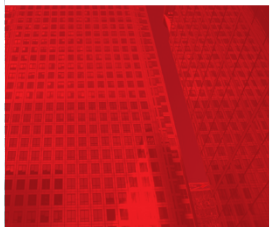
Insurance/
Reinsurance

March 2014

INSURANCE BULLETIN



Negotiating the jurisdictional maze

Insurance Company of the State of Pennsylvania (ICSP) v Equitas Insurance Company Ltd (EIL)

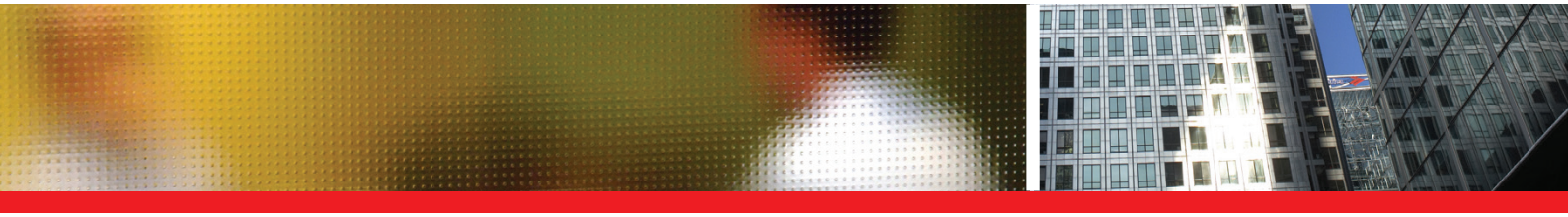
This case illustrates the complex jurisdictional issues and consequent tactical considerations which may arise when an insurance or reinsurance contract does not contain clear provisions as to jurisdiction.

A dispute arose under certain reinsurance contracts pursuant to which EIL (as transferee of the liabilities of the Lloyd's syndicates originally subscribing to those contracts) reinsured ICSP.

The reinsurance contracts did not contain clear provisions as to jurisdiction. In order to protect its position, and despite the negotiations between the parties only having contemplated English proceedings, ICSP commenced proceedings in both the English Commercial Court and the New York Court. ICSP then wrote to EIL clarifying that it only intended to pursue the English proceedings if for any reason the New York proceedings could not proceed, and asking EIL to agree to a stay of the English action. EIL refused and so ICSP applied to the English Court for a stay. EIL made its own application in England for an anti-suit injunction against the New York proceedings.

EIL's application for an anti-suit injunction failed. Whilst ICSP's conduct in launching its claim in New York despite no previous mention of any such intention was, in the Court's view, "most unsatisfactory", EIL's detrimental reliance on the impression created by ICSP that only English proceedings were in contemplation was not sufficiently prejudicial to make it unjust for ICSP to sue in New York.

Nor, however, was the Court prepared to grant ICSP's application for a stay of its English proceedings. The manner in which ICSP had negotiated with EIL by reference to contemplated English proceedings without informing EIL that it would sue in New York if negotiations failed, meant that ICSP had, in the Court's view, failed to show that this was an exceptional case in which ICSP as claimant should be granted a stay.



As a result, both sets of proceedings continue.

The absence in this case of any clear provisions as to jurisdiction was at least partly explained by the age of the contracts and the incompleteness of the surviving documentation. Those negotiating insurance and reinsurance contracts in today's market will of course ensure, with the assistance of their advisers, that clear, appropriate and effective provisions as to governing law are included, so as to prevent issues such as these arising in the event of future disputes.

In the absence of such provisions, ICSP was forced to take those steps which it considered necessary to pursue its claim. However, the case illustrates that parties faced with such circumstances must protect their own interests whilst at the same time recognising the need to conduct matters in a manner which will be regarded favourably, should it become necessary to seek the discretionary assistance of the Court. This will involve keeping the other party sufficiently informed of one's intentions, on the basis that, as the Court put it in this case "generally speaking, parties to litigation, threatened or on foot, are entitled to know where they stand with the opposition".

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hfw Directors' defence costs: NZ Supreme Court allows Bridgecorp appeal

We have previously reported on the high profile *Bridgecorp* decisions of the High Court and Court of Appeal of New Zealand. The NZ Supreme Court (that country's highest court) has recently provided the latest instalment of this saga in a decision[1] which was an unwelcome Christmas present for directors and officers (and other professionals insured under defence costs-inclusive liability policies) in New Zealand who may not now be able to access defence costs cover where the amounts claimed exceed the limits in combined limit policies.

