CITY OF LONDON LAW SOCIETY

INSURANCE LAW COMMITTEE

Minutes of a Meeting held at the offices of Allen & Overy at 5pm on Wednesday 11th December 2007

Present:

Ian Mathers (Chairman) – Allen & Overy
Christian Wells - Lovells
Geoff Lord – Kennedys
Beth Dobson (for Glen James) - Slaughter & May
Michael Mendelowitz – Norton Rose
Helen Clark (for Richard Spiller) – Kendall Freeman
Stephen Lewis – Clyde & Co
Anna Tipping – Linklaters
Terry O'Neill – Clifford Chance

Apologies for absence:

Martin Bakes – Herbert Smith
Kenneth McKenzie - Davies Arnold Cooper
Martin Mankabady – Lawrence Graham
Catherine Hawkins - Berrymans Lace Mawer

1. The minutes of the meeting of 19th September were approved.

2. Insurance Contract Law: Law Commission

The Chairman noted that the Committee's response to the Commission's CP on misrepresentation, non-disclosure and breach of warranty had now been submitted. BD said that their next issues paper, on insurable interest, was due by the end of the year. MM indicated that he would be happy to take the lead in preparing a response from the Committee on this subject, depending upon the deadline for reply and other pressures on his time, and CW said that he would also be happy to do so. It was agreed that the Chairman should progress the matter when the issues paper emerged. A meeting of the Contract Law Working Party might be planned to discuss the paper, perhaps around mid-February.

3. Reinsurance Directive

The Treasury's proposals for further implementation of the Reinsurance Directive have now been implemented by regulations. The Chairman noted that the Committee had been largely supportive of those proposals, subject to a few including, in the case of Part VII transfers, on the proposed procedures for notification of parties with a material interest. He had not yet had an opportunity to review the regulations in detail but, as regards notification, it might be that the Committee's comments would flow into the Treasury's earlier consultation on proposed amendments to the Part VII procedure (on which the Committee had also commented). As to this, the Treasury had not yet responded. MM mentioned that the question had been raised recently in connection with the amendments for Lloyd's Names, which appeared to be required for the proposed transfer of their liabilities to National Indemnity Company. It was not clear what was holding the amendments up.

4. FSA procedure on Part VII transfers

The Chairman said that he had been unable to attend a meeting convened by the FSA to discuss their proposals for formalising the procedures for their intervention on Part VII transfers. However, Glen James had said that his colleague Oliver Wareham attended. There appeared to have been general agreement that the FSA's idea of setting an effective date for transfer schemes to allow for the possibility of an adjournment of the court hearing was likely to produce unnecessary delay, and there were one or two High Court judges attending (including David Richards) who thought that the template for the FSA's report to the court was too heavy handed. The FSA had agreed to reflect on the discussion and produce revised proposals.

5. Rome I

The Chairman reported that developments on this project had speeded up and the draft regulation had been approved by the European Parliament. He understood that the draft as approved by the Parliament had included some wording on insurance to replace the current provisions in the EU insurance Directives. It seemed that this wording would maintain freedom of choice for large risks (as well as reinsurance), and if so it should not be of too much concern to the Committee. However, HMCS had convened a stakeholders meeting for 14th January which he would attend, and would report further thereafter.

6. EU Common Frame of Reference

The Chairman reported that he had received no recent information on this project, and expected that further developments would depend upon the reports from academic experts, which were due around the end of the year.

7. Solvency II

The Chairman reported that he had attended the most recent conference on this subject convened by CEIOPS. Mostly this had focused on the calibration of the MCR and SCR following the publication of the committee's report on QIS 3. In sum, it appeared that considerably more work was required to ensure that these measures hit a satisfactory level. But there had been some discussion of proposals in the draft Directive for allowing groups of companies to determine where within the group they could locate regulatory capital. These proposals appeared to have gained general acceptance on condition that there were adequate arrangements for the transfer of capital to any individual company in distress. The Chairman suggested that some lessons could be drawn fro Lloyd's arrangements for parent company covenants. However, he had the impression that these covenants were now out of vogue. CW confirmed: Lloyd's sponsors typically wished to limit their liability so far as possible and the preferred means of providing security for syndicate underwriting was now by LOC. Nevertheless, it was agreed that the operation of such covenants, and also the guarantees previously required by the ILU, might be usefully reviewed to see whether they could provide a precedent, including the method by which they were enforced.

The Chairman also mentioned that he had spoken briefly at the conference with a representative from the ABI, who had said that there might be a need to reconvene the ABI Legal Working Party which had looked at the text of the draft Directive. He agreed to ask the ABI what was proposed on this front, and whether there was anything to be gained by involving the Committee in the negotiations.

8. Other policy developments

CW drew attention to the draft Sex Discrimination Act 1975 (Amendment) Regulations which were intended to give effect in the UK to the EU Gender Directive 2004/113/EC. However, he did not think that these regulations were a matter of concern. The provisions on insurance are designed to fortify the existing provisions of the Act by making clear that where there are proportionate differences in an individual's premiums and benefits as a result of sex being a determinant factor in risk assessment, then these differences must be based on relevant and accurate data, and this data must be compiled, published and regularly updated. CW also noted the FSA's announcement of its intention to carry out further work in the field of commission disclosure. An independent review had concluded that the cost of mandating commission

disclosure would outweigh the benefits, but the FSA intend to publish a discussion document on the subject. TO'N commented on the amendments to the FSCS which would take effect from 1 April 2008, following the FSA's Funding Review. There are to be five broad contribution classes – deposit taking, investment, life and pensions, general insurance and home finance. There will be two sub-classes in each broad class divided along provider and distributor lines –with the exception of deposits. Each sub-class will have a limit on what it could be required to contribute to compensation claims in each year. There is however an explicit provision for cross-subsidy in so far as (a) if a sub-class (e.g. general insurance intermediaries) reaches its annual threshold, the other sub-class in their broad class (e.g. insurers) will be required to contribute to any further compensation costs and (2) a final layer of cross-subsidy will then be available from the general retail pool, through which the other broad classes support any broad class which has reached its overall threshold. There was some discussion in the Committee of the concepts of affinity and mutual financial interest on which the new model has been based, but no particular conclusions were drawn.

