PART 1
INTRODUCTION AND OVERVIEW

1.1 Our terms of reference[1] are to examine, jointly with the Scottish Law Commission, the scope and operation of the 1930 Act in the light of current law and market practices of the insurance industry.[2]

1.2 The aim of the Third Parties (Rights Against Insurers) Act 1930 was, as its long title indicates, "to confer on third parties rights against insurers of third-party risks in the event of the insured becoming insolvent ...". Before the Act, the proceeds of any insurance policy covering a liability which the insured had incurred to a third party were payable to the insured's insolvency practitioner. Once paid over, they formed part of the insured's assets and were distributed as such to his general creditors. The third party whose loss had triggered the claim against the insurer was likely only to recover a small dividend as one of those creditors.

1.3 When it was first debated in October 1929, the Bill was described as a measure which would "commend itself to all quarters of the House"[3] and this proved to be the case.

1.4 The Act gives third parties a right to claim the insurance proceeds from the insurer ahead of the other creditors. It operates by transferring the insured's rights against the insurer to a third party to whom liability has been "incurred"[4] on the happening of one of the insolvency situations set out in the Act. It also gives third parties certain rights to disclosure of policy information[5] and prohibits policy terms designed to avoid the operation of the Act[6] and settlements between the insurer and the insured reached after the transfer of rights.[7]

1.5 As we shall see, the court has held that the precondition to the transfer of rights in section 1 of the Act that liability has been "incurred" is only met once the third party has established the liability of the insured by judgment, award or agreement.[8] It is not met on the happening of the event giving rise to the liability of the insured. Until the third party has established liability in this way, he has no right of

[1] Set out in the Law Commission's Sixth Programme of Law Reform(1995) Law Com No 234 and the Scottish Law Commission's Fifth Programme of Law Reform (1997) Scot Law Com No 159.

[2] In preparing this paper we have consulted with the Northern Ireland Law Reform Advisory Committee.

[3] Hansard (HC) 29 October 1929, vol 231, col 128.

[4] Section 1(1).

[5] Section 2.

[6] Sections 1(3) and 2(1).

[7] Section 3. The Act is set out in Appendix A.

[8] *Post Office v Norwich Union Fire Insurance Society Ltd* [1967] 2 QB 363. See para 1.9 and paras 4.3-4.5 below where we also discuss briefly different views of when the right to an indemnity under a liability insurance policy should arise.

action against the insurer under section 1[9] and no right to the disclosure of policy information under section 2.[10]

CALLS FOR REFORM

1.6 Calls for reform of the Act have centred on the practical consequences for third parties of this judicial construction of sections 1 and 2.[11] Attention has been drawn, for example, to the fact that third parties may go to the expense of establishing the liability of the insured only then to discover, once the duty to disclose has arisen, that the insurer is not liable under the insurance contract.[12] Criticism has also been made of the requirement that third parties restore dissolved companies to the register so that they can establish their liability and acquire rights under the Act.[13]

1.7 The ability of insurers to rely against third party claimants under the Act on all the defences and policy terms on which they could have relied against the insured[14] has been questioned. Also, it has been suggested that distribution of a limited insurance fund, inadequate to meet the claims of all third parties, to those who establish their claims first rather than pro rata to all claimants is unfair.[15] Questions have also been raised as to whether what limitation period governs claims under the Act[16] and the territorial scope of the Act[17] should be clarified.

1.8 As well as reviewing the problems which have been caused by the current operation of the Act, we consider in this Paper whether, in view of changes in insurance law and practice since 1930, the scope of the Act should be extended or

[9] It is unclear whether English procedural rules allow the third party to join the insurer into proceedings against the insured for a declaration of the insurer's future liability. In Scotland, the third party may establish the liability of the insured and of the insurer in the same proceedings. See paras 4.27-4.29 below.

[10] *Nigel Upchurch v Aldridge Investments* [1993] 1 Lloyd's Rep 535 and *Woolwich Building Society v Taylor* [1995] 1 BCLC 132. See paras 4.13-4.17 below.

[11] Although the operation of the Act may also cause problems for insurers and for officeholders. See para 1.15 below.

[12] See dicta of Phillips J in *Banque Bruxelles Lambert v Eagle Star* unreported, 26 February 1993, see para 4.18, n 33 below. See also *Cox v Bankside* [1995] 2 Lloyd's Rep 437 discussed at para 7.2 and 13.13 below. It has been questioned whether this was the intention of Parliament in 1930. See Sir Jonathan Mance "Insolvency at Sea" [1995] LMCLQ 34 and J Goodliffe "What is Left of the Third Party (Rights against Insurers) Act 1930?" [1993] JBL 590. See Part 4 below.

[13] See paras 4.38-4.50 below.

[14] See eg Clauson LJ in *Smith v Pearl Assurance* (on the enforceability of arbitration clauses) and Lord Goff in *The Fanti* (on pay first clauses which require the insured to have paid the third party's claim before being entitled to an indemnity from the insurer). See Part 5 below.

[15] See Part 7 below.

[16] See Part 9 below.

[17] See Part 8 below.

restricted.[18] As part of our review, we look at schemes of third party rights in other jurisdictions.[19]

THE NATURE OF LIABILITY INSURANCE

1.9 A liability insurance policy is a contract of indemnity in which the insurer agrees to indemnify his insured for any loss suffered by reason of the insured's liability to another. In *Post Office v Norwich Union Fire Insurance Society Ltd*,[20] the Court of Appeal held that an insured did not suffer loss until his liability had been determined by judgment, arbitration or agreement. This approach differs from that taken by the court in *Chandris v Argo Insurance Co Ltd*,[21] where it was held that an insured had suffered loss when he had incurred liability to the third party, even though the existence and amount of that liability had not yet been established.[22]

THE PURPOSE OF LIABILITY INSURANCE

1.10 The view is taken in some jurisdictions that the purpose of liability insurance is not merely to protect the financial interests of the insured, but is also to protect the interests of those to whom the insured may incur liability. The Louisiana Direct Action Statute provides, for example, that "all liability policies ... are executed for the benefit of all injured persons ... to whom the insured is liable"[23] and allows third parties a right of direct action against insurers, regardless of the solvency of the insured.[24]

1.11 Some commentators in this country have also suggested that liability insurance could be seen as being for the benefit of third parties.[25] The doctrine of privity of contract[26] is still generally upheld by the English court, although it has been

[18] See Part 11 below.

[19] Brief summaries of third party rights in other jurisdictions are set out in Appendix F.

[20] [1967] 2 QB 363. See also *Bradley v Eagle Star Insurance Co Ltd* [1989] AC 957. These cases are discussed further at paras 4.4-4.7 below.

[21] [1963] 2 Lloyd's Rep 65.

[22] See also *Castle Insurance Co Ltd v Hong Kong Shipping Co Ltd* (*The Potoi Chou)* [1984] 1 AC 226. The approach taken in the *Post Office* and *Bradley* cases has been criticised. See para 4.5, n 7 and 4.7, n 13 below. See also Sir Jonathan Mance, "Insolvency at Sea" [1995] LMCLQ 34, at p 39 who suggests that, following these cases, the alternative approach is confined to general average loss and s 66(5) of the Marine Insurance Act 1906. See also Peter Goldsmith QC, "The Third Parties (Rights against Insurers) Act 1930" (1995) 11 Int ILR 378.

[23] See para 1.24 of Appendix F.

[24] In France, the progressive strengthening of the victim's position with regard to the insurer has been described as "decontractualisation".

[25] In 1929, the Attorney-General, Sir William Jowitt, said that the proposed Act would "confer a direct right in favour of the third party so that the third party may deal directly with the insurance company and that the money which comes into being by reason of the fact that the third party has been injured shall be money allocated to that third party and not taken away from him and utilised for the benefit of other persons". See Hansard (HC) 29 October 1929, vol 231, cols 128-143.

[26] Which means that a person who is not a party to a contract cannot enforce any rights which that contract purports to give him.

subject to criticism.[27] The Law Commission has recommended that a third party should be permitted to enforce contractual provisions when the parties to the contract intend that he should have the right to do so.[28] Scottish law already has the concept of ius quaesitum tertio, whereby an identified third party may have rights under a contract to which he is not a party if there is an express or implied intention to benefit him.[29]

1.12 As we have already noted, the 1930 Act operates by transferring the insured's rights against the insurer under the insurance contract to the third party. In cases brought under the 1930 Act, the court has stressed that third parties generally acquire no better rights under the Act than the insured had against the insurer.[30] In the Road Traffic Act 1988[31] and the Employers' Liability (Compulsory Insurance) Act 1969,[32] Parliament has intervened to protect the interests of third parties by laying down compulsory insurance regimes and prohibiting insurers from relying on particular defences. One of the issues which we consider in this paper is whether insurers should be prevented from relying, as against third party claimants under the 1930 Act, on defences and policy terms on which they could have relied against the insured.[33]

OUR APPROACH TO REFORM

1.13 Our approach to reform has been to balance a principled approach to what rights third parties should have against insurers and an appreciation of the practical consequences of any wide-ranging reform on the insurance industry and, through possible rises in insurance premiums, on those seeking insurance cover.

1.14 The UK insurance market, despite serious losses suffered by Lloyd's between 1988 and 1992, is the world's leading insurance market. In 1995, the UK insurance industry earned world-wide premium income of £92 billion (equivalent to 14.3% of gross domestic product) and invisible earnings of £5.4 billion.[34] We are aware of the importance of safeguarding the reputation and competitive position of the UK insurance market. We believe that a system of insurance law which adapts to

[27] There have been some inroads into the doctrine. In *Swain v The Law Society* [1983] AC 598, for example, the court held that a public law right of action against insurers existed for third party beneficiaries of statutory insurance schemes.

[28] Privity of Contract: Contracts for the Benefit of Third Parties (1996) Law Com No 242.

[29] *Peddie v Brown* (1857) 3 Macq 65; *Finnie v Glasgow South Western Railway Company* (1857) 3 Macq 75.

[30] See *Farrell v Federated Employers Insurance* [1970] 2 Lloyd's Rep 170, and *Pioneer Concrete v NEM* [1985] 1 Lloyd's Rep 274, discussed at paras 5.24-5.30 below.

[31] Sections 143-145. Earlier road traffic legislation is discussed briefly in Part 4 below.

[32] Section 1(1). See also Regulation 2 of the Employers' Liability (Compulsory Insurance) General Regulations 1971. See para 5.11 below. In September 1997, the Department of the Environment, Transport and the Regions published a consultative document recommending certain amendments to these regulations. See para 5.11, n 17 below.

