepresentation are common to all contracts. However, non-disclosure and a breach of the continuing duty of utmost good faith are peculiar to a class of contracts, those said to be *uberrimae fidei* or of the utmost good faith, of which the insurance contract is the principal example. Leaving aside fraud and misrepresentation, the parties to an insurance contract are also both under a duty of utmost good faith which means that they are bound to volunteer to each other before the contract is concluded any information that is material. The question also arises as to whether the duty of utmost good faith effectively continues to require disclosure throughout the term of the contract, as well as at its inception.

The duty binds both parties, but is substantially more onerous on the insured. An applicant for insurance is under a duty to disclose to the insurer, prior to the conclusion of the contract, all material facts within their knowledge that the latter does not know or is not deemed to know. A failure to disclose, however innocent, entitles the insurer to avoid the contract *ab initio*, and upon avoidance the contract is deemed never to have existed.

The rule was first explained by Lord Mansfield in *Carter v Boehm* (1766) 3 Burr 1905 as follows:

> Insurance is a contract upon speculation. The special facts, upon which the contingent chance is to be computed, lie most commonly in the knowledge of the insured only: the under-writer

34 *Rayner v Preston* (1881) 18 Ch D 1.

35 Compare *Beacon Carpets v Kirby* [1985] QB 755 where the provisions in the lease and the insurance policy were different.

36 See, for example, the Unfair Terms in Consumer Contracts Regulations 1999 in England.

> trusts to his representation, and proceeds upon the confidence that he does not keep back any circumstance in his knowledge, to mislead the under-writer into a belief that the circumstance does not exist, and to induce him to estimate the risque[37] as if it did not exist.

The duty extends to facts and not opinions. An opinion given in good faith as to his health by the proposer for life insurance will not affect cover, but failure to disclose the fact of a previous consultation with a doctor, even if the proposer believes himself to be fit, may be a breach of the duty and vitiate the policy. However, so long as the proposer is honest and does not wilfully close his eyes to facts he is under no obligation to make further enquiries and is not fixed with so-called constructive knowledge of facts of which he is unaware.[38]

What need not be disclosed

Material facts need not be disclosed if they: (1) diminish the risk; (2) are facts which the insurer knows or is presumed to know or are matters of common knowledge; or (3) are facts of which the insurer waives disclosure.[39] Most insurance is conducted through agents. Where the agent of the insurer knows or is deemed to know a fact, it is not required to be disclosed.[40]

As to waiver, the form of question in the proposal form may reduce the scope of the duty of disclosure. For instance, where a question in a proposal form is not answered, and where the question is not followed up by the insurer, this may evidence a waiver of the question[41] unless the lack of an answer implied a negative answer to the question, which a somewhat narrow distinction. A proposal form will often ask for specific facts, such as details of previous losses suffered during a specified period. The duty of disclosure will only extend to the period in question. There has been relatively recent judicial consideration as to whether the duty can be contractually excluded,[42] but it is difficult to see how a duty imposed by law can be contracted out since the duty of disclosure arises by law independently of the contract.

Materiality

More interesting questions arise in the determination of whether a fact is material for the purposes of non-disclosure. It is material if it would influence the formation of an opinion of a reasonable or prudent insurer in deciding whether or not to accept the risk or what premium to charge.[43] Accordingly, the fact is material even if the insurer would not have

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37 Creative spelling was more acceptable in the 18th century than now: Dr Johnson preferred smoak to smoke.

38 *Joel v Law Union & Crown Insurance Company* [1908] 2 KB 863 per Fletcher Moulton LJ at p. 884 approved by the English Court of Appeal in *Economides v Commercial Union* [1997] 3 All ER 636 at p. 648.

39 For an example of the second category see the facts in *Carter v Boehm* or, in the modern context, the dangers of asbestos of which insurers are deemed to know: *Canadian Indemnity v Canadian Johns-Manville* (1990) 72 DLR (4th) 478.

40 *Ayrey v British Legal & United Provident Assurance* [1918] 1 KB 136.

41 *Roberts v Avon Insurance* [1956] 2 Lloyd's Reports 240.

42 *HIH Casualty & General Insurance v Chase Manhattan Bank* [2001] 2 Lloyd's Reports 483, *Pan Atlantic Insurance Company v Pine Top Insurance* [1995] 1 AC 501 and *Toomey v Eagle Star Insurance* [1994] 1 Lloyd's Reports 516.

43 *Lambert v CIS* [1975] 2 Lloyd's Reports 485, as explained by the House of Lords in *Pan Atlantic*.

acted differently if he had known the fact: it is sufficient if the insurer would merely have wanted to know of the fact when making his decision. This test imposes a heavy burden on the insured and in *Pan Atlantic Insurance Company v Pine Top Insurance* [1995] 1 AC 501 the House of Lords appeared to attempt to mitigate this harshness by introducing an additional requirement that the non-disclosed, but material, fact must also have induced the insurer to enter into the contract. On analysis, this requirement may not help the insured because it would probably be extremely difficult for the insured to prove that the actual insurer was not induced by the non-disclosure. However, despite the confused results arising from the decision of the House of Lords in *Pan Atlantic*,[44] the problem has been mitigated by the subsequent decision of the Court of Appeal in *Drake Insurance v Provident Insurance* [2004] Lloyd's Reports IR 277 in which it was held that inducement must be proved by the insurer.

The present state of the law on this question may be of considerable importance in the CI. In relation to property insurance, a fact will generally be material if it relates to the physical hazard to the property in question. Accordingly, facts will be material if they relate to the nature, construction or use of an insured building or whether it is particularly exposed to risk. It is plain from an analysis of common form policies that hurricane and other similar natural perils are insurable in the CI, but it may well be that different properties and locations may be peculiarly susceptible to such risks, the nature of which may not have been disclosed on the assumption of risk.[45]

Is the duty continuing?