This decision is also of significance to directors and officers, other insured professionals and insurers operating in Australia, where certain States and Territories (New South Wales, Australian Capital Territory and Northern Territory) contain equivalent legislation to that considered in *Bridgecorp*.

In our October 2013 Bulletin, we said that the earlier *Bridgecorp* NZCA decision and, in particular, the decision of the NSWCA in *Chubb Insurance Company of Australia Limited v Moore*[2] would provide comfort to Australian directors that they should be able to access their cover for defence costs. We noted, however, that Australian directors may wish to maintain any arrangements put in place to deal with the potentially adverse consequences of the original *Bridgecorp* NZHC judgment (such as separate limits or separate policy coverage for defence costs) until the result of the *Bridgecorp* NZSC appeal was known and assuming no change in Australia to the position stated in *Chubb*.

In light of this recent *Bridgecorp* NZSC decision and the pending special leave application to the High Court of Australia in *Chubb*, we consider that these structures should be maintained (or entered into) where there is a prospect of claims being brought against directors in New Zealand and, for the time being, in Australia until the *Chubb* appeal is determined and the position in Australia is confirmed or clarified.

Background

The relevant legislation in NZ, NSW, ACT and NT[3] creates a statutory "charge" over insurance monies which are, or may become, payable in respect of an insured's liability to pay damages or compensation.

The precise scope and effect of this legislation has, however, been difficult to determine with the NZHC (but not the NZCA or the NSWCA) holding that a "charge" under the relevant legislation prevented D&O insurance policy funds being advanced to meet the directors' defence costs following notification of the existence of the charge.

In contrast, the NZCA and NSWCA found that a charge under this legislation cannot apply to defence costs paid by insurers before liability has been determined. In *Chubb*, it was also held that the relevant NSW legislation does not apply to claims brought outside NSW. This was not an issue in *Bridgecorp*.

1 BFSL 2007 Ltd (in liquidation) v Steigrad [2013] NZSC 156.

2 [2013] NSWCA 212.

3 Section 9 of the NZ Law Reform Act 1936, which is substantially mirrored in NSW by section 6 of the Law Reform (Miscellaneous Provisions) Act 1946, in ACT by section 206 of the Civil Law (Wrongs) Act 2002 and in NT by section 26 of Law Reform (Miscellaneous Provisions) Act.

At present this minority view remains the position in Australia but, as noted above, *Chubb* is the subject of a pending application for leave to appeal to the High Court of Australia.

NZ Supreme Court decision

The former directors of *Bridgecorp* are being sued for damages in excess of NZ$340 million for breach of their director duties. They have been convicted of offences under the *Securities Act 1978* for breach of statutory duties.

There were two relevant insurance policies taken out by *Bridgecorp* with QBE – one for statutory liability with a limit of $2 million (exhausted in defence of the *Securities Act* proceedings), and the other for D&O liability with a limit of $20 million, which provided that QBE would advance defence costs as and when those costs were incurred if QBE had given its prior written consent.

The majority (3:2) followed the NZHC decision that the charge attaches at the time the event giving rise to the claim occurs, even if the liability to third party claimants has not yet been determined. Thus, where the claim is for an amount exceeding the limit of liability under the policy, reimbursement of directors' defence costs can only be made at insurers' risk of paying additional sums over the policy limits if, once the claim has been determined, there are insufficient insurance monies remaining to meet the third party liability. The majority were influenced by a view that depletion of the potential monies available to a successful third party would effectively (and unfairly) require the claimant to fund an unsuccessful defence.

In contrast, the minority followed the decision in *Chubb* that the charge should only attach to insurance monies that would be payable in respect of the insured's liability to pay damages or compensation, and that the charge only became fully operational once that liability has been determined. Payment of amounts due before that time can be made in accordance with the contract of insurance. To find otherwise would be altering the contractual rights as between the insured and the insurer and impacts on their ability to defend the claim.

At present, this minority view remains the position in Australia but, as noted above, *Chubb* is the subject of a pending application for leave to appeal to the High Court of Australia. We will report further on this in due course.

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Suspension of Iran sanctions: a golden opportunity?

The recent EU and US suspensions of certain sanctions against Iran have caused companies to consider carefully their policy on trade with Iran and, as a result, insurers, reinsurers and brokers will increasingly find themselves asked whether insurance can now be provided for trade with Iran.

As ever with sanctions programmes (and particularly sanctions against Iran), the position is incredibly complex and our January 2014 Briefing aims to summarise the key developments.