[33] See Parts 5 and 14 below.

[34] See written answer of the President of the Board of Trade, Hansard (HC), 23 July 1997, vol 298, col 676. The underwriting capacity of Lloyd's alone in 1996 was £9.99 billion. See Lloyd's market figures, September 1996.

changing circumstances and operates fairly can only add to the reputation of the UK market.

1.15 As we consider amendments which would alter the rights of third parties under the Act, we look at how such amendments would affect insurers,[35] the insured,[36] the insured's insolvency practitioner[37] and the insured's other creditors.[38]

1.16 Some of the issues raised by this paper are not only relevant to the 1930 Act: they relate to insurance law and practice in general. Such issues include the disclosure of policy information, the ability of insurers to rely on defences and the distribution of a limited insurance fund to multiple claimants. We have attempted to concentrate on the relevance of such issues in the particular context of the 1930 Act but have, where appropriate, referred briefly to their wider implications. We have, for example, mentioned recommendations for reform to the law on non-disclosure and breach of warranty made previously by the Law Commission and reforms recently recommended by the National Consumer Council.[39]

1.17 We have sought to identify problems which have arisen and which might arise from the current wording of the Act and its construction by the courts. Some of the issues discussed in this paper, such as the limited rights of third party claimants to the disclosure of policy information, have regularly caused problems in practice and have been subject to much criticism. Others, such as the use of pay first clauses and the distribution of limited insurance funds to multiple third party claimants, have been given prominence by a number of recent high profile cases[40] but are rarely encountered.

[35] Who will wish to ensure that the third party's action against the insured is properly defended and that if they defend such actions on behalf of the insured they do not waive their right to rely on policy defences. See our discussion of *Wood v Perfection Travel Ltd* [1996] LRLR 233 at para 4.25 below. Insurers may also object to any amendment to the Act depriving them of defences which they would have had against the insured under the insurance contract. At paras 14.3 to 14.6 we discuss whether the problems faced by third party claimants under the Act would justify such an amendment.

[36] Who will wish to ensure that any amendment to the Act does not limit his rights against the insurer or against the third party. See for example para 12.18 below.

[37] Or other officeholder. Officeholders may be concerned were any amendment to the Act to place more onerous duties on them and if their fees and costs fell to be met by the insured's estate rather than from the insurance fund. We discuss what officeholders' duties of disclosure of policy information might be under an amended Act at para 13.18 below. At para 15.11, we consider the possibility of the officeholder administering a new statutory scheme providing for the distribution of the insurance fund to multiple third party claimants under the Act, were such a scheme to be introduced.

[38] Were the 1930 Act not to apply in particular cases, the claims of the insured's other unsecured creditors would rank equally with those of third party claimants, as was the case prior to 1930 (see para 1.2 above). In Part 11, we consider whether the interests of third parties in the insurance fund should always be preferred to those of the insured's other creditors or whether the Act should only apply, for example, when the insurance is compulsory or the third party's claim is for death or personal injury.

[39] See for example para 2.7, n 16 and 5.13, n 20.

[40] See *The Fanti* [1991] 2 AC 1, and *Cox v Bankside* [1995] 2 Lloyd's Rep 437, discussed at paras 5.59 and 7.2 below.

1.18 Given the costs of legal reform to end users, we are acutely aware of the importance of not reforming for the sake of reforming. We have indicated if, to our knowledge, a particular issue has not caused problems in practice and have sought consultees' views on those issues which they believe to be problematic. Most claims involving the Act appear to be settled without recourse to litigation[41] and we need to balance any advantages of increasing third party rights against insurers against the disadvantages of uncertainty and increased litigation. We need also to bear in mind the importance of the Act as a means of promoting settlement between insurers, insureds and third parties.

1.19 We refer in this paper to a number of proposals contained in Lord Woolf's report on the civil justice system in England and Wales, published in July 1996.[42] Lord Woolf has recommended a number of fundamental changes, some of which will have implications for proceedings under the 1930 Act. One of Lord Woolf's main objectives is increased openness and co-operation between parties.[43] In our view, many of our provisional conclusions are in line with Lord Woolf's approach to reform.[44]

STRUCTURE OF THIS PAPER

1.20 In Part 2, we look briefly at the historical background to the introduction of the Act and changes in law and practice since 1930. In Parts 3 to 9, we consider the current operation of the Act and in Parts 10 to 17, we consider possible options for reform. In Part 18, we summarise our provisional views and consultation questions. The Act and other relevant UK legislation, regulations and material are set out in appendices A to E. Brief notes on schemes of third party rights in foreign jurisdictions are to be found in Appendix F. The relevance of such schemes cannot be assumed as we consider possible options for reforming the 1930 Act because of the different legal and insurance contexts in which they operate.

[41] Following a survey of its members, the Association of British Insurers ("the ABI") gave us the following comments on their experience of the Act: "We estimate that insurers have had no more than 100 and probably nearer to 60 or 70 cases only under or involving the 1930 Act. It is often raised by the third party but it is rare that either liability or the status of the policy cover is in dispute. Therefore, generally the insurer will deal directly with the third party, without reference to the 1930 Act and without obliging the third party first to establish the liability of the insured by legal process or otherwise. However, insurers will apply the provisions of the Act in a case where liability or the status of the policy cover is in dispute. The experience is that such cases are few and far between but more often than not will involve prejudice to the insurer because of delayed notification of the claim. Occasionally also, the insurer will resist liability on the basis of a breach of a policy condition or warranty, sometimes because of non-disclosure". The ABI statistics are discussed further in Appendix C.

[42] *Access to Justice, Final report to the Lord Chancellor on the Civil Justice System in England and Wales* (July 1996). This was accompanied by a draft of the general rules which were to form the core of a new combined code of rules for civil procedure ("the Draft Civil Proceedings Rules"). The rules are to be renamed the Civil Procedure Rules; see s 1 of the Civil Procedure Act 1997. For the purposes of this consultation document we continue to refer to the Draft Civil Proceedings Rules.

[43] See *Access to Justice*, Section 1, page 4, para 9. See also paras 10.9-10.11 below.

[44] We have suggested, for example, that the liability of the insured and of the insurer should be resolved in the same proceedings and that there should be an earlier duty to disclose policy information. See Parts 12 and 13 below.

OVERVIEW

1.21 By way of a brief overview, we set out here some of the issues raised by this paper and the provisional approach we have taken to them.

(i) The scope of the Act

1.22 We have discussed possible extensions to and restrictions of the scope of the Act.[45] We have suggested that the Act should continue to apply to all liability insurance policies.[46]

(ii) The third party's rights under an amended Act

1.23 We suggest that a third party's rights against an insurer under an amended Act should not be dependant on his first establishing the liability of the insured, but should arise once two events have occurred: the incident giving rise to the liability of the insured and the happening of one of the insolvency events set out in the Act.[47] We suggest that, as well as acquiring the insured's right to be indemnified, the third party should have an immediate right to seek a declaration or declarator that, on the liability of the insured being established, the insurer will be liable to indemnify the third party.[48] The effect of this would be that the liability of the insured and of the insurer would be dealt with in one set of proceedings.[49]

(iii) The disclosure of policy information

1.24 We have suggested that the duty to disclose policy information should also arise on or be referable to the happening of one of the insolvency situations set out in the Act.[50] We have given our provisional view that the categories of information which should be disclosed should include the terms of the policy, details of any purported repudiation and the value of the insurance fund.[51]

(iv) The ability of insurers to rely on defences

1.25 We have suggested that third parties should be able to meet certain policy conditions themselves and that insurers should only be able to rely against third parties on breaches of certain policy conditions to the extent that such breaches are causative of the loss and have caused prejudice to the insurer.[52]

[45] See Part 11.

[46] See para 11.9 below.

[47] See para 12.10 below.

[48] It is uncertain whether or not a third party can already seek such a declaration under English procedural rules. He can seek a declarator under Scottish rules. See paras 4.27-4.29 below.

[49] Although the ability of insurers to rely on defences may be subject to new restrictions. See para 1.25 below.

[50] See para 13.4 below.

[51] See para 13.13 below.

[52] See Part 14 below. We have not made any recommendations regarding the insurer's ability to rely on the defences of non-disclosure and misrepresentation. See para 14.29 below.

(v) The distribution of a limited insurance fund to multiple claimants

1.26 We seek consultees' views on whether the courts' existing powers are adequate to impose a scheme of rateable distribution on claimants under the Act and on whether there should be a new statutory scheme and, if so, how it should operate.[53]

(vi) Limitation and prescription

1.27 We seek consultees' views on whether or not a fresh limitation or prescriptive period should apply to rights and duties under the Act. We have suggested that third parties should be able to substitute themselves in arbitrations started by the insured.[54]

(vii) Private international law aspects of the Act

1.28 We have suggested that the applicability of the 1930 Act to cases with a foreign element should be clarified and have sought consultees' views on the criteria which could be applied to determine its applicability.[55]

ACKNOWLEDGEMENTS

1.29 We gratefully acknowledge assistance from the persons and the bodies listed in Appendix G. We would like to express our particular thanks to our consultant, Dr Malcolm Clarke of the University of Cambridge. In addition to acting as our consultant, he arranged a conference to discuss the Act. The contributions of all who attended that event were of great assistance to our work. We are also grateful to officials of the Companies Court who assisted us in the statistical work referred to in Appendix C. The views expressed in this Consultation paper are those of the Law Commissions.

[53] See paras 15.5 and 15.18 below.

[54] Third parties can already do this under Scottish rules. See para 9.22 below.

[55] See Part 16 below.

PART 2
HISTORICAL BACKGROUND TO THE INTRODUCTION OF THE ACT AND CHANGES IN LAW AND PRACTICE SINCE 1930

INTRODUCTION

2.1 In this Part, we consider the reasons for the introduction of the 1930 Act and outline some of the changes in law and practice which have occurred since then. We consider the extent to which the Act continues to be relevant and look briefly at developments in liability insurance which might need to be taken into account were the Act to be amended.