9. Recent court decisions

There was a discussion of the decision of the Court of Appeal in *AIG Europe v Faraday Capital* [2007] EWCA Civ 1208 concerning a claims cooperation clause in a reinsurance policy written by Faraday in respect of AIG's directors and officers' liability business. The clause required notice to be given to the reinsurer, within 30 days, of "any loss or losses which may give rise to a claim". A potential claim arose from an announcement in November 2002 by the original insured to restate its accounts, which was followed by a fall in the listed value of the insured's shares and, subsequently, class actions by shareholders against the insured and various of its directors. The insured notified AIG in late December 2002 that claims had been made against them, but AIG did not notify Faraday until 19 April 2004, following a settlement of the actions on 23 March 2004. At first instance, the judge held that the reference in the CCC to "loss" must mean actual loss which was attributable the insured's directors and that could not be proved until the actions had settled, hence AIG's notice was in time. In this, the judge followed a decision of the Commercial Court in *Royal & Sun Alliance v Dornoch* [2005] EWCA Civ 238. That was a similar case in which a class action was started following an allegation that there had been a drop in share value following an admission by the directors of the original insured that certain figures in the accounts had to be restated. However the Court of Appeal reversed the judge's decision, and distinguished the *Dornoch* case on the grounds that in that case it was arguably uncertain whether the fall in the share price had been due to the admission or to normal market fluctuation. CW pointed out that the decision in *Dornoch* frustrated the obvious purpose of the CCC, which was to give the reinsurers some control over the handling of the shareholders' claims. However, the clause appeared to have been, in effect, lifted from the typical wording for a property policy without proper thought as to its application to liability insurance and there had perhaps been a difficulty for the court to engage in the task of rewriting it. This was particularly so because the notification period in *Dornoch* was only 72 hours and there would have been arguments for rewriting that too.

SL drew attention to *Limit No 2 v Axa Versicherung AG* [2007] EWHC 2321 which involved (1) a statement by a reinsurance broker on first presentation and renewal that the reinsured would not normally write construction risks unless the deductibles were at least £500,000, and (2) a presentation by the broker on renewal of certain loss statistics. As to (1) the court found that this statement was a representation of fact which could not be substantiated since the prevailing market conditions meant that it could not be achieved, thus entitling the reinsurer to avoid (the Court appeared to have considered that while it might have been open to a reinsured to argue that a UK reinsurer should have been aware of the position regarding deductibles, this could not apply to the reinsurer in this case which was based in Germany). As to (2), the Court held that there was a breach of the duty of non-disclosure because there had been a doubling of outstanding claims between their presentation and the reinsurer's scratch which went beyond an ordinary or routine development in the claims position. Generally it was felt that this decision was reasonable, although there was some concern that the reinsured or its broker might find itself continuously reviewing presentations until it is informed that the reinsurer has made its scratch.

10. Insurance arbitration

GL responded to the Chairman's previous suggestion that there might be some mileage in the Committee looking at this subject, especially since it did not appear to be covered on any systematic basis by the Litigation Committee or any other expert committee. GL said he was uncertain whether there were in fact any areas which could be regular candidates for discussion. There were in his experience two broad categories of arbitration, the first concerning the valuation of claims, in which lawyers were not much involved and the second concerning coverage which had been comparatively rare but were growing in number, probably due in part to a perceived anti-insurer bias on the part of the courts. It would be possible to look at particular forms of arbitration clauses and for example the composition of tribunals, but he was not clear that this would yield very much. MM agreed, as regards reinsurance arbitration. The trend was to appoint three member tribunals and for the procedure to be conducted on similar lines to the procedure before a court. CW agreed: the quality of insurance arbitrators was somewhat variable but this was not something that the Committee was likely to be able to do very much about. Parties would be likely to try to select arbitrators who from previous experience seemed likely to be sympathetic to their case more than on the basis of their intrinsic abilities. HC also agreed: in her experience the main problem with arbitrators lay in the availability of potential appointees. SL also agreed: while Lord Justice Rix had recently given a talk to BILA at which he had lamented the potential impoverishment of the law resulting from an increasing trend towards arbitration, combined with its confidentiality, it was not clear how the position could best be remedied.

The Chairman said that he would reflect on the points which had been made. Maybe there were some issues which could be picked up, such as the position of non-parties, but he would take a look at what had been published and see what if anything the Committee might contribute.

11. Training

The Chairman reported that he had recently attended a meeting of Committee Chairs at which there had been some discussion of the Society's role in this field. It appeared that the Construction Committee were in the course of developing a foundation course for new entrants to construction practice and he wondered whether there would be any appetite for a similar exercise in the case of insurance. AT said she expected that the larger firms would be generally self-sufficient and the Chairman agreed that there would perhaps be more interest from smaller practices, although perhaps not exclusively. SL mentioned that Clyde & Co were soon to discuss the issue of training with the Kaplan Law School, including the possibility of 14 week elective courses on designated subjects. He agreed to report back on the results of this discussion at the next meeting, when the question could be considered further.

12. Next meeting

It was agreed that next year's meetings would be held on 11 March, 10 June, 23 September and 9 December. Mark Mankabady has kindly agreed to hold the meeting on 10 June at Lawrence Graham's offices. Provisionally, the other three meetings will be held at the offices of Allen & Overy.