There is no doubt that the duty of utmost good faith binds the parties up to the date of the contract. While there appears to be a continuing duty of utmost good faith during the life of the contract, the exact nature of this continuing duty is unclear and has been the subject of hot debate in recent cases.[46] It is assumed that there are unlikely to be relevant issues in the CI.

Increase of risk clauses

Some contracts of insurance, particularly fire policies, impose a duty on the insured to disclose facts occurring during the term of the policy which materially increase the risk. Such provisions clearly impose an express duty of further disclosure. Unless temporary increases in risk are specifically provided for, the increases must be permanent or at least long term, such as permanent alterations to the building insured.[47] More importantly, policies often require notification that the property is unoccupied for a specified period, requiring that fact to be reported to the insurer. For property to be unoccupied there must normally be the absence of any physical presence in the building insured.[48] Problems may arise in the CI, where vacation property is unoccupied for long periods, unless the degree of lack of

44 In which the House of Lords was sharply divided by 3 to 2, the minority giving strong dissenting judgments.

45 On these difficult questions, see in particular the discussion in Birds at pp. 121–24.

46 See the decision of the House of Lords in *The Star Sea* [2003] 1 AC 469 and of the Court of Appeal in *The Mercandian Continent* [2001] 2 Lloyd's Reports 563 and *Agapitos v Agnew* [2003] QB 556.

47 *Exchange Theatre v Iron Trades Mutual Insurance* [1984] 1 Lloyd's Reports 149.

48 *Marzouca v Atlantic & British Commercial Insurance* [1971] 1 Lloyd's Reports 449. Compare mere absence on holiday: *Winicofsky v Army & Navy General Insurance* (1919) 88 LJKB 111.

occupancy has been clearly stated by the insured. This may give rise to difficulties under the general duty of good faith, increase of risk clauses or warranties discussed below.

Warranties and Conditions

The contract of insurance will invariably consist not just of the policy document itself, but also the completed proposal form and other documents, including renewal notices and standard terms. The contract will usually contain, in particular, four types of relevant terms:

(1) warranties;

(2) conditions;

(3) clauses descriptive of the risk; and

(4) exceptions to the risk.

Warranties

The warranty is the most fundamental term of an insurance contract with the most fundamental consequences of breach.[49] A warranty is a promise made by the insured which must be strictly complied with, and breach of which will automatically discharge the insurer from liability under the contract.[50] The status of warranties was considered by the House of Lords in *The Good Luck* [1992] 1 AC 233, where fulfilment of a warranty was described as akin to compliance with a condition precedent to the liability or further liability of the insurer. The insurer only accepts the risk provided that the warranty is fulfilled. Automatic cancellation of the cover for breach of warranty applies equally to property as it does to marine insurance.[51] It is possible for the contract to provide for a breach to have the effect of suspending cover rather than leading to a complete discharge of liability, but this is not usually the case.[52]

Types of warranty

A warranty may be of a past or present fact, but is more likely, in the property context, to be a warranty as to the future, known as a continuing or promissory warranty. Common examples are warranties to maintain alarms or sprinkler systems in commercial fire policies or a warranty to maintain property in a reasonable condition, which is found in most property policies. Continuing warranties may arise from completed proposal forms or from the body of the policy. Whether a warranty is continuing or present depends primarily on the language used. It may be both, but in order to be continuing it must contain in its wording a clear reference to the future. For example, in *Woolfall & Rimmer v Moyle* [1942] 1 KB 66, the insured warranted in a proposal form that its machinery, plant and paths 'are … properly fenced and guarded, and otherwise in good order and condition'. The English Court of

49 This is in contrast to general contract law where conditions are more fundamental terms than warranties. See *Hongkong Fir Shipping v KKK* [1962] 2 QB 26.

50 For the classic examples see the facts in *De Hahn v Hartley* (1786) 1 TR 343 and *Pawson v Watson* (1778) 2 Cowp 785, both decisions of Lord Mansfield.

51 See the decision of the English Court of Appeal in *Hussain v Brown* [1996] 1 Lloyd's Reports 627.

52 *The Lydia Flag* [1998] 2 Lloyds Reports 652.

Appeal rejected the insurer's argument that the warranty was continuing. The use of the present tense, rather than the future, was decisive. In *Hair v Prudential Assurance* [1983] 2 Lloyd's Reports 667, a warranty in a fire policy that the property 'is occupied' was held not to have continuing effect.[53] The construction of warranties of this kind is likely to be of particular interest in the CI in respect of current claims concerning Hurricane Ivan because so much property – particularly condominiums – is vacation property.

Basis of the contract clauses

Historically, a device commonly used by insurers was to introduce a clause into the contract making the questions, answers and declarations on a proposal form the basis of the contract, thereby converting all statements into warranties. This, and other devices of a similar kind, have led the courts, where possible, to construe such draconian provisions *contra proferentem*, that is against the insurer as the provider of the standard terms. The principle of construing terms in favour of the weaker party, in this case the insured who normally has to accept standard terms from the insurer, is, however, irregularly used in practice.

Having said that, it is plain that the courts will strive to protect the insured from unreasonable conditions. For example, the question often arises whether a warranty applies throughout the policy or only in respect of particular risks, particularly in a policy containing a number of different sections. In *Printpak v AGF Insurance* [1999] Lloyd's Reports IR 542 the English Court of Appeal held that breach of a warranty, plainly directed to only one section of a multi-section policy, did not vitiate cover in respect of the other sections. This reinforces the idea that a multi-section policy may be regarded as, in effect, consisting of several different insurance contracts along the lines of the principles relating to the insurance of third party risks being treated as separate policies in respect of different insureds.[54]

Clauses descriptive of the risk

Sometimes a term in a policy, which appears to be a warranty, may be construed as a statement or clause descriptive of or delimiting the risk. This sort of term, relating to the use of insured property, has a similar effect to an exception to the risk properly so-called. This is sometimes called a 'suspensive condition'. The most recent decision on this aspect of the law is *Kler Knitwear v Lombard General Insurance* [2000] Lloyd's Reports IR 47. The claimant's renewal of its business policy in May 1998 was subject to the following endorsement:

> It is warranted that within 30 days of renewal 1998 the sprinkler systems … must be inspected by an … approved engineer with all the necessary rectification work commissioned within 14 days of the inspection report being received.