THE INTRODUCTION OF THE 1930 ACT

2.2 It is clear from the Parliamentary debates of the Bill which was to become the 1930 Act that it was intended to deal particularly with the insolvency of insured motorists whose insolvency prevented third party victims from recovering insurance proceeds.[1] In *Re Harrington Motor Co Ltd,*[2] the court had rejected the claim by a third party who had been knocked down by a car belonging to an insured company which had gone into liquidation. The court reluctantly agreed with the insured's liquidator that the insurance proceeds formed part of the assets of the company for distribution to the creditors as a whole.[3]

2.3 Both Atkin LJ and Lord Hanworth MR suggested that the law should be amended[4] and further calls for reform followed a similar decision of the Court of

[1] Hansard (HC) 29 October 1929 vol 231, col 128 and 130. In *McCormick v National Motor and Accident Insurance Union Ltd* (1934) 49 Ll L Rep 361 at 363, Scrutton LJ referred to the problems faced by the victims of motor accidents where insured drivers were insolvent and said of the 1930 Act: "this Act of 1930 was passed to deal with the difficulty, and it gave a third party who was injured by a motor car certain rights against the defendant against whom he got a judgment if he went bankrupt but not otherwise". The wording of the Act was general, however, and mention was also made by the proposer of the Bill to problems faced by employees of insolvent employers: Hansard (HC) 29 October 1928, vol 231, col 130.

[2] [1928] Ch 105.

[3] Lord Hanworth concluded that, "it appears to me that this appeal must be dismissed, even though one may regret that it is not possible to earmark this sum and to say that the liquidator ought to be allowed to receive it and to pay it over, inasmuch as it was the misfortune of [the third party appellant] which caused this sum to be received, a sum which will enure to the benefit of all the creditors of the company and not to the particular advantage of the man who suffered the loss which quantified the risk which the insurance company had taken", *ibid* at p 116.

[4] Lord Hanworth referred to the legislative precedent of s 7 of the Workmen's Compensation Act 1925 which, he said, "enables the workman, in the event of the employer who has entered into a contract with insurers becoming bankrupt or making a composition or arrangement with his creditors, to stand in the shoes of the employer, with the result that the rights of his employer are transferred to and vest in him, the workman, subject to certain conditions and limitations of liability", *ibid* at p 116.

Appeal in *Hoods Trustees v Southern Union General Insurance Company of Australia Ltd.*[5] A Bill was introduced in April 1928 and the Act became law in July 1930. The only amendments to it since have been consequential amendments to the detail of its insolvency provisions following the introduction of the Insolvency Acts 1985 and 1986 and the Bankruptcy (Scotland) Act 1985.

CHANGES IN INSURANCE LAW SINCE 1930

The growth of liability insurance since 1930

2.4 There has been a huge development in the number of activities covered by insurance since 1930 as areas of liability have expanded[6] and insurance markets diversified.[7] In some cases, Parliament has made insurance compulsory. Shortly after the 1930 Act was passed, the Road Traffic Act 1930 made it compulsory for the user of a motor vehicle on a road to be insured against liability for the death of or injury to third parties.[8] Other legislation laying down schemes of compulsory insurance[9] includes the Employers' Liability (Compulsory Insurance) Act 1969, the Nuclear Installations Act 1965, the Merchant Shipping Act 1995 and the Dangerous Wild Animals Act 1976.[10]

2.5 Some compulsory insurance schemes, such as the Road Traffic Acts and the Merchant Shipping Act 1995, provide third parties with specific rights against insurers on the insolvency of the insured. Others, such as the Employers' Liability

[5] [1928] 1 Ch 793.

[6] The landmark decision on negligence in *Donoghue v Stevenson* [1932] AC 562 was decided two years after the Act was introduced. The law of negligence has developed since the 1930s, opening up the number of potential claimants. There is a greater awareness of legal rights and fear of legal action. Advances in medical knowledge have led to an understanding of the causes of insidious diseases (where there is a long time lag between the contraction of the disease and the manifestation of symptoms). Changes in the law on limitation have allowed plaintiffs to pursue personal injury actions long after the event which caused the injury although third parties have faced problems pursuing actions against insurers under the Act in respect of such claims. See our discussion of *Bradley v Eagle Star Insurance Co Ltd* [1989] AC 957 at para 4.6 below.

[7] In 1930, few activities were covered by liability insurance: cover had been available since 1875 for accidents arising from the increased horse traffic in cities, for motor accidents since 1898 and for employers' liability, largely since the introduction of the Employers' Liability Act in 1880. Further employers' liability legislation in 1897, 1900, 1906 and 1925 increased the demand for such cover. Contract guarantee bonds guaranteeing a builder would complete a contract had been available since 1904 and businessmen were likely to have fire, fidelity guarantee, glass and boiler insurance to protect themselves against certain property and pecuniary losses.

[8] Subsequent amendments to the 1930 Act were consolidated in the Road Traffic Act 1988. Any person using a motor vehicle on the road must now have compulsory insurance covering, for an unlimited sum, the user's liability for death or personal injury and, for a minimum of £250,000, liability for property damage to third parties. See ss 143-145 of the 1988 Act.

[9] Either directly or by requiring those engaged in a particular activity to be licensed or to be member of a particular body, the grant of a licence or membership being dependant on the applicant having a minimum level of cover.

[10] Legislative and other schemes of compulsory insurance are discussed further in Part 11 below when we consider arguments that the scope of the Act should be restricted to activities covered by compulsory insurance.

(Compulsory Insurance) Act 1969, do not. Prior to 1930, employees were given rights of direct action against insurers on the bankruptcy or insolvency of their employers under the Workmen's Compensation Acts 1906 and 1925. This is no longer the case and employees must now proceed under the 1930 Act in such cases.

Regulation of the insurance industry

2.6 The insurance industry is regulated by legislation and by voluntary codes and statements of practice. The main legislation governing insurance is the Insurance Companies Act 1982 which provides, among other things, for the authorisation of insurers.[11] The 1982 Act has been substantially amended since 1982, partly as a result of EU law. The Policyholders Protection Act 1975[12] allows policyholders owed sums by insolvent insurers to recover those sums from a fund set up by insurers.[13]

2.7 The insurance industry, mainly through the ABI, has also adopted a number of voluntary codes and statements of practice, modifying insurance law in some areas.[14] Many insurers are also members of the dispute handling scheme operated by the Insurance Ombudsman Bureau. Not all insurers belong to the ABI, however, or are members of the Bureau's scheme. It is also unclear whether or not insurers apply the Statement to claims brought by third parties under the 1930 Act.[15] Concern has also been voiced that the gap in self regulation will widen as the single European market opens up and insurance is increasingly offered by foreign insurers.[16]

[11] Which is currently the task of the Department of Trade and Industry. It appears that the FSA (which will take on the duties of the Securities and Investment Board ("SIB") and other regulatory bodies) will assume responsibility for supervising the insurance industry. See written answer of the President of the Board of Trade, Hansard (HC) 23 July 1997, vol 298, col 676.

[12] Which will be amended when the Policyholders Protection Act 1997 is brought into force.

[13] The 1975 Act and the 1997 Act are discussed at paras 11.4-11.5 below.

[14] These include the Statement of General Insurance Practice, 1986 (revised in 1995 and which does not apply to commercial lines business) and codes on the selling of insurance by intermediaries and the selling of private medical insurance. We refer at Part 5, n 20 below to changes in insurance practice following publication of the Law Commission's report on Non-disclosure and Breach of Warranty (1980) Law Com No 104.

[15] We consider at Part 14 below whether the particular problems faced by third party claimants under the 1930 Act would justify greater restrictions on the ability of insurers to rely on defences than those already laid down by the general law, by the Act itself and by voluntary insurance practices.

[16] See comments in the report of the National Consumer Council: Insurance Law Reform: The Consumer Case for a Review of Insurance Law (May 1997) p 12. The size of this "gap" and the suggestion that it may widen as the single European market opens up have been disputed by the ABI: Insurance Law Reform: the Response of the ABI to the NCC Report, July 1997, p 4, para 3.11.

The relevance of the 1930 Act today

2.8 As we have already noted, Parliament's main intention when passing the 1930 Act was to provide a remedy to the victims of insolvent insured motorists.[17] Specific road traffic legislation now protects victims in such cases. It could be argued, therefore, that the 1930 Act has no continuing relevance. We would dispute this, both on the basis that the wording of the 1930 Act is general in scope and that, whatever Parliament's intention in passing the Act, it has operated successfully since 1930 to assist third parties and to encourage settlement of claims over a wide range of activities now covered by insurance.[18]

2.9 Those drafting the 1930 Act borrowed wording from the Workmen's Compensation Acts, which was drafted specifically to cover employee rights, but they did not restrict the wording of the new statute to road traffic cases. Nor did they seek to include the regime of third party rights as part of the Road Traffic Bill which was shortly to be passed. Although the availability of insurance cover was limited in 1930, it was available in respect of a number of activities.[19]

2.10 As we have seen, unlike earlier statutes, the Employment Protection Act 1969 did not include a specific regime of third party rights against the insurers of insolvent employers.[20] Employees rely instead on the provisions of the 1930 Act.[21] Our research suggests that many claims involving the 1930 Act are based on employer's liability cases, cases involving public liability cover, general personal injury claims and professional indemnity cases.[22]

2.11 We discuss in Part 12 whether or not the Act should continue to apply to all liability insurance policies or whether its scope should be restricted. Relevant to this issue is whether developments in insurance law and practice which were not foreseen by those passing the Act need to be reflected in amendments to the Act. We look briefly below, for example, at the growth of reinsurance, at reinstatement provisions and at the use of "claims made" polices.

CHANGES IN INSURANCE PRACTICE SINCE 1930

2.12 As insurance business has expanded and more players have entered the insurance market, insurance practice has changed and insurance arrangements have become more complex. We outline below some of the developments in insurance practice

[17] See para 2.2 above.

[18] Also, s 153 of the Road Traffic Act 1988 (which provides a right of recourse against the insurers of insolvent insureds) relates only to compulsory risks. With regard to other risks, third parties must rely on the provisions of the 1930 Act, as they must also do with regard to compulsory risks if, for example, the vehicle causing the accident was not "on a road".

[19] See para 2.4 above.

[20] See para 2.5 above.

[21] The employees of insolvent employers may also have a right to recover arrears of pay from the National Insurance Fund under s 182 of the Employment Rights Act 1996.

[22] See our summary of ABI statistics at paras 1.1-1.2 of Appendix C. See also the summary of our survey of applications to restore dissolved companies to the Register of Companies at paras 1.3-1.6 of Appendix C. This survey is discussed further at paras 4.44-4.50 below.

which may be relevant to our review of the 1930 Act and indicate where they are discussed in more detail in the rest of this paper.