The key messages for insurers, reinsurers and brokers are as follows:

- The great majority of restrictions remain in place and are unaffected.
- The EU and US asset freezes are largely unaffected, save in the case of a small number of Iranian trading entities in the case of certain trades.
- Insurance in connection with some trades (eg transport of crude oil to China, India, Japan, Korea, Taiwan and Turkey, and purchase and transport of petrochemicals) is now permitted, provided various restrictions are satisfied.
- The financial thresholds under EU rules on transfers of funds have been increased.

Regulators, particularly those in the US, have stressed that the suspensions do not mean that Iran is now "open for business" and they have made clear that they will enforce the restrictions which remain in place. Any insurers, reinsurers or brokers who are asked to insure trade with or related to Iran therefore need to conduct

thorough due diligence and obtain appropriate contractual protection to ensure they do not inadvertently violate the onerous sanctions which remain in place.

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Any insurers, reinsurers or brokers who are engaged in trade with or related to Iran therefore need to conduct through due diligence and obtain appropriate contractual protection to ensure they do not inadvertently violate the onerous sanctions which remain in place.

The blame game

The comments below appeared as an HFW contribution to an insurance article for issue 151 of *The Superyacht Report*, investigating where the blame should be placed when discrepancies occur during paint jobs. This section is re-published with permission.

For the owner of a superyacht, the focus is on the aesthetics of the external hull coatings and quality of finish. Generally, the technical specification sets out the detailed provisions on the yacht's paint coating, including but not limited to the chosen paint system, standard of workmanship, surface preparation, gloss levels, acceptance criteria, etc. It is therefore important that the specification dovetails with the construction agreement (particularly with regard to warranty and performance characteristics of the paint). The construction agreement will include warranties from the builder and while the builder's warranty might include paintwork, it is not uncommon for it to be dealt with by a stand-alone warranty, which might be given directly from the paint applicator or paint supplier.

With the cost of rectifying defective paint installation running into, in some cases, several million euros, clear responsibility for these liabilities is something that both builders and owners will need to get right. The benefit of having suitable insurance cover in place is that if a successful claim is made under the policy, the assured will be indemnified for its loss by the insurer, and avoid any delays in pursuing the contractors or manufacturers for the losses, which will be the insurer's responsibility as per their subrogation rights.

Most yacht builders will have their own all-risk builders' insurance in place.

The benefit of having suitable insurance cover in place is that if a successful claim is made under the policy, the assured will be indemnified for its loss by the insurer.

However, if the cover is deemed to be insufficient, then the owner/buyer should consider taking out his or her own insurance.The most common policies are based on the Institute Clauses For Builders' Risks (cl.351), which is basically an 'all risks' policy, covering every kind of accident or fortuity, but does not include the cost of renewing faulty welds, and whilst loss or damage arising from faulty design is usually covered, the actual object itself is not normally covered. Also, costs incurred by reason of betterment or alteration in design are not covered. The cover also excludes the statutory exclusions for wilful misconduct, ordinary wear and tear, and any consequences of delay in progressing or completing the building works. It is therefore important for an owner to understand what a builder/ sub-contractor is liable for under the warranties as well as any applicable insurance cover that may be available. In short, the role that insurance has to play to both builders and owners should not be overlooked.

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Australian bushfires: application for security for costs dismissed

Matthews v SPI Electricity Pty Ltd & Ors[1]

Our December 2013 Bulletin reported on a decision by the Supreme Court of Victoria using its discretion to dismiss an application brought in a class action to exclude evidence which had been obtained as a result of trespass, which ordinarily would be inadmissible owing to a breach of Australian law.

In the same case, relating to one of the 2009 *"Black Saturday"* bushfires, a defendant brought an application for security for its costs against not only the lead plaintiff, but also against the insurers of a substantial number of group members of the class action. In dismissing the application, Derham AsJ held that the power of the court to order the insurers to provide security for the costs, assuming it to exist, was not enlivened because there was no evidence that the insurers would not be able to pay the defendant's costs, if ordered to do so on judgment.

An application for security for costs by a defendant in a proceeding seeks an order that security be given, usually by the plaintiff but in more limited cases by a non-party, in respect of sums expected to be incurred by the defendant in defending the proceeding. There are many different factors which a court may take into account when determining whether to exercise its discretion in granting an order for security for costs. However, the central factor in determining whether the court's power is enlivened is whether the defendant has demonstrated that there is a real risk that the plaintiff will not be able to meet an order for costs on judgment at the conclusion of the trial.