General Condition 2 clearly stated that all warranties would attach and apply throughout the duration of the contract and that non-compliance with any of them would be a bar to any claim, other than one made during the renewal period itself. The premises suffered storm damage in October 1998. It transpired that no inspection of the sprinkler systems had been carried out within the prescribed 30 days, although the Claimant contended that an inspection had taken place in August, approximately 90 days after renewal. The judge held that the clause

53 See also *Hussain v Brown* [1996] 1 Lloyd's Reports 627.

54 These principles have been repeatedly propounded in the American courts. See Clarke at para 20-6C1.

was a 'draconian term' and that 'it would be absurd and make no rational business sense for a claim for property damage to be barred if inspection of the sprinkler system was not carried out on time'. The sprinkler system was relevant to fire and not to storm damage.

This case is instructive in the context of recent events in the CI. The term in respect of the sprinkler system plainly related to potential fire damage. The damage actually suffered was storm damage. Nonetheless the insurer attempted to repudiate liability. The decision has been the subject of criticism,[55] but it is an illustration of the tension between the strict contractual rights of the insurer on the one hand and, on the other hand, the sympathy which the court may have for the insured who suffers damage by a risk, in this case storm damage, which was plainly not relevant to the term in question.

Conditions

Conditions in insurance law, by contrast to warranties, are lesser terms, compliance with which may be dispensed with if it is unnecessary, for example by reason of information which the insurer possesses from another source. Furthermore, a breach of condition is said to be actionable only if it causes the loss whereas, as has been seen, there is no such requirement as regards warranties.

A good example of a term that may be a condition or a warranty is the standard provision in insurance contracts requiring the insured to give prompt notice of any occurrence likely to give rise to a claim.[56] Such terms may be conditions precedent to the bringing of a claim, suspensive conditions or merely procedural conditions giving rise only to a claim in damages by the insurer.[57] In practice, unless there is a reference to the condition in question being precedent to the insurer's liability, a breach of condition does not normally entitle the insurer to repudiate liability. The problem is that many policies will contain a general reference to the conditions being conditions precedent and in these cases it is difficult to avoid the conclusion that compliance with the condition is a condition precedent to the insurer's liability. The position has not been helped by a recent decision of the English Court of Appeal describing such a provision as an innominate term, breach of which in particular circumstances could entitle the insurer to defeat the claim.[58]

As now appears to be the case with warranties, the burden of proof in relation to alleged breach of condition in insurance law is always on the insurer.[59] The burden of proof may be reversed contractually, but only by very clear words.[60]

Assignment

A number of questions in insurance law and practice arise under this heading. There are three particular problems.

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55 Eg Birds at pp. 160–61.

56 For what constitutes 'likely' in this context see *Jacobs v Costa & Avon Insurance* [2000] Lloyd's Reports IR 506 and *Layher v Lowe* [2000] Lloyd's Reports IR 510.

57 Indeed it was recently said in the English Court of Appeal, in *Virk v Gan Life Holdings* [2000] Lloyd's Reports IR 159 at p. 162, that the issue as to whether a particular term is a condition precedent to liability usually arises in the context of clauses governing claims procedures.

58 *Alfred McAlpine v BAI* [2000] 1 Lloyd's Reports 437.

59 *Bond Air Services v Hill* [1955] 2 QB 417 at p. 427 per Lord Goddard CJ.

60 Ibid at p. 428.

Assignment of the subject matter of insurance

This problem concerns insurance of property when the property is sold or otherwise disposed of by the insured. It has often been considered in connection with the sale and purchase of land. In principle, the assignment of the subject matter of an insurance policy cannot operate to assign the contract of insurance. Once contracts for the sale of land are exchanged, the purchaser obtains an equitable interest in the property, although the vendor retains the legal estate. The vendor has ceased to have an insurable interest and if the property is lost or damaged he can recover nothing for this reason. This is why the existence of the relevant insurable interest (considered above) is so important in this context. If, between contract and completion, the purchaser does not insure the property, the question arises as to whether, in the absence of an assignment the benefit of the vendor's policy (considered below), the purchaser can claim the benefit of the vendor's policy. In principle, the answer is 'no'.[61] The result is that on exchange of contracts the purchaser has to insure the property and this may lead to double insurance which, apart from being a waste of money, leads to its own problems as regards the liability for rateable proportion of any indemnity as between insurers.

Assignment of the benefit of a policy

If the assignment of the subject matter of a policy does not of itself assign any benefit under the policy to the assignee, the question arises as to whether or not it is possible to assign the benefit itself expressly. The benefit is a chose in action which can be assigned at law[62] or in equity. A mortgagor's covenant to insure operates as an equitable assignment in favour of the mortgagee because of the close relationship between those interests.[63] But to bind the insurer, and to make the insurer directly liable to pay the assignee, notice must be given to the insurer so that the assignment is legal. Otherwise the assignee can proceed only by suing the assignor to compel the assignor to claim from the insurer. The insurer's consent is not required because the insured is simply saying that the proceeds of any claim he may have are to go to a third party. However, the assignee will recover only what the assignor/insured is entitled to and accordingly express assignment of the benefit of the policy may not satisfy the assignee to the desired extent, as in the case of a vendor and purchaser.[64]

Assignment of the policy

In principle, any insurance policy is freely assignable, being itself a chose in action. However, because all presently relevant forms of insurance are regarded as personal to the particular insured, any assignment of them requires the consent of, and not just notice to, the insurer. The result is that, in effect, non-life and non-marine policies, being the policies relevant for present purposes, are not really assignable at all because insurers would consent to an 'assignment' to a new insured only in circumstances that would amount to the creation of a new contract or a novation.