Reinsurance

2.13 As insurers began to take on greater risks, for a wider range of activities, they sought to spread their risk through reinsurance. Reinsurance is currently excluded from the 1930 Act by section 1(5) but the justification for its exclusion has been questioned.[23]

2.14 Reinsurance terminology is complex and views as to the meaning of a particular term may vary.[24] There are two main forms of reinsurance: facultative reinsurance and treaty reinsurance. Facultative reinsurance is the reinsurance of individual risks[25] where the insurer has no obligation to cede and the reinsurer no obligation to accept a particular risk. The reinsurer knows in advance the risks which he is to cover. Because of the high administrative costs of facultative reinsurance, it has largely been replaced by treaty insurance.

2.15 Treaty reinsurance involves an agreement between the insurer and the reinsurer under which the insurer is obliged to cede and the reinsurer to accept all risks falling within the scope of the agreement. Among the issues covered by the treaty will be the monetary limits of the cover and the classes of business covered. The reinsurer will not know in advance the particular risks which he will cover.

2.16 Insurance business may be reinsured proportionally or non-proportionally. Where reinsurance is proportional, the insurer decides what part of the risk it wishes to retain and reinsures the balance with one or more reinsurers. Premiums and losses on a risk or portfolio of risks are shared by insurer and reinsurer proportionately to that division. Where reinsurance is non-proportional, losses in excess of a certain agreed level are reinsured.[26]

2.17 Although there may be a close relationship between the reinsurer and the reinsured, the reinsured is not the agent of the reinsurer and there is no contractual relationship between the original insured and the reinsurer.[27] If the reinsured defaults, the insured has no right of action against the reinsurer. The

[23] See Sir Jonathan Mance "Insolvency at Sea" [1995] LMCLQ 34 at 51.

[24] We discuss at para 5.62, n 78 below the different interpretations given by reinsurers to "ultimate nett loss" clauses in reinsurance contracts in *Home & Overseas Insurance Co Ltd v Mentor Insurance Co (UK) Ltd* [1989] 1 Lloyd's Rep 473 and *Charter Reinsurance Co Ltd v Fagan* [1996] 2 WLR 726.

[25] Although it could involve the reinsurance of a series of related insurance policies. See *Balfour v Beaumont* [1982] 2 Lloyd's Rep 493, at 496.

[26] The excess amount may be split between a number of different layers of policies which are triggered as previous layers are exhausted. The number of times the insurer will be able to recover from the reinsurer under a treaty will depend on how many "reinstatements" he has under the treaty. Where a layer has been exhausted, cover is said to be reinstated, allowing further claims to be brought. There will usually be limits on the amount recoverable per claim; if one claim exceeds the per claim limit, there will be no access to higher layers of cover. The implications of reinstatement provisions for third party claims were discussed in *Cox v Deeny* [1996] LRLR 288. See para 7.5, n 4 below.

[27] *Western Assurance Company of Toronto v Poole* (1903) KB 13.

validity of "cut-through" clauses which purport to give the insured a cause of action against the reinsurer on the insolvency of the reinsured has been doubted.[28]

Insurance intermediaries

2.18 The growth in insurance business and the increasing complexity of insurance arrangements has meant that insurance cover is likely to be obtained and managed through insurance brokers and other intermediaries.[29] In many cases, information about the insurance cover held by an insured is likely to be kept by insurance brokers who are not themselves bound by the disclosure provisions contained in section 2 of the Act.[30]

Triggers for cover - "occurrence" and "claims made" policies

2.19 In the mid 1980s, some markets (principally the USA and London) converted liability insurance policies to a "claims made" form. The use of claims made policies grew in response to fears of huge claims in respect of asbestosis and other latent injuries. Under such policies, the insured is covered for claims reported during the period covered by the policy, whenever the incident occurred. Traditional "occurrence" policies cover loss or damage occurring during the policy period, whenever those claims are notified. By using claims made policies, insurers seek to protect themselves from claims made a long time after the incident giving rise to the liability of the insured, for which they might have inadequate reserves.

2.20 If the insured has a claims made policy which terminates before the third party has acquired rights under the 1930 Act and the insured (or his liquidator or trustee in bankruptcy) cannot renew the policy, there may be no insurer against whom the third party can proceed. This may be a particular problem in the case of "long tail" personal injury claims.[31] It has been suggested that claims made cover may not provide the cover required by employers' liability legislation.[32]

[28] Being in conflict with the doctrine of privity of contract. See para 1.11 above. At Part 11 below, we consider whether the 1930 Act should be extended to policies of reinsurance.

[29] Such as insurers' or underwriters' agents employed or instructed by insurers. Insurance brokers are regulated by the Insurance Brokers (Registration) Act 1977. Other intermediaries are generally regulated by ABI codes of conduct. See also Commission Recommendation 92/48/EEC. In June, 1997 the European Commission announced that it was about to propose a directive on insurance intermediaries. Professor R M Merkin "Intermediaries; EC Proposals" Insurance Law Monthly, July 1997 pp 11-13. See paras 13.19-13.20 below.

[30] At para 13.20, we seek consultees' views on whether the duty to disclose policy information should extend to brokers and other insurance intermediaries.

[31] Where symptoms and the gravity of the injury may not manifest themselves fully for a long period of time.

[32] General Insurance Study Group Report of the Liability Insurance Working Party to the 1989 Conference, Brighton, para 5.2. Claims made policies are most commonly used in relation to professional indemnity insurance. At para 14.31 below, we seek consultees' views on whether insurers under claims made policies should be prevented from declining liability on the ground that notification by the third party was made outside the claims period.

CHANGES IN INSOLVENCY LAW AND PRACTICE SINCE 1930[33]

2.21 As a result of amendments to the 1930 Act by the Insolvency Acts 1985[34] and 1986[35] and the Bankruptcy (Scotland) Act 1985,[36] the Act now applies where an administration order has been made or a voluntary arrangement proposed.[37] It also applies where the estate of the insured falls to be administered in accordance with an order under section 421 of the Insolvency Act 1986,[38] which relates to the administration of the insolvent estates of deceased persons, and an award of sequestration of the estate of a deceased debtor[39] or a judicial factor appointed on the insolvent estate of a deceased person.[40]

[33] We suggest in Parts 8 and 16 below that cross-border insurance is likely to increase and look at rules governing cross-boarder insolvencies.

[34] Section 235 and Sched 8, para 7.

[35] Section 439 and Sched 14.

[36] Sched 7.

[37] For the sake of brevity, we refer generally in this Paper to winding up and bankruptcy orders rather than to the other orders and arrangements covered by the Act.

[38] Which contains provisions formerly in section 228 Insolvency Act 1985. Before that, provisions regarding the administration of insolvent estates were found in sections 33(5) and 130 Bankruptcy Act 1914 and section 34(1) and Sched 1, Part 1 Administration of Estates Act 1925.

[39] Bankruptcy (Scotland) Act 1985, s 6.

[40] Judicial Factors (Scotland) Act 1889, s 11A. At para 12.10, we seek consultees' views on whether, in its application to Scotland, the term "becoming bankrupt" should be replaced by "person's estates being sequestrated".

PART 3
CURRENT LAW: SUMMARY OF THE SCHEME AND OPERATION OF THE ACT

THE SCHEME OF THE ACT

3.1 The Act has only five sections. The Act is set out in Appendix A. Section 1 transfers the insured's rights against the insurer to a third party to whom liability has been "incurred" on the happening of one of the insolvency situations set out in subsection (1).[1] In the case of an insured individual, these are the insured becoming bankrupt or making a composition or arrangement with his creditors.[2] In the case of an insured company, they are the winding up of the company, the making of an administration order, the passing of a resolution for a voluntary winding up, the appointment of a receiver or manager, possession being taken of any property subject to a floating charge or the approval of a voluntary arrangement under Part I of the Insolvency Act 1986.[3]

3.2 Section 2 provides for the disclosure of policy information by the insured and the office holder[4] and by the insurer[5] and prohibits terms in insurance contracts purporting to prevent the disclosure of such information or to avoid the contract or to alter the rights of insurer or insured on the disclosure of such information.[6]

3.3 Section 3 provides that settlements between the insurer and the insured after the transfer of rights under the Act will not defeat or affect the rights transferred to third parties under it.[7]

3.4 Section 4 relates to the applicability of the Act to the estates of deceased insureds in Scotland and section 5 gives the short title of the Act.

ASPECTS OF THE OPERATION OF THE ACT WHICH HAVE BEEN CRITICISED

3.5 In Parts 4 to 9, we consider the following aspects of the operation of the Act which have given rise to criticism:-

1 The Act will not apply if the insurer is not contractually bound to indemnify the insured but has a discretion as to whether or not to do so. See *CVG Siderurgicia v London Steamship Owners Mutual ("The Vainqueur Jose")* [1979] 1 Lloyd's Rep 557.

2 Section 1(1)(a). In the case of a deceased debtor, where the estate is administered in accordance with s 421 of the Insolvency Act 1986, s 6 of the Bankruptcy (Scotland) Act 1985 or s 11A of the Judicial Factors Act 1889. See para 2.21 above.

3 Section 1(1)(b). See also para 2.21 above.

4 Section 2(1).

5 Section 2(2).

6 Section 2(1).

7 Section 3.

(i) Third parties may have to establish the liability of the insured in separate proceedings before they can proceed against the insurer under the Act or obtain policy information;[8]

(ii) Where the insured is a dissolved company which has been struck off the Register of Companies, third parties may have to restore the company to the register and establish its liability before they can proceed against the insurer;[9]

(iii) Third parties may find their claims defeated because insurers can rely on defences which they would have had against the insured;[10]

(iv) The scope of the provisions in section 2 relating to who owes a duty of disclosure and as to what information should be disclosed is narrow;[11]

(v) Third parties' potential claims under the Act may be defeated by the insurer and the insured settling the insured's claims under the policy before the happening of one of the insolvency situations set out in the Act;[12]

(vi) An insurance fund which is inadequate to meet the claims of all third parties is distributed to those who establish their claims first rather than rateably to all claimants;[13]

(vii) The territorial scope of the Act is unclear;[14]

(viii) It is unclear under English law[15] when limitation periods governing claims under the Act start to run and whether third parties can substitute themselves in arbitrations started by the insured against the insurer;[16]

(ix) The current operation of the Act may cause unnecessary costs to third parties, insurers and officeholders.[17]

[8] See Part 4 below. As we discuss at paras 4.21-4.30, it is uncertain whether English procedural rules allow third parties to proceed against insurers for a declaration of liability. In Scotland they can seek a declarator. Third parties may also be entitled to earlier disclosure of policy information under Scottish law. See para 4.18 below.