Background to the application in the class action proceeding

The application for security for costs in this case was made in a class action proceeding involving claims for loss and damage arising out of the *"Kilmore East"* fire, one of the *"Black Saturday"* bushfires which occurred in February 2009 in Victoria, Australia. It is estimated that more than 8,000 claims have been made in the class action, a significant proportion of which involve subrogated claims for property loss and damage in respect of which numerous insurers (group member insurers) have made payments to members of the class action group.

The application for security for costs was made by the first defendant in the proceeding (the utility), the owner and operator of an overhead electricity powerline which is alleged to have failed, resulting in the ignition of the Kilmore East fire. The application was made in April 2013 in circumstances where the proceeding has been on foot since 2009. The trial, which involves five defendants, commenced in early March 2013 and remains ongoing. Derham AsJ observed that the proceeding has involved (and continues to involve) huge expense by all parties, including the utility.

Prior to the application, the utility obtained from the plaintiff:

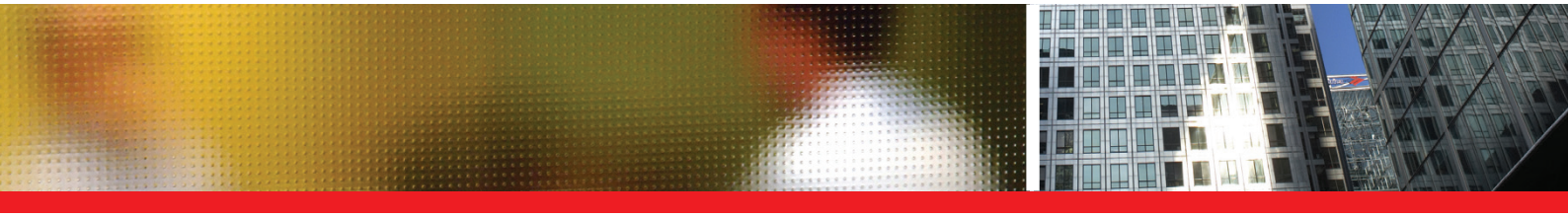
1. A table detailing the amounts sought to be recovered by group member insurers in respect of claims paid to insured persons who had suffered economic loss and property damage loss.
2. Copies of two agreements (insurer agreements) with two different groups of the group member insurers (the funding insurers) pursuant to which those funding insurers agreed to contribute to the disbursements incurred by (but not the costs of) the plaintiff's solicitors in the proceeding. The insurer agreements also provided for the establishment of a consultation committee to allow for the funding insurers to have some input into the decision-making processes concerning the proceeding.
3. Five conditional costs agreements between the plaintiff's solicitors and five other group member insurers.

The utility pressed four alternative forms of orders against a variety of group member insurers, or the plaintiff, to provide security for its costs in the proceeding. The orders sought were complicated but, in essence, the utility sought orders that the group member insurers provide security for its future disbursements:

1. In proportion to the sums each group member insurer sought to recover in the proceeding as a percentage of the total sum

The application for security for costs was made by the first defendant in the proceeding (the Utility), the owner and operator of an overhead electricity powerline which is alleged to have failed resulting in the ignition of the Kilmore East fire.

1 Ruling No 9 [2013] VSC 671



sought to be recovered by all group member insurers.

2. By reference to the sums paid by the funding insurers in reimbursement of disbursements under the insurer agreements.

The application as against the plaintiff

In dismissing the application in relation to the plaintiff, Derham AsJ found that it was not appropriate for the court to make an order for security (even though it was clear that the plaintiff would not be able to pay the utility's costs if ordered to do so) for a number of reasons including: the lateness of the application at a time well after the commencement of trial, the prejudice to the plaintiff in making such an order at that late stage in the proceeding, and the public interest in a group proceeding of this size.

The application as against the group member insurers

In dismissing the application with respect to the group member insurers, Derham AsJ found that the power of the court to order a group member insurer to provide security costs was not enlivened because there was no suggestion that there was any risk that the group member insurers would not be able to pay the utility's costs if any were ordered to do so. This was the *"critical factor"* necessary to enliven the jurisdiction of the court to make the order to provide security for costs.