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61 See the leading case of *Rayner v Preston* (1881) 18 Ch D 1.

62 In England under s 136 of the Law of Property Act 1925.

63 *Clerical Mutual General Insurance v ANZ Banking Group* [1995] 3 All ER 987.

64 In England, s 47 of the Law of Property Act 1925 provides that insurance monies will be held by a vendor on behalf of a purchaser, but this provision appears not to apply in the CI.

Construction and Causation: Risks Covered and Risks Excepted

Standard terms

Unlike the position in the conveyancing of interests in real property, and like the position in respect of domestic and international trading contracts, insurance contracts are invariably made on the standard terms of the insurer. Depending on the bargaining position of the insured, the standard terms may be subject to variations, exclusions or additions, but in general the contract is based on the standard, and in principle immutable, terms proffered.[65]

There is no requirement in law that an insurance policy should be reasonably intelligible in terms of content or even readily legible. Insurance policies are still often notoriously complex documents riddled with jargon, duplication and inconsistency, the layout incomprehensible to the untrained eye, and the print, or some of it, small and difficult to read. However, if it is legible, albeit with difficulty, it will still be binding.[66]

Risks

It is of the essence of insurance that it provides protection against the risks of uncertain events befalling the insured, normally events that would be adverse to the insured. As a general rule, the fact that a loss is occasioned by the negligence of the insured is irrelevant, but insurance does not cover losses deliberately caused by the insured. Accordingly, an insured who is negligent can normally recover, but subject to the important qualification that a term of the policy may frequently seek to exclude the insurer's liability in this respect, by imposing on the insurer an obligation to take reasonable care. This may be phrased as a warranty, a condition or as an exception to the risk. Whichever way it is done, if the insured is found not to have taken reasonable care, the effect will be to relieve the insurer from liability in respect of the relevant event. Such a term does appear in property insurances, requiring the insured, for example, to take reasonable care of the insured property or to maintain it in a reasonable condition. However, it now seems clear that such a term will not be construed so as to preclude recovery in the case of mere negligence.[67] In the case of hurricane damage difficult questions may arise as to whether failure to take such precautions as the installation and use of hurricane shutters would vitiate standard hurricane or storm cover. This is an issue that is understood to be becoming contentious in the CI in the context of current claims.

For example, in *Sofi v Prudential Insurance* [1993] 2 Lloyd's Reports 559, cover was subject to a condition requiring the insured to take 'all reasonable steps to safeguard any property insured' in a domestic all risks policy and a travel policy. The insured was travelling to France, arrived at the Dover Ferry Port with time to spare and left his car for 15 minutes in an unattended car park with £50,000 worth of valuables locked in the glove compartment. During that brief period the car was broken into and the valuables stolen. The English Court

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65 Hence the insurer being the *proferens* and the contract in appropriate circumstances being construed *contra proferentem*.

66 *Koskas v Standard Marine Insurance* (1927) 17 Lloyd's LR 59.

67 *Stephen v Scottish Boat Owners Mutual Insurance Association* [1989] 1 Lloyd's Reports 535 at p. 541 and *Devco Holder v Legal & General* [1993] 2 Lloyd's Reports 567.

of Appeal held that the insured was entitled to recover, not having, on the facts, acted recklessly. This case shows the tendency of the English courts to protect the insured in such cases. It remains to be seen how such conditions will be construed in the case of real property insurance.

In any event, it is well established that certain perils, such as wear and tear and inherent vice (that is what occurs or happens naturally, such as rust or the general effect of the weather), are never covered by indemnity insurance. This emphasizes the need for the precise definition of severe weather risks in policies concerned with potential hurricane damage.

Construction of particular terms and specified risks

Insurance contracts construed under the principles of English law will be governed by the normal rules for the interpretation of contracts most recently summarised by Lord Hoffmann in *Investors Compensation Scheme v West Bromwich Building Society* [1998] 1 All ER 98. The objective of the court is to divine the objective intention of the parties from the words of the contract construed in the context of the background facts known to the parties, but not their subjective intentions or the negotiations between them, except where words have a technical legal meaning, which is rare.

A relevant example of words construed in context can be seen in *Young v Sun Alliance & London Insurance* [1977] 1 WLR 104. Here, the insured's household policy insured him against loss arising from a number of causes, one group of which was 'storm, tempest or flood'. His house was built on a meadow. Several times water seeped in and caused damage to the ground floor lavatory. On one occasion, the water was three inches deep on the floor. The insured claimed that this constituted a 'flood'. The English Court of Appeal rejected his claim. The word 'flood' had to be construed in the context of the words 'storm' and 'tempest', which both imported notions of the abnormal and violent. In that context the word 'flood' was to be construed in the same way and meant a much larger irruption of water than mere seepage to a level of three inches.[68]

By contrast, the Court of Appeal held, in *Rohan Investments v Cunningham* [1999] Lloyd's Reports IR 190, that a flood occurred where damage was caused by an escape of water from a roof where the water had built up over a period of nine days of prolonged heavy rainfall and where the words in question were also 'storm, tempest and flood'. In that case the rapid accumulation of water was abnormal and was exactly the type of event that the insurance was intended to cover.