[9] Part 4, paras 4.38-4.51.

[10] See Part 5 below.

[11] See Part 6 below.

[12] See paras 5.8-5.9 below.

[13] See Part 7 below.

[14] See Part 8 below.

[15] We discuss the position under Scottish law at paras 9.18-9.22 below.

[16] See Part 9 below.

[17] See Part 4, paras 4.31-4.35 below for costs to third parties and insurers. See paras 6.9-6.10 for officeholders' costs.

PART 4
WHEN DO RIGHTS TRANSFER AND DUTIES ARISE UNDER THE ACT? THE JUDICIAL CONSTRUCTION OF SECTIONS 1 AND 2 AND THE IMPLICATIONS OF THAT CONSTRUCTION

4.1 Interpreting section 1 of the Act, the courts have held that the liability of the insured must have been established before the third party can acquire rights under section 1 of the Act and before the duty to disclose can arise under section 2. In this Part, we look at case law on sections 1 and 2[1] and consider the implications of the judicial construction of these sections.[2] We look, for example, at the costs consequences of the parties being involved in two or more sets of proceedings, at the outset of which the third party may not even know if the insured has insurance cover.[3] Where the insured is a dissolved company which has been struck off the Companies Register, these may include proceedings to restore the company to the Register so that the third party can bring proceedings against the company and establish its liability before proceeding against the insurer.[4]

WHEN DO RIGHTS TRANSFER TO THE THIRD PARTY UNDER SECTION 1 OF THE ACT?

4.2 Section 1 of the 1930 Act[5] sets out the insolvency events to which it applies, then provides that

> if, either before or after that event, any such liability ... is incurred by the insured, his rights against the insurer under the contract in respect of the liability shall ... be transferred to and vest in the third party to whom the liability was so incurred.

4.3 As we shall see, many of the practical problems associated with the Act stem from the decision in *Post Office v Norwich Union Fire Insurance Society Ltd*[6] and subsequent cases that a cause of action against an insurer under a liability insurance policy does not arise until the insured's liability to the third party has been established by judgment, arbitration or agreement. Third parties wishing to proceed under the Act must first, therefore, establish the liability of the insured.

1 See paras 4.2-4.18.

2 See paras 4.19-4.51.

3 See paras 4.31-4.37.

4 See paras 4.38-4.39.

5 See Appendix A.

6 [1967] 2 QB 363.

Post Office v Norwich Union Fire Insurance Society Ltd

4.4 In the *Post Office* case, the Post Office alleged that a firm of contractors had damaged one of their cables. Before proceedings could be started against the contractors, they went into liquidation. The Post Office started proceedings against the contractors' insurer, claiming that, on the insolvency of the insured, they were entitled to sue the insurer direct under the 1930 Act.

4.5 The Court of Appeal held that the insured could not have sued the insurer for an indemnity until his liability to the third party had been established as, before that point, he would not have suffered any loss.[7] Under section 1 of the Act, third parties could only sue the insurer in circumstances in which the insured could have done so. Before proceeding under the Act, they must first, therefore, establish the liability of the insured. This could be by judgment of the court, by an award in arbitration or by agreement.[8]

Bradley v Eagle Star Insurance Co Ltd

4.6 The Court of Appeal's decision in *Post Office v Norwich Union Fire Insurance Society Ltd*[9] was approved by the House of Lords in *Bradley v Eagle Star Insurance Co Ltd*.[10] The applicant in the *Bradley* case had been employed by a company in their cotton mill and developed a respiratory disease caused by the inhalation of cotton dust. The company was wound up in 1975 and dissolved in 1976. Intending to bring an action against the company's insurers under the 1930 Act, the applicant

[7] Lord Denning referring, at p 373, to the following obiter dicta of Devlin J in *West Wake Price & Co v Ching* [1957] 1 WLR 45, 49: "The essence of the main indemnity clause, as indeed of any indemnity clause, is that the [insured] must prove a loss. The [insured] cannot recover anything under the main indemnity clause or make any claim against the underwriters until [the insured] have been found liable and so sustained a loss. If judgment were given against them for the sum claimed, they would undoubtedly have sustained a loss and the question would then arise, what was the cause of the loss". Harman LJ, at p 376, reached the same conclusion as Lord Denning on what he called the narrow ground that the right transferred under the statute was subject to rights and obligations under the contract of insurance: as the insured could not yet have sued the insurer under the contract, nor could the third party. Lord Denning's reliance on Devlin J's dicta has been criticised: see Enright, *Professional Indemnity Insurance* (1st ed 1997) p 109: "The emphasis and point of the passage in Devlin J's reasoning is that the insured must "prove a loss". This says nothing about the nature of the right to an indemnity, the time at which it arises or the form of action which an insured may or may not take ... the proposition that it is necessary to prove a loss to recover under a right to an indemnity does not compel the conclusion that the right "arises" only on proof of loss".

[8] It appears that a third party who has been awarded an interim payment against the insured will be held to have established his liability. See *Cox v Bankside* [1995] 2 Lloyd's Rep 437, and see para 7.4, n 3 below. Lord Denning suggested, at p 374, that the insured might be able to sue the insurer earlier for a declaration if, for example, the policy had been repudiated. In *Nigel Upchurch Associates v Aldridge Estates Investment Co Ltd* [1993] 1 Lloyd's Rep 535, at 538, the court held that no contractual right to seek declaratory relief transferred to third parties before a specific liability had been established. At paras 4.21-4.30 below, we discuss whether procedural rules allow third parties to seek declaratory relief.

[9] [1967] 2 QB 363.

[10] [1989] AC 957.

sought an order requiring the insurers to disclose to her the terms and particulars of relevant insurance policies.[11]

4.7 The House of Lords applied *Post Office v Norwich Union Fire Insurance Society Ltd*[12] and held, by a majority, that an insured could not sue for an indemnity from the insurer until its liability to the third party had been established.[13] The court held that as the insured company had been dissolved and it was not possible for the third party to restore the company and establish its liability, no right of indemnity could be transferred to her under section 1 of the Act.[14] Accordingly, no useful purpose could be served in making an order for pre-action discovery.

4.8 Scottish law also provides that the liability of the insured must be established before the insured's rights under the insurance contract are transferred to the third party. In *Greenlees v Port of Manchester Insurance Company*,[15] the victim of a motoring accident obtained a decree against the driver who became bankrupt. Lord Murray stated that liability to the third party is incurred by the insured only when it is established.[16]

[11] Under s 33(2) of the Supreme Court Act 1981 and RSC O 24, r 7A. See CCR O 13, r 7(1)(g) and 2(a).

[12] [1967] 2 QB 363.

[13] Lord Templeman, dissenting, held, at p 970, that "[t]he Act of 1930 was intended to protect a person who suffers an insured loss at the hands of a company which goes into liquidation. That protection was afforded by transferring the benefit of the insurance policy from the company to the injured person. In my opinion, Parliament cannot have intended that the protection afforded against a company in liquidation should cease as soon as the company in liquidation reaches its predestined and inevitable determination in the dissolution of the company". The reasoning in the *Post Office* and *Bradley* decisions has been questioned on the ground that "'ascertainment' is just one matter which can establish loss" and that its "continuing status as a separate requirement for a right to an indemnity is a recusant relic of the common law and has wrongly hindered the development of the authorities on the equitable rule". See Enright at para 3.094, who also suggests that the *Bradley* decision is "arguably inconsistent" with comments of Lord Goff in *The Fanti*. Lord Goff suggested that the right transferred to a third party on insolvency was "at best a contingent right to indemnity". See para 4.18, n 31 below. The approach taken by the court in the *Post Office* and *Bradley* cases appears, however, to represent current law. See Malcolm Clarke, *The Law of Insurance Contracts* (3rd ed 1997) p 416 and *MacGillivray and Parkinson on Insurance Law* (8th ed) p 886. See also our discussion of *Nigel Upchurch v Aldridge Estates Investment Co Ltd* [1993] 1 Lloyd's Rep 535, and *Woolwich Building Society v Taylor* [1995] 1 BCLC 132 at paras 4.13 to 4.17 below.

[14] The consequences of the court's approach were worse for the third party in the *Bradley* case than they were in the *Post Office* case*:* the law at that time did not permit the third party in the *Bradley* case to restore the dissolved company to the register so she could never establish its liability nor acquire rights against the insurer under the 1930 Act. As a result of the *Bradley* case, the law was changed; the two year time limit from the date of dissolution on the right to apply to restore companies to the register does not apply in cases involving death of personal injury. See s 651 Companies Act 1985 and paras 4.38-4.39 below.

[15] 1933 SC 383.

[16] Lord Anderson also expressed the view that the reference to "liability" indicated a situation where liability had already been established. This approach was followed in *Vickers Oceanic Ltd v Liquidator of Speedcranes Ltd* 1985 JLSS 85 and *Landcatch Ltd v Gilkes* 1990 SLT 688, 693.

4.9 As we shall now see, on the basis of the *Post Office* and *Bradley* cases the courts have also held that the duty to disclose policy information under section 2 of the Act does not arise until the liability of the insured has been established.

WHEN DO THIRD PARTIES ACQUIRE RIGHTS TO DISCLOSURE UNDER SECTION 2 OF THE ACT?

4.10 Section 2(1) of the Act provides that, in the event of one of the insolvency situations set out in the Act:

> it shall be the duty of the bankrupt, debtor, personal representative of the deceased debtor or company, and, as the case may be, of the trustee in bankruptcy, trustee, liquidator, administrator, receiver, or manager, or person in possession of the property to give at the request of any person claiming that the bankrupt, debtor, deceased debtor, or company is under a liability to him such information as may reasonably be required by him for the purposes of ascertaining whether any rights have been transferred to and vested in him by this Act and for the purpose of enforcing such rights, if any ...[17]

4.11 Section 2(2) imposes a duty on an insurer to disclose information if the information provided to the third party under section 2(1) "discloses reasonable ground for supposing that there have or may have been transferred to him under this Act" rights against that insurer.

4.12 The wording of section 2(1) might suggest that the duty of the insured and of the officeholder to disclose policy information would arise on the happening of one of the insolvency situations set out in the Act. However, as the following cases show, the court has interpreted section 2 in accordance with cases decided under section 1, holding that third parties have no rights to disclosure under the Act until the liability of the insured to the third party has been established.