In light of the finding that the power was not enlivened, Derham AsJ did not find it necessary to reach a conclusion on the question of whether the court possesses the power to order a group member insurer to provide security for costs; he simply found that the power was not enlivened *"assuming it to exist"*. As a result, the question of whether a court has the power to make such an order remains open to be answered in another case. In relation to this question, Derham AsJ did, however, reject the submission made on behalf of group member insurers that the court does not have the power to order them to provide security for costs because they are, in effect, group members and the relevant provisions of the *Supreme Court Act 1986* (Vic) curtail the power of the court to make orders for costs against group members. His Honour found that, whilst the group member insurers stand in the shoes of group members, they are not the group members. Accordingly, His Honour stated that, *in his view*, the power to make an order for costs against the group member insurers existed, but it was unnecessary to come to a final conclusion as to the power because the power would not be enlivened in any event.

In dismissing the application with respect to the group member insurers, Derham AsJ found that the power of the court to order a group member insurer to provide security costs was not enlivened because there was no suggestion that there was any risk that the group member insurers would not be able to pay the utility's costs if any were ordered to do so.

The application by the utility is unique in that, whilst applications for security for costs have previously been made (in some cases successfully) against non-parties, including litigation funders, the utility was unable to point to any case where an order for security for costs had been made against an insurer exercising its subrogated rights. Whilst Derham AsJ did not come to a final conclusion as to the power of the court to make an order for security for costs against group member insurers, his obiter comments suggest such a power may exist.

HFW are representing the second defendant in the class action and related litigation.

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News

HFW wins Captive Review's *Onshore Law Firm of the Year Award 2014*

HFW was delighted to be presented with the *Onshore Law Firm of the Year Award 2014* at the UK Captive Services Awards gala dinner on Monday 24 February.

The UK Captive Services Awards (organised by Captive Review) are now in their second year, and recognise excellence in the delivery and management of captive insurance, and celebrate those who have excelled over the past year.

Paul Wordley, HFW's global head of insurance and reinsurance, collected the award on behalf of the firm.

The Mining Journal's Global Risk and Insurance Guide 2014

HFW recently contributed an article entitled "Legal and Insurance Considerations in the Mining Sector" to the Mining Journal's annual Global Risk and Insurance Guide 2014.

There has been an unprecedented level of losses in the mining sector in recent times. In the last five years, over US$5 billion of property damage and business interruption claims were produced to the global insurance industry on an annual premium of US$500 million–US$750 million. In this article, we highlight the considerations necessary to ensure contract and coverage certainty. We suggest some ideas to ensure effective claims handling processes in a variety of jurisdictions that could help minimise disputes between policyholders and insurers, and to identify coverage issues early to avoid protracted and distressed claims. We also provide an update on the RIMS Mining Forum Initiative, which has been working to produce a bespoke (i) mining industry claims handling protocol; and (ii) mining property damage and business interruption policy.

The full article can be read here http://www.hfw.com/Legal-and-Insurance-considerations-in-the-mining-sector-February-2014. The Mining Journal's Global Risk and Insurance Guide 2014 can be viewed at http://www.hfw.com/Mining

HFW has hosted or participated in a range of industry events during February and March. Below is a short summary of each.

Market representatives visit

In February 2013, Geoffrey Conlin visited market representatives in London. HFW Partner Craig Neame, Senior Associate Geoffrey Conlin and Associate Matthew Wilmshurst presented to various underwriters and claims managers handling underwriting claims and issues relating to ports and terminals in Latin America.

Strategic Claims Conference

HFW Partner James Clibbon chaired the Strategic Claims Conference on 4 March. HFW sponsored the morning session on large complex commercial risks.

For more information, please visit http://www.theinsurance-network.co.uk/scc14programme.aspx

Cyber Liability Seminar

HFW hosted a seminar in Dubai focusing on data breach and cyber liability issues. Cyber security is a fundamental requirement for the conduct of global business. An understanding of cyber risk is imperative to ensure that digital assets and activities are properly protected.

The seminar was chaired by HFW Partner Sam Wakerley and featured presentations from HFW Consultant Peter Schwartz, HFW Associate Luke Hacker and guest speaker JLT Partner Peter Hacker. The seminar addressed the following areas:

- Identifying "data" held and processed and the applicable regulations.
- Identifying the risks and the types of claim which have arisen.
- Preparing for and dealing with a significant breach.
- How insurance helps to provide solutions.

Conferences and events

3rd Rio de Janeiro Reinsurance Conference
Rio de Janeiro
8–9 April 2014
Attending: Geoffrey Conlin

Lloyd's Brazil Meet the Market 2014
Rio de Janeiro
10 April 2014
Attending: Geoffrey Conlin

ACI – Run-offs and Communications Conference
New York
23–24 April 2014
Presenting: Costas Frangeskides

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