It is a question of degree in every case. It is likely that questions of this kind will arise in the context of claims in the CI in respect of hurricane and ancillary damage. As has previously been pointed out, the *contra proferentem* rule may be utilised by the courts against an insurer in an appropriate case, but it is by no means consistently applied.[69]

'All risks'

The phrase 'all risks' often appears in policies, particularly in respect of chattels. The nature of an 'all risks' policy was explained in *British & Foreign Marine Insurance v Gaunt* [1921] 2 AC

68 See *also Computer & Systems Engineering v John Lelliot* [1989] 54 BLR 1.

69 The rule was considered and rejected in *Glengate-KG Properties v Norwich Union* [1996] 1 Lloyd's Reports 614 at p. 623. See also *Marzouca v Atlantic and British Insurance* [1971] 1 Lloyd's Reports 449.

41. It covers all loss to the property insured occurring through some accidental cause, but not 'such damage as is inevitable from ordinary wear and tear and inevitable depreciation' or from inherent vice. The other significant feature of 'all risks' cover is that the insured has to show only that a loss is accidental; he need not show the exact nature of the accident or casualty which occasions the loss. However, even an 'all risks' policy can be subject to exceptions that will be upheld on usual principles of construction if they are clearly stated in the policy.[70]

'Accident'

Policies often refer to accidental damage or words to that effect. In *Mills v Smith* [1964] 1 QB 30 a householder's liability policy indemnified the insured against liability for 'damage to property caused by accident'. The insured was held liable in damages to a neighbour for settlement damage to the neighbour's house that was caused by the root action of a tree in the insured's garden taking water from the soil on the neighbour's land. It was held that this was caused by accident. The reasoning in this case is difficult to follow because the behaviour of the tree would seem to be natural and uninsurable rather than caused by 'accident'. However, this case illustrates the extent to which one party may be held liable to his neighbour on a policy of this kind and may be relevant to claims in relation to adjoining property in the CI.

'Loss'

A number of problems arise out of the relevant meaning of the word 'loss' as it appears in insurance contracts. What if insured goods have been removed by insured perils from the possession of the insured and the insured knows where the property is, but is unable to recover it? This may be relevant to the CI in the case of sand, soil, building materials, vehicles or boats and other chattels blown by the force of the hurricane onto other land, such as government property, from where the insured cannot recover it or only with difficulty.

If the lost property remains safely in the hands of bailees, then it is not lost if it can be readily recovered. In *Moore v Evans* [1918] AC 185, jewellery retained in enemy occupied Belgium under safekeeping was held by the House of Lords not to be lost even though it could not for the time being be recovered. The question is whether, after all reasonable steps have been taken, recovery is uncertain. In *London & Provincial Leather Processes v Hudson* [1939] 2 KB 724 a series of events had left insured chattels in the possession of a foreign trustee in bankruptcy. Even though in theory the insured might have had remedies in a foreign court to recover the chattels, it was nevertheless held that he had no obligation to attempt to recover them and that he could recover on the basis that the insured property was lost.

However, it is axiomatic that the lost property claimed must be the subject of insurance cover. Most property policies would cover the materials of which buildings are built, such as roof tiles or timbers that have blown away, but most such policies exclude the land itself, thereby precluding recovery of sand or soil washed or blown away from the insured's

70 See, for example, *Queensland Government Railways v Manufacturers' Mutual Life Insurance* [1969] 1 Lloyd's Reports 214. An all risks policy contained an express exception of loss caused by 'faulty design'. A bridge in the course of construction was swept away by a flood. It was held that the loss was caused by the faulty design of the piers of the bridge and not by the flood.

property. This may be a particular problem in the case of storm damage in coastal regions where sand and soil may be washed from one area to another.

Consequential losses

In principle, insurance of property only covers the property in respect of the loss attributable to is own value. Consequential losses are not recoverable unless they are separately insured. In *Re Wright & Pole* (1834) 1 A&E 621, an insured inn was destroyed by fire, but the insured was unable to recover in respect of the loss of custom and hire of other premises where consequential loss was not expressly insured. In *Theobald v Railway Passengers Assurance Company* (1854) 10 Exch 45, lost business profits were not recoverable under an accident policy. It is of course possible to effect insurance against loss of profits and other consequential losses arising as a result of damage or loss of the insured property itself and such cover, commonly known as interruption insurance, is now common in commercial policies.[71]

Prevention costs

If property is insured against a specific loss, can the insured recover if that loss does not actually operate upon the insured property, but the property is lost or damaged in circumstances when the insured peril was imminent? Furthermore, if there is no loss, but only because the insured incurred expenditure in preventing what would have been a certain loss, can the insured recover this expenditure? For example, where house contents are insured against fire and are damaged by water to prevent an existing fire spreading, such damage would normally be covered even if water damage was not covered or was an excepted peril. A more relevant question in the present context might be this: suppose that following heavy storms the level of the sea and the force of the waves are rising and it is as certain as it can be that unless measures are taken property will be flooded or damaged. The insured incurs expenditure in taking measures that prevent or lessen the damage to property. Can there be recovery of those costs under the policy? The answer appears to be no, at least in England.[72]

Causation

A normal policy requires the insured to show that the loss was caused by the insured peril. The cause does not have to be the last cause, but the effective, dominant or real cause of the loss.[73] It remains to be seen whether problems of causation will arise in the CI as a result of Hurricane Ivan, but an example may indicate how such difficulties might arise. In *Winicofsky v Army & Navy Insurance* (1919) 88 LJKB 111 goods were stolen from a building during an air raid. It was held that the theft and not the air raid was the real cause of the loss. The air raid facilitated the theft, but it was the theft that was the cause of the loss.[74] These principles may be relevant to such incidents as looting following hurricane damage, particularly where, as is usual, riot, civil disturbance and similar events are excluded from the insured perils.[75]

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71 See, for instance, *Glengate-KG Properties v Norwich Union* [1996] 1 Lloyd's Reports 614.

72 *Yorkshire Water Services v Sun Alliance & London* [1997] 2 Lloyd's Reports 21.