Nigel Upchurch Associates v Aldridge Estates Investment Co Ltd[18]

4.13 In *Nigel Upchurch Associates v Aldridge Estates Investment Co Ltd*,[19] the third party sought an order for disclosure under section 2 of the Act against the insured and the supervisor of the insured's scheme of voluntary arrangement. The Deputy Judge[20] refused the third party's application, construing section 2 in the light of the interpretation which had been given to section 1 in the *Post Office* and *Bradley* cases.

[17] Section 2(1) prohibits insurers from making the disclosure of policy information to a third party a basis for avoiding the insurance contract. The sub-section provides that "any contract of insurance, in so far as it purports, whether directly or indirectly, to avoid the contract or to alter the rights of the parties thereunder upon the giving of any such information in the events aforesaid or otherwise to prohibit or prevent the giving thereof in the said events shall be of no effect".

[18] [1993] 1 Lloyd's Rep 535.

[19] *Ibid.* See also para 4.5, n 8 above.

[20] Miss Barbara Dohmann QC.

4.14 The Deputy Judge reasoned that the statutory duty imposed by section 2 was to provide information for the purposes of ascertaining whether any rights had been transferred under the Act and of enforcing such rights. As the insured could not sue for an indemnity from his insurer until the existence and amount of his liability to the third party had been established, which had not yet happened, no right to claim an indemnity from the insurer could have transferred to the third party. Section 1 transferred to the third party neither a contractual right to seek declaratory relief before a specific liability had been established nor a right to be indemnified contingent upon liability being established.[21]

4.15 The third party argued that interpreting section 2 so as to require liability to have been established before there was a duty to provide information was inconsistent with the wording of section 2 which referred to the third party's "*claiming* that the insured is under a liability to him" and to his ascertaining "*whether any* rights have been transferred" and "enforcing such rights, *if any*". The Deputy Judge rejected this argument and the argument that "commercial common sense requires early information as to insurance cover, so that time and money are not wasted on what may turn out to be a fruitless effort." She held that "the Act was not designed to deal with such mischief, it was designed to remedy the injustice that a creditor had no right to the proceeds as such of any third party insurance effected by an insolvent person when the insurance monies became payable to meet his claim."[22]

Woolwich Building Society v Taylor[23]

4.16 In *Woolwich Building Society v Taylor*, the judge adopted a different line of reasoning, although the result for the third party plaintiff seeking disclosure[24] of policy information and of the grounds of the purported avoidance was the same.[25] Refusing the plaintiff's application, Lindsay J pointed out that the wording of section 2(1) was in the past tense; it referred to rights which "have been transferred". He recognised that the liability of the insured to the third party "arises ... from the moment when the accident occurred and the damage was suffered",[26] but held that it was impossible to determine whether, in the words of section 1(1), liability had been "incurred" until it had been established. Until liability had been established, it could not be known whether any rights had been

[21] Lord Denning in the *Post Office* case had suggested that, where the insurer had purported to repudiate liability under the policy, the insured might have a right to sue the insurer for a declaration as to the continuing liability of the insurer before the insured's liability to the third party had been established. See para 4.5, n 8 above.

[22] See, however, para 4.18 below.

[23] [1995] 1 BCLC 132.

[24] From the liquidator and from the insurers under section 2 of the 1930 Act. The insurers declined to rely on the precondition that the third party acquire information under s 2(1) from the insured before their duty to disclose arose. *Ibid,* at p 137.

[25] Lindsay J referred to *Nigel Upchurch v Aldridge Estates Investment Co Ltd* but declined to examine the reasoning in that case on the basis that he had reached his conclusion "on a quite separate and different ground". [1995] 1 BCLC 132, at 146.

[26] Referring to Salmon J's judgment at p 377 in *Post Office v Norwich Union Fire Insurance Society Ltd* [1967] 2 QB 363.

transferred so no information could reasonably be required to ascertain whether they had done so.[27]

4.17 Lindsay J concluded that, likewise, the third party could not seek disclosure from the insurer. He suggested that it was "inherently improbable that in 1930 Parliament intended any such pre-trial or advance discovery as between the third party and the insured and as between the third party and the insurer".[28]

4.18 It appears from Hansard, however, that the intention of those passing the 1930 Act was to allow pre-trial disclosure of policy information.[29] The court's construction of section 2 has been criticised.[30] It has been suggested that following the House of Lords' earlier decision in *The Fanti*,[31] it was "open to Miss Dohmann to have held that when the event of insolvency takes place, a contingent right is transferred and the duty arises under section 2 to give information to any person 'claiming that the [insured] is under a liability to him.'"[32] There is judicial support for allowing a plaintiff with a claim against an insolvent insured access to policy information before he has undertaken the costs of litigation.[33] In Scotland, information as to

[27] He suggested that the words "ascertaining" and "enforcing" in section 2 suggested present ascertainability rather than "assisting towards assessment of whether rights have been or may upon certain later events transpire to have been transferred". *Ibid*, at p 141.

[28] *Ibid*, at p 142.

[29] See, for example, RA Taylor, MP (whose proposal for a disclosure obligation was taken up by the Solicitor General), who suggested that third parties should have access to policy information "before they resort to the expensive and uncertain processes of the law". Hansard (HC) 10 April 1930, vol 237, col 2505.

[30] See Sir Jonathan Mance, "Insolvency at Sea" [1995] LMCLQ 34, at 41: "Third party liability either exists or not from the moment it is incurred. Any citizen is free to advise himself, with the aid of lawyers and others, as to his legal position. Why should it be regarded as unreasonable for a third party, if he has a reasonable basis for considering that third party liability exists, to ask for any relevant insurance policy to ascertain whether, if he be right about liability, there will be third party insurance making it worth his while establishing this through the courts?" See also Jonathan Goodliffe, "What is left of the Third Parties (Rights Against Insurers) Act 1930?" [1993] JBL 590, the submissions of both counsel in the *Woolwich* case, Edward Coulson, "Woolwich Building Society v Taylor" [1994] IBFL 69-70 and Philip Rocher and Mark Pring in Insurance Day, 7 September 1995, p 6.

[31] [1991] 2 AC 1, at 32E. *The Fanti* did not involve an application under section 2, but the enforceability of a pay first clause in the rules of a Protection and Indemnity Club providing cover to shipowners. The House of Lords accepted that some form of contingent or conditional right might transfer to the third party on the defendant's insolvency. In the words of Lord Goff of Chievely: "I start from the position that what is transferred to and vested in the third party is the member's right against the club. That right is, at best, a contingent right to indemnity, the right being expressed to be conditional upon the member having in fact paid the relevant claim or expense". See also 31E. The case is discussed further at paras 5.59-5.61 below.

[32] See P Hayward, "The duty to provide information under s 2 of the Third Parties (Rights Against Insurers) Act 1930" [1993] 9 Int ILR 317-319.

[33] *Banque Bruxelles Lambert SA v Eagle Star Insurance Co Ltd*, (unreported), 26 February 1993 where the effect of section 2 of the Act was one of the issues considered by Phillips J in deciding whether to set aside a subpoena. It was, he said, "a perfectly reasonable desire" for a plaintiff involved in costly litigation to know the terms and level of insurance covering the defendant: "one might have expected in a situation such as this the Third Parties (Rights Against Insurers) Act 1930 to enable a plaintiff to ascertain the extent of insurance cover

the identity of the insurer and the terms of the policy may be obtained pre-action if the insured is insolvent under section 1 of the Administration of Justice (Scotland) Act 1972.[34]

THE IMPLICATIONS OF THE JUDICIAL CONSTRUCTION OF SECTIONS 1 AND 2

4.19 In light of the court's approach in the *Post Office* case and in subsequent cases, it appears that third parties cannot sue the insurer for an indemnity or apply for insurance information under section 2 of the Act before the liability of the insured has been established. We now consider the practical consequences of the court's interpretation of sections 1 and 2 of the Act. As we shall see, it is unclear whether English procedural rules allow third parties to join insurers to proceedings against the insured to seek a declaration of future liability.[35] Third parties can seek a declarator against insurers under Scottish law.[36]

Multiple proceedings

4.20 To obtain judgment under the 1930 Act, a third party may have to bring two or more sets of proceedings. Before he can proceed under the Act, he may have to expend considerable time and money pursuing an insolvent defendant who has no interest in the proceedings. Before bringing proceedings to establish the liability of the insured, he may have to apply for a bankruptcy or winding up order against the insured or for an application to restore a dissolved company to the register and for an order allowing him to proceed against an insolvent insured.[37] He may have problems funding all these applications.

4.21 In *Carpenter v Ebblewhite*,[38] an action involving section 10(1)[39] of the Road Traffic 1934, the third party victims of a motor accident argued that they should be able to join in the insured's insurer for such a declaration. They recognised that their cause of action against the insurer had not yet accrued but argued that the desirability of avoiding multiplicity of actions meant that they should be able to proceed against both insured and insurer.

before incurring costs of litigation, because the rationale of that Act is to afford to those who can establish a good claim the protection of insurance of the insolvent company against that liability". He concluded, however, that the court's decision in *Bradley v Eagle Star Insurance Co Ltd* [1989] AC 957 precluded an application for disclosure based on the 1930 Act, although he allowed the application for other reasons. The case is discussed further at para 4.37 below.

34 This provision is not limited to personal injury actions.

35 See paras 4.21-4.23 below and the outline of RSC O 15 and 16 (CCR, O 5, O 12, O 15) and the Draft Civil Proceedings Rules, Part 18 in Appendix B.

36 See paras 4.27-4.29 below.

37 See para 4.50 below.

38 [1939] 1 KB 346.

39 Section 10(1) provides: "If ... judgment in respect of any such liability as is required to be covered by a policy ... against any person insured by the policy, then, notwithstanding that the insurer may be entitled to avoid or cancel, or may have avoided or cancelled, the policy, the insurer shall ... pay to the persons entitled to the benefit of the judgment any sum payable thereunder in respect of the liability ...".

4.22 The Court of Appeal rejected the plaintiffs' claim for a declaration, although their grounds for doing so varied. Greer LJ held that the plaintiffs could not seek a declaration as they had no immediate cause of action against the insurer. This approach appears to have been supported by MacKinnon LJ[40] but Slesser LJ based his decision on his view that, on the facts of the case, to disclose the fact that a defendant was insured would tend to prejudice, embarrass or delay the fair trial of the action.[41] He gave no "concluded opinion" on the issue of the plaintiff's right to seek a declaration against the insurer.

4.23 It appears that *Carpenter v Ebblewhite* is still cited as authority for the principle that "an insurer will not be allowed to be added as a defendant in a negligence action where there is no dispute between him and the other defendants, and the only claim against the insurer is for a declaration of liability to satisfy the plaintiff's claim."[42] We are not aware of any cases where a plaintiff third party has successfully applied for the joinder of an insurer to proceedings against an insured defendant, although it is possible that the court would allow the joinder of the insurer by a third party given the width of the discretion given to the court in RSC Order 15 and in the light of dicta in *Brice v Wackerbarth*[43] and *Wood v Perfection Travel.*[44] Alternatively, it may be that the court is more willing to allow joinder of the insurer by the insured or of the insured by the insurer because of their existing rights and obligations under the insurance contract.

[40] The rights of third parties against insurers under section 10 of the 1934 Act were far wider than they would generally be under the 1930 Act: Under the 1934 Act, the insurer was not generally able to repudiate liability under the insurance contract once the third party had established the liability of the insured. The fact that the majority refused to allow the plaintiff to join the insurer where the insurer had only a very limited ability to refuse to indemnify third parties who established the liability of the insured was evidence of its reluctance to allow the joinder of parties against whom the plaintiff has no immediate cause of action.

[41] Pages 361-362. On the facts, he held that it was not the case that, if the plaintiffs succeeded, the insurers would automatically be liable. It is interesting to note that one of the reasons given by the Court of Appeal for their decision in the *Post Office* case was court practice which had prevented the parties from disclosing to a jury the fact that the defendant was insured. This practice changed following *Harman v Crilly* [1943]1 KB 168, which postdated *Carpenter v Ebblewhite.* In *Brice v Wackerbarth* [1974] 2 Lloyd's Rep 274, this change in practice was referred to by Denning LJ in support of the decision of the Court of Appeal to allow an insured to join an insurer to proceedings started by an injured plaintiff. See para 4.24 below.

[42] See RSC O 15, r 4(4), O 16, r 4(13) and O 18, r 19(14). Interestingly, however, the commentary to RSC O 15, r 4(4) proceeds as follows: "*Quaere,* whether in such case leave under this rule may now be given". (This may be because there is no longer a court practice barring disclosure of a defendant's insurance cover in the course of a hearing. See n 41 above). In *Meadows Indemnity Co Ltd v Insurance Corporation of Ireland plc* [1989] 2 Lloyd's Rep 298, the Court of Appeal held that a reinsurer was not entitled to seek a declaration against an insurer in respect of the liability of the reinsurer to the insurer and of the insurer to the insured until the liability of the insurer had been established. Referring to *Bradley v Eagle Star Insurance Co Ltd* [1989] 1 Lloyd's Rep 465 and dicta of Diplock LJ in *Gouriet v Union of Post Office Workers* [1978] AC 435, at 501, Neill LJ held that, although there was good sense in a person being able "to establish by means of declaration the legal rights of a third person if those rights will in due course directly affect him as an insurer ... such a use of a declaration is not at present admissible.

[43] [1974] 2 Lloyd's Rep 274.

[44] [1996] LRLR 233. See para 4.25 below.

4.24 *Brice v Wackerbarth*[45] concerned the application by an insured party to join an insurer into an action against him by an injured plaintiff.[46] The court granted the application, Lord Denning referring to the importance of preventing multiplicity of actions.[47]

4.25 In *Wood v Perfection Travel*[48] the Court of Appeal allowed the application by an insurer to be joined to an action brought by a third party against a dissolved company which had been restored to the register.[49] The problem which had faced the insurer was described as follows by Hirst LJ:

> The present problem arises because the insurers wish to dispute both [the insured's] liability to the plaintiff (the liability issue) and their own liability to [the insured] (the coverage issue) ... Under the coverage issue, they wish to contend that they can avail themselves of the exclusion clause ... In relation to liability, they say that the facts cannot be properly scrutinised and adjudicated unless they assume conduct of [the insured's] defence; this they would readily be prepared to do under the subrogation clause, provided that it was agreed between them and the plaintiff that they could assume conduct of the defence under that clause without prejudice to the coverage issue. Their anxiety is that, without such agreement, there is a risk that they may in consequence, find themselves estopped from disputing coverage.
>
> This anxiety is based on a passage in MacGillivray and Parkington on Insurance Law, 8th edition paragraph 1999 where it is stated that: "... care is needed in undertaking the defence of the claim on behalf of the

45 [1974] 2 Lloyd's Rep 274.

46 Under RSC O 16, r 1, set out in Appendix B. See also Rule 26.1(1)(a) of the Rules of the Scottish Court of Session, also set out in Appendix B and *Barton v William Low and Co Ltd* 1968 SLT (Notes) 27.

47 Citing RSC O 16, r 1, set out in Appendix B. He referred also to the fact that, since *Harman v Crilly* [1943] 1 KB 168, it was permissible to bring in insurers as third parties (see para 4.22, n 41 above) and rejected the argument that the decision in the *Post Office* case would prevent joinder: "Now I see nothing in the clause or in the general law which prevents these third party proceedings going on. Even if they continue, the Judge will give his decision in the main action before he decides in the third party proceedings. So the liability of the insured will have been ascertained - judgment will have been given against the insured - before the decision in the third party proceedings. In any case, there is nothing to prevent the insured asking for a declaration that, if he is liable, he is entitled to indemnity from the third parties". See also the judgment of Roskill LJ, p 278.

48 [1996] LRLR 233.

49 Under RSC O 15, r 6(2)(b)(ii), set out in Appendix B. The Court of Appeal distinguished *Spelling Goldberg Productions v BPC Publishing Ltd* [1981] RPC 280, where it had rejected an application for joinder under RSC O 15, rule 6(2) Bridge LJ had held in that case that "what is contemplated is that, at the time when an order for joinder is made under this provision, the question or issue arising out of, or relating to, or connected with the relief or remedy claimed in the cause already arises between the party seeking to be joined and one or other of the existing parties to the litigation". The Court of Appeal distinguished *Spelling* on the basis that, in that case, "the possibility of an issue arising between any of those seeking to intervene and the parties to the action was wholly speculative". Rule 24.1(2)(d) of the Rules of the Scottish Court of Session provides that insurers can apply to become (or be sisted as) parties to the proceedings in respect of any interest they have. See Appendix B and see *Thomson v Bose*, unreported, 17 December 1993.

assured, or else the insurers may become precluded from denying liability under the policy".

4.26 The possibility of this problem arising[50] was overcome by the court allowing the insurer to be joined to the third party's action in its own name.[51]

4.27 In Scotland, an action may contain "eventual conclusions", conclusions which depend on some other eventuality in the action.[52] Thus, in an action by a third party against an insolvent insured to establish the insured's liability, it appears that a declarator may be sought against the insurer that, in the event of liability being established, the insurer is liable to pay the third party in terms of the policy. A declarator was granted in *Bell v Lothiansure Ltd*[53] although the insurer had conceded the liability of the insured and was defending on the basis that there was no cover under the policy. In *Landcatch Ltd v Gilkes*,[54] it was held that the insurer and the insolvent insured could not be regarded as jointly and severally liable and the opinion was expressed that the correct way of bringing the insurer in to the proceedings was by way of a declaratory conclusion. Similarly, in *McDyer v Celtic Football and Athletic Co Ltd*,[55] Lord Macfadyen said that it could be competent for a pursuer to seek declarator as there was sufficient connection between a claim for damages and a conclusion for declarator that if it succeeded, there would be liability on the insurer by virtue of the 1930 Act.

4.28 Scottish procedural rules allow the insured to apply for a third party notice.[56] The insurer may then take pleas as to his own liability to the insured under the terms of

[50] It is not clear whether or not the insurer is estopped in this way: Professor Merkin has suggested that "the legal basis for this risk is unclear, but after *Wood* it plainly cannot be discounted". See "When is the Reinsurer Liable?" (1996) Insurance Law Monthly, vol 8(1) p 4. The recommended practice now is for insurers to include "non-waiver" agreements in the insurance contract which allow them to defend the liability action against the insured whilst reserving their rights to dispute cover. See M Clarke, *The Law of Insurance Contracts* (3rd ed 1997) p 442. Such agreements were not included, however, in occurrence based liability policies written many years ago under which insurers may still face long-tail liability.

[51] Hirst LJ commented as follows: "The reality of these proceedings is that although technically the issue raised in the action is one between the plaintiff and [the insured], the true protagonists are the plaintiff and the insurers ... .The relationship between a plaintiff suing an insolvent defendant and the insurers of the defendant at risk under the provisions of the 1930 Act is very different. In our judgment the issue which arises in the action between the plaintiff and [the insured] can properly be said to be an issue which "may exist" between the insurers and each of the parties to the action within O 15, r 6(2)(b)(ii)". The implications for the insurer of not being joined into the proceedings would potentially have been greater than they would for third parties unable to join insurers into proceedings against the insured, however, as the insurer would have lost its first line of defence. The court stressed that joinder was in the interests of justice to allow the insurer to challenge the third party's claims.

[52] McLaren, *Court of Session Practice*, p 296; Macphail, *Sheriff Court Practice*, para 9-87.

[53] 19 January 1990, Lord Cameron of Lochbroom, Second Division's refusal of reclaiming motion 1993 SLT 421.

[54] 1990 SLT 688.

[55] 1997 GWD 30-1536.

[56] Rule 26 of the Court of Session Rules. See Appendix B. See also *Winchester v Ramsay* 1966 SLT 97 and *Barton v William Low & Co Ltd* 1968 SLT (Notes) 27.

the policy. Once the insurer has been brought in, the third party pursuer could amend his pleadings so as to include a declaratory conclusion against the insurer.[57]

4.29 It is not clear whether the insurer is entitled to sist himself in a third party's action against the insured in order to take pleas as to the insured's liability and his own liability to the insured. The general rule is that any person having sufficient title and interest may apply to be sisted as a party to an action[58] and this requirement will probably be met if the insured is insolvent or verging on insolvency.[59]

4.30 The requirement that third parties bring proceedings to establish the liability of the insured before they can bring proceedings against the insurer under the 1930 Act causes problems to third parties and to others. Consideration is given below to whether or not third parties should be allowed to proceed directly against the insurer or against both the insured and the insurer in the same set of proceedings.[60]

Funding actions under the Act and related proceedings

4.31 A third party[61] who has to bring two or more sets of proceedings before he can obtain judgment under the Act will face legal fees and costs in respect of each set of proceedings. Many of the actions brought under the 1930 Act involve employers' liability and other negligence claims by plaintiffs who may be unable to fund them.[62] The means of funding legal proceedings, which include legal aid, conditional fee agreements and legal expenses insurance, are currently under review.[63]

[57] Rule 24 of the Court of Session Rules, which would also allow such an amendment on application by the third party pursuer were the insured to become insolvent after the action against him had commenced.