73 As explained by Lord Sumner in *Becker, Gray & Co. v London Assurance* [1918] AC 101.

74 See also *Marsden v City & County Insurance* (1865) LR 1 CP 232 concerning a riot following a fire.

75 See, for instance, the unreported Jamaican case of *West Indies Alliance Insurance Company v Jamaica Flour Mills* (PC 24 of 1998), concerning Hurricane Gilbert.

If it can truly be said that there are two real causes of a loss, discovering the proximate cause may not be an easy matter, but may be critical if only one of the causes is an insured peril.[76] Of course a policy may specifically address the question, for example by providing that loss be caused by a particular cause 'independently of all other causes' or words to that effect.[77]

Law of the Contract

Before considering the assessment of claims it is necessary to consider the proper law of the contract. Most cross-border contracts, such as an insurance contract made between a foreign-based insurer and a Caymanian insured, might be expected to contain an express term nominating the proper law of the contract. In the absence of such a clause it is for the court in which any claim is brought to decide whether it has jurisdiction and what the proper law of the contract is.[78] However, s 7(2) of the Insurance Law of the CI provides:

> Every contract of domestic business shall be subject to the jurisdiction of the Courts of the Islands, notwithstanding any provision to the contrary contained in such contract or any agreement related to such contract.

The subsection goes on to require every licensed insurer to have a nominated resident to take service of proceedings. Accordingly, it appears that the litigation of claims in the CI will be subject to the jurisdiction of the Grand Court in the CI.

The Claims Procedure

Time of claim

Most policies will expressly require the insured to claim for loss within a reasonable time of the relevant event. The question then arises whether the provision in respect of notice is a warranty or a condition precedent, failure to comply with which would be a breach of the duty of utmost good faith, or otherwise a warranty debarring the claim. It is a question of construction in every case whether such a time provision is such a fundamental term. In most cases these will be fundamental terms and failure to comply may permit the insurer to repudiate cover.[79] However, an insurer may choose not to operate the term with full rigour in a particular case.

Arbitration

Almost all commercial policies provide for arbitration or some other form of dispute resolution in default of agreement on liability and/or quantum of loss. Most such clauses provide that a claim must be submitted to arbitration before it can be litigated in court. Such a clause

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76 For an extreme example see *Leyland Shipping v Norwich Union* [1918] AC 350.

77 For an example see *Jason v Batten* [1969] 1 Lloyd's Reports 281.

78 See *MacGillivray* at paras 13–17ff.

79 See for example *Adamson v Liverpool London & Globe Insurance* [1953] 2 Lloyd's Reports 355.

is called a *Scott v Avery* clause after the case of that name.[80] In the CI, domestic arbitrations are subject to the Arbitration Law (2001 Revision). Whether the arbitration clause refers to disputes over liability in principle or only the quantum of loss, the courts will normally stay any attempt to litigate the relevant question in court until the arbitration process has been exhausted; see s 6 of the Arbitration Law. This Law also provides for certain aspects of procedure, appeals to the Grand Court, costs, interest and fees.

The Quantum of Claims

It is well established that a claim under an insurance contract is treated as a claim for damages for breach of contract[81] even where the insurer admits liability. The insurer's promise to pay is categorised as a promise to prevent the insured from sustaining loss so that an action for damages for breach of contract arises upon the occurrence of the loss.[82]

The first relevant question concerns the time at which the claim arises. It is normally the occurrence of the event triggering the claim that is treated as equivalent to the breach of contract by the insurer and starts the relevant limitation period, which will normally be six years: see s 7 of the Limitation Law (1996 Revision) in the CI.[83]

Delay

The next important principle is that damages are not awarded for a failure to pay damages so that, subject to any statutory interest on court claims,[84] no damage is payable in respect of the delay between notification of a claim and its settlement.[85] Accordingly, an insurer may drag his heels in settling a claim and even if the delay causes further damage to the insured's business or personal interests the insurer will not be liable for loss caused by the delay. Accordingly, it is important for the insured to be in a position to give all relevant information to the insurer and assessor and to chase them during the negotiation of the claim.

Total and partial loss

An insurance contract is a contract of indemnity. In the absence of express provision it follows that the insured can never recover more than the maximum sum expressly stated in the policy, usually referred to as the 'sum insured'. Nor can the insured recover more than the relevant property is actually worth at the time and place of loss. Accordingly, the recoverable amount will be the second-hand or resale value of the goods in question with no recovery of sentimental value or emotional or other loss caused by the event in

80 (1856) 5 HLC 810.

81 See, most recently, *The Fanti and the Padre Island* [1991] 2 AC 1.

82 Which makes it all the more surprising that the costs of prevention of damage may not be recoverable since they fit neatly into the concept of mitigation of damage.

83 For the latest statement to this effect, see the judgment of Potter LJ in *Virk v Gan Life Holdings* [2000] Lloyd's Reports IR 159 at 162.

84 See in the CI the Grand Court Rules 1995 (as amended).

85 For an extreme example of the unfairness of this principle see *Sprung v Royal Insurance* [1999] Lloyd's Reports IR 111. See also *MacGillivray* at paras 19–70.

question.[86] This principle is always subject to contractual variation and many chattel policies now provide 'new for old' cover which will entitle the insured to replacement value, albeit at significantly higher premiums.

Total loss

In the case of land, total loss is rare. There is accordingly little English authority on this event. However, hurricane damage may give rise to claims of this kind, particularly where foundations, sand and subsoil have been washed or blown away. As has already been pointed out, many policies expressly exclude cover of land itself, but in other cases the insured may be able to recover lost value unless they are compelled by the terms of the policy to reinstate or the insurer exercises its invariable option to reinstate, in which case nice questions may arise as to whether it is more cost effective to reinstate or to indemnify the loss.

In *Leppard v Excess Insurance Company* [1979] 1 WLR 512, the insured purchased a cottage which was worth £4,500, including site value, when it was burnt down, but which would have cost £8,000 to rebuild. On the evidence the insured never intended to live in the cottage but purchased it as an investment for resale. The English Court of Appeal held that the loss was the market value of the cottage, that is what the insured lost by not being able to sell it. The judgments indicate, however, that in the normal case of the insured who lives in, or otherwise occupies, his home, office or factory, the measure of indemnity will be the cost of rebuilding because otherwise the actual loss will not be made good.

Partial loss

In the case of partial loss, the measure of damage based on market value is generally inappropriate because the insured can go into the market and obtain restoration to the pre-loss position with a partly damaged property. Therefore the basis for the indemnity ought, where the property is capable of being repaired, to be the cost of repair, less perhaps any betterment.[87] If the property in question is not capable of repair, then the court has to work out the difference between value before and after the loss.[88]

Suppose the top floor of a building has been damaged to such an extent that, although the bottom half is more or less intact and usable, it is necessary to demolish the remaining part of the building in order to start again and restore the house to its original condition. In *Leppard*, would the insured have been entitled to the costs of repairing the cottage that might well have been more than the market value of the property as a whole? It appears that the fact of the insured's non-occupation in that case was crucial and that if it had been his home he would have recovered the otherwise excessive costs of repair. This problem is likely to arise in many cases in the CI. In summary, the principle appears to be that in the case of a partial loss, damage is assessed on the cost of repair or reinstatement save where the insured does not genuinely intend to reinstate.[89]

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86 For an extreme example see *Richard Aubrey Film Productions v Graham* [1960] 2 Lloyd's Reports 101.

87 For betterment see *Reynolds v Phoenix Assurance* [1978] 2 Lloyd's Reports 440.

88 See *Quorum v Schramm* [2002] Lloyd's Reports IR 292, which concerns damage to a valuable painting.

89 An interesting parallel arises in the law of landlord and tenant where damages for dilapidations are limited to actual damage to the reversion at common law (and in England by statute under s 18 of the Landlord and Tenant Act 1927).

In *Reynolds v Phoenix Assurance* [1978] 2 Lloyds Reports 440,[90] the Claimants bought an old maltings in 1969. Subsequently, on professional advice, the sum insured was increased to cover the likely cost of reinstatement in the event of a total loss and at the material time the sum insured was over £500,000. The Claimants had a sound business reason for purchasing the building: it was not a speculative investment. A fire destroyed about 70% of the building. This was clearly a partial loss. The insurer elected not to reinstate as it was entitled to under the policy, but it was accepted that the Claimants intended to reinstate. There were three possible bases for indemnity:

(1) Market value, which would be difficult to assess, there being no ready market for commercial buildings like the maltings in question, but which would probably be far less than the cost of reinstatement;
(2) Equivalent modern replacement value, namely the cost of building a modern building for the purposes of the Claimants, where it would not be commercially sensible to retain the old building. Again this would be considerably less than the cost of reinstatement;
(3) The cost of reinstatement, which was easily the most expensive option.

The judge held that the Claimants were entitled to the third option, namely the full cost of reinstatement, on the basis that they had a genuine intention to reinstate and that this would be the only way to give them a genuine indemnity, less an allowance for betterment. This case neatly illustrates the relevant considerations in the case of a partial loss or destruction of real property where the insured is not entitled automatically to the cost of reinstatement,[91] but has a genuine intention to reinstate.

Where the insured has only a limited interest he will normally only receive an indemnity up to the value of his own interest unless he has also bound himself to reinstate by covenant, as in *Re King* [1963] Ch 459.

Under-insurance and average

Because of the effects of inflation and inadequate valuation or consideration of the values of individual items put on risk, the property insured is often under-valued. If so, the insurer may be entitled to avoid the policy or all liability under it on the basis that the under-valuation was a breach of the insured's duty of disclosure under the duty of utmost good faith and/or a breach of warranty.[92] The terms of the policy may have to be construed in such a way as to provide that the initial estimate of value put on the property by the insured was a warranty properly so called. However, it is believed that insurers rarely attempt to avoid all liability in the case of under-insurance, but instead rely on the principle of average.

In the case of a total loss, the maximum recoverable will be the sum insured. In the case of partial loss, and if the policy is subject to average, the insured will recover only on a *pro rata* basis. He is deemed to be self-insured with respect to the balance. Many policies contain such 'average' or 'insured his own insurer' provisions. If a house worth $600,000 is insured, subject to average, for $400,000, the insured will be entitled to only two-thirds of any loss. Commercial policies generally contain express average clauses and it has been suggested that the principle of average would be implied into commercial policies on

90 See also *Pleasurama v Sun Alliance & London* [1979] 1 Lloyd's Reports 389.

91 See this case and *Leppard*, above.

92 See, for instance, *Economides v Commercial Union Assurance* [1998] QB 587 at 603.

goods.[93] However, average clauses are less usual in household policies except those issued by Lloyd's underwriters and the principal of average will not normally be implied in a household policy.[94]

Subject to average clauses are a matter for commercial negotiation. There is nothing to prevent an insurer from proffering such a clause. Where, as in the case of the Strata Title Law of the CI, statutory obligations are imposed on property owners to insure to replacement value, that obligation can only be complied with if the insured insures to replacement value without average or is astute enough to ensure that the sum insured is a full valuation if the policy is subject to average. This is plainly a trap for the unwary. In the light of the statutory obligation on strata title corporations in the CI to insure to replacement value, the insured may have a claim in negligence against a broker who acted in procuring a subject to average policy in these circumstances.

Excess and deductible clauses

Many property and household policies contain excess clauses or deductibles whereby the insured is to bear an initial amount of any loss expressed as an amount of money or a stated percentage of loss. This is another example of the insured being deemed to be self-insured.

Reinstatement

Property insurance contracts invariably provide an option in favour of the insurer to reinstate or repair. Reinstatement is the conventional term, but it includes rebuilding, replacement or repair, as appropriate. Once the insurer has made an election the insurer is bound by it and effectively enters into a building contract enforceable by the insured. Modern policies often qualify the insurer's obligation once the option is exercised by providing that reinstatement will be 'as circumstances permit and in a reasonable sufficient manner' or words to that effect. This will cover impossibility of performance caused by planning or modern building regulation provisions which would not have been in force at the time when the property was originally built. In default of performance the insured is entitled to damages, but will not be granted specific performance.[95] However, the insurer is bound to fulfil the obligation once he has elected even if the costs turn out to be more than originally estimated or even than the sum insured in the policy. It is likely that insurers will be careful before electing to reinstate hurricane damage in the CI, bearing in mind building costs and relative values.

In some cases the insured has an obligation to reinstate, for instance where a tenant covenants to reinstate in a lease; but in the absence of an express provision the courts will not usually imply one, even where the insured has covenanted to insure.[96]

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93 *Carreras v Cunard* [1918] 1 KB 118.

94 *Sillem v Thornton* (1854) 3 E&B 868.

95 *Home District Mutual Insurance v Thompson* (1847) 1 E&A 247. Compare the position in the law of landlord and tenant where both landlord and tenant can now obtain specific performance of repairing covenants. See *Jeune v Queen's Cross Properties* [1974] Ch 97 and *Rainbow Estates v Tokenhold* [1998] 2 All ER 860.

96 See *Mumford Hotels v Wheeler* [1964] Ch 117, where the tenant had an interest in the insurance monies, but no obligation to reinstate. In England, s 108(2) of the Law of Property Act 1925 gives a mortgagee a statutory option to compel the mortgagor, who is insured and has received money, to use it on reinstatement, but it is not believed that this provision applies in the CI.

Assessment

Where it is necessary to make complex calculations in order to decide the amount of the indemnity due to the insured, policies sometimes provide for an assessor to be appointed whose conclusions are to be binding on both parties. Such an assessor is independent, although he may apparently be called as a witness and cross-examined in proceedings in order to determine whether he made the assessment in accordance with the provisions of the policy.[97] The assessor's position is probably more analogous to that of an expert valuer rather than an arbitrator, whose certificate is *prima facie* unchallengeable by the parties.[98]

Quite apart from formal assessors, insurers invariably appoint their own assessors, who are of course agents of the insurer rather than independent third parties, to value and calculate the insured's claims. It is understood that concern has been expressed in the CI as to the degree to which such assessors can be interrogated by the insured or the insured's representatives and the extent to which the assessor's findings may be disclosable to the insured. In the absence of express provisions in the contract, the documents would be the property of the insurer and not disclosable until the normal provisions of discovery in legal proceedings applied and any duty to disclose would depend on whether the insurer could claim privilege. It is doubtful whether, in arbitral or court proceedings concerning the quantum of a claim, an insurer could claim privilege over the assessor's working papers, but that may be small comfort to the insured if there is a desire to settle the claim before such proceedings.

Double Insurance and Contribution

Contribution is a principle designed to prevent unjust enrichment and applies as between insurers. Commercial insurance policies invariably contain rateable proportion clauses which provide that if there is any other insurance on the property or the risks covered by the policy the insurer will not be liable to pay or contribute more than the insured's rateable proportion of any loss or damage. This means that the insured will be prevented from recovering all of the loss from one insurer. Apart from rateable proportion clauses, policies may contain other provisions in relation to double insurance. Sometimes insurers purport to disclaim liability completely where the property in question is covered by other insurance, but such clauses are usually construed by the courts to provide for contribution between insurers.[99]

Subrogation

A final fundamental principle of insurance law, correlative to the principle of indemnity, is the insurer's right of subrogation. This is a restitutionary remedy designed to prevent the insured from receiving anything more than a full indemnity. It applies to all contracts of indemnity, including property insurance. The principle prevents the insured from making a

97 See *Recher v North British & Mercantile Insurance* [1915] 3 KB 277.
98 See *Frewin v Poland* [1968] 1 Lloyd's Reports 100.
99 See the English Court of Appeal in *National Employers' Mutual v Hayden* [1980] 2 Lloyd's Reports 149.

profit from the loss and permits the insurer to step into the shoes of the insured[100] and to pursue claims against third parties in the name of the insured if such claims might diminish the insurer's loss.[101]

Conclusion

At the Commonwealth Law Conference in London in September 2005, the Attorney General of Barbados addressed the lack of, and need for, a pan-Caribbean body to monitor and coordinate the prevention and remedy of hurricane damage. The need is acute because the problem is more or less predictable and more or less inevitable. The difficulty is that in the Caribbean, in particular, there are numerous small jurisdictions individually unable to cope with the level of loss that is likely to occur on an irregular basis.

Nevertheless, it is to be hoped that this article, which is intended to be a relatively simple analysis of the relevant legal problems, may go some way to identify the common themes that arise when hurricanes strike. A code of practice for insurers might emerge from those themes. Governments could co-operate on consequential problems, such as the need for anti-inflationary measures in the aftermath of hurricanes, sometimes called anti-price-gouging, to use the colourful American phrase. The drafting of conveyancing documents, particularly those concerning common property covered by strata titles, could be modified to take account of the need for flexibility in rebuilding. Above all, the exchange of information and the pooling of ideas may avoid the ad hoc and ill-thought out measures that often follow natural disasters.

This article is not intended to be a complete treatment of modern insurance law and should not be read as such. It is intended to highlight those issues that are considered to be likely to give rise to difficulties in the case of catastrophic storm damage such as the aftermath of Hurricane Ivan in the CI. Doubtless there will be other relevant issues not covered by this article, for which omission the author apologises.

100 The literal meaning of the word 'subrogation'.

101 For a full treatment of the principles of subrogation see *MacGillivray* at pp 568–634.