[58] *Muir v Glasgow Corporation* 1917 2 SLT 106.

[59] Policies usually allow the insurer to take over the insured's defence in any event. See para 12.18 below.

[60] See Part 12.

[61] The insurer, who will usually be conducting the insured's defence, may also face two sets of proceedings and two sets of costs although, in many cases, the insurance contract will provide that the insurer's costs are to be deducted from any sums recovered under the policy. Where the third party's case against an insolvent insured who is supported by an insurer succeeds and the insurer has a clear contractual obligation to indemnify the insured against his liability to pay the costs of the third party, the court may make an order under s 51 of the Supreme Court Act 1981 requiring the insurer to pay costs directly to the third party. See *Murphy v Young & Co's Brewery plc* [1997] 1 All ER 518 at 528 and *T G A Chapman Ltd v Christopher*, *The Times* 21 July 1997.

[62] See para 2.10 above and Appendix C.

[63] Following publication of "*The Price of Success*", a report by Stella Yarrow of the Policy Studies Institute, in October, the government is consulting on extending the scope of conditional fee regulations. See the Lord Chancellor's address to the Solicitor's Annual Conference, 18 October 1997. Were the Lord Chancellor's proposals to be implemented, many civil actions are likely to be funded by conditional fee arrangements rather than by legal aid and there will be an increase in the use of legal expenses insurance. As the figures in Appendix C reveal, a substantial proportion of claims under the Act relate to injuries at work. The TUC is proposing to assist employees in obtaining legal advice to pursue claims for compensation from employers. See John Monks' speech to AIRMIC, 3 November 1997.

4.32 Some claimants may meet the financial criteria entitling them to legal aid but, if they cannot show that they are likely to recover from the insolvent insured's insurer, may not be granted legal aid for their proceedings against the insured.[64]

4.33 Other ways in which third parties may be able to fund proceedings are through conditional fee agreements and legal expenses insurance. Since 1995, solicitors have been able to enter into conditional fee agreements with clients bringing particular types of claim, including those relating to personal injury.[65] Such arrangements are commonly known as "no win, no fee" arrangements as the claimant is not responsible for his lawyer's costs unless he wins the case (although he will usually be responsible for his lawyer's disbursements and the other side's costs and disbursements). If he does win, the solicitor's fee is usually based on a percentage of the sum recovered. In Scotland, agreements as to conditional fees have been permitted since 1992. Advocates, solicitors and their clients may agree that fees are payable only in the event of success and the fees may be up to twice the normal fees.[66]

4.34 Unless the chances of the third party's claim succeeding are high, a solicitor may be unwilling to enter into a conditional fee agreement with him. The early disclosure of the existence of insurance cover may therefore be useful in persuading solicitors to take third parties' cases under conditional fee arrangements.

4.35 Legal expenses insurance has been available in this country since the early 1980s. Currently, most claimants bringing proceedings under the 1930 Act are unlikely to have legal expenses insurance but its use by those entering into conditional fee agreements is likely to increase.

Access to policy information

4.36 The third party may not obtain policy information until he has established the liability of the insured.[67] Once he obtains disclosure,[68] he may discover that the

It appears that the insurance industry is backing this initiative, see "TUC Rehabilitation call wins insurers' support," Insurance Day, 5 November 1997.

64 We discuss the problems caused by the inability of third parties to obtain policy information further below. See paras 4.36-4.37.

65 Although the third party's claim against the insurer is a claim under the Act rather than for death or personal injury, the conditional fee regulations may apply: they were intended to cover non-specified proceedings if they formed part of an action involving specified proceedings. This question has not yet come before the courts. There are proposals to extend the scope of regulations in any event. See para 4.31 above.

66 Solicitors (Scotland) Act 1980, s 61A, added by s 36(3) of the Law Reform (Miscellaneous Provisions)(Scotland) Act 1990; Act of Sederunt (Fees of Solicitors in Speculative Actions) 1992, SI 1992/1879 and for advocates SI 1992/1897.

67 Although, in some cases, it may be in the interests of the insurer to give early disclosure voluntarily if it is clear that he has no duty to indemnify the insured. See para 6.12 below. Third parties in Scotland may be entitled to earlier disclosure under s 1 of the Administration of Justice (Scotland) Act 1972. See para 4.18 above.

68 In many cases, the third party may be unlikely to obtain disclosure of relevant information from the insured. Records may not have been kept and an insured who has been declared wound up or declared bankrupt may not be willing or able to assist the third party with his

insurer has no duty to indemnify the insured under the insurance contract. The third party may discover, for example, that certain policy conditions have been breached by the insured, entitling the insurer to repudiate cover.[69] In some cases, the third party might have been able himself to meet those conditions (for example those requiring notice of claims to be given to the insurer) had he known of their existence.

4.37 An interlocutory application in the case of *Banque Bruxelles Lambert v Eagle Star Insurance*[70] illustrates the wasteful court proceedings that may follow from lack of information as to insurance cover. The plaintiff had lent money on the basis of a surveyor's negligent valuation. One of the defendants to the plaintiff's action, joined to that action in May 1991, was a firm of professional advisers which went into voluntary liquidation. The plaintiff was unable to obtain disclosure of the defendant's insurance position but pursued its action against the defendant. Settlement was finally reached with the defendant's insurer after the trial of the action had started, nearly a year and a half after the defendant had been joined, in October 1992. Another of the defendants, also joined in May 1991, had insurance cover arranged in layers. Its first and third layer insurers purported to repudiate cover at a late stage and it was only following this that the defendant disclosed details of its insurance cover and of the insurers' grounds for purported repudiation. The costs incurred by the plaintiff against these two defendants ran into millions of pounds.[71]

claim. The insured is likely to assume that the insolvency practitioner or official receiver will manage third party claims and it is from those parties that the third party is often more likely to obtain disclosure.

69 The ability of insurers to rely, as against third parties, on their defences against the insured is discussed at Part 5 below.

70 *The Times* 21 February 1995. The case was finally heard by the House of Lords as *South Australia Asset Management v Forke Montagu* [1996] 3 WLR 87.

71 The value of the plaintiff's claim was in the tens of millions of pounds. We suggest at Part 13 below that there should be an earlier duty to disclose policy information. Philips J suggested that it was a "perfectly reasonable desire" for a plaintiff involved in costly litigation to know the terms and level of the defendant's insurance. See para 4.18, n 33 above.

Third parties may have to restore a dissolved company to the register of companies and establish its liability before they can proceed against the insurer[72]

Section 651[73] of the Companies Act 1985

4.38 As we have seen, the requirement that the third party establish the liability of the insured before acquiring rights to proceed against the insurer meant that, in *Bradley v Eagle Star Insurance Co Ltd*,[74] the third party could never acquire rights under the 1930 Act as section 651 of the Companies Act 1985 provided at that time that an application to restore a dissolved company to the register had to be made within two years of the date of dissolution and that period had expired.[75] Following the *Bradley* case, it was appreciated that the limitation period contained in section 651 was inadequate, particularly in cases involving insidious diseases, such as that suffered by Mrs Bradley, where the injury might take a long time to manifest itself.[76] The Limitation Act 1980 allowed for the three year limitation period for death and personal injury claims to run from the time when the injury was discoverable[77] and gave the court an absolute discretion to extend time limits in personal injury cases,[78] but third parties might not be able to take advantage of these provisions if the wrongdoing company had been dissolved in the interim.

4.39 Amendments to section 651 were introduced by section 141 of the Companies Act 1989.[79] Under the amended section, the two year time limit does not apply to actions involving death or personal injury.[80] Third parties bringing such actions may now apply to resurrect a dissolved company at any time after its dissolution, although the two year limit continues to apply to other types of actions. The

[72] Dissolution of a company usually results from winding up under ss 202-205 Insolvency Act 1986. It may also result from s 652 Companies Act 1985 if the registrar has reasonable cause to believe that the company is not carrying on business or is not in operation or, where a winding up has commenced, that no liquidator is acting or that the affairs of the company are fully wound up and the returns required to be made by the liquidator have not been made for six consecutive months. In certain circumstances other than winding up, the company may apply itself to be dissolved under Companies Act s 652A-F (as amended by section 13 and Schedule 5 of the Deregulation and Contracting Out Act 1994).

[73] The wording of s 651 is set out in Appendix A. While an application under s 653 is expressly for restoration to the register, under s 651 the application is for a declaration that a company's dissolution is void. Nevertheless it is often described as an application to restore the company to the register (see, for example, *Re Workvale Ltd* [1992] 1 WLR 416, 420E and *Re Oakleague Ltd* [1995] 2 BCLC 624, 628I).

[74] [1989] AC 957.

[75] Mrs Bradley could not, therefore, restore the company to the register so could not bring proceedings against it to establish its liability. See paras 4.6-4.7 above.

[76] See also para 2.20 above, where we considered problems which might be faced by those with long tail claims under non-renewed claims made policies.

[77] Section 11 of the Limitation Act 1980.

[78] Section 33 of the Limitation Act 1980.

[79] Article 75 of the Companies (No 2)(NI) Order 1990.

[80] S 651(5). See Appendix A. At para 17.17, we suggest that the limitation period for restoring companies to the register should be the same in all types of proceedings.

amended section was made retroactive to allow Mrs Bradley's action and other outstanding cases to proceed.[81]

Limitation of the third party's underlying claim

4.40 Under the amended section 651(5), an order for restoration may be made unless "it appears to the court that the proceedings would fail by virtue of any enactment[82] as to the time within which proceedings must be brought." Section 651(6) provides that section 651(5)does not affect the power of the court to direct that the period between the dissolution of the company and the making of the order be disregarded for limitation purposes.[83]

4.41 The effect of section 651, subsections (5) and (6) was considered by the Court of Appeal in *Re Workvale*.[84] Scott LJ held that:

> in a case where the primary limitation period has expired the judge should, in my opinion, ask himself whether the applicant has an arguable case for an order under section 33 of the Limitation Act 1980. If there is an arguable case for an order under section 33, then it cannot, in my judgment, be predicated that "the proceedings would fail".

4.42 Given the wide discretion given to the court by section 33 of the 1980 Act, it appears, following *Re Workvale,* that many applications under section 651(5) will be granted without lengthy consideration by the court as there is likely to be at least an arguable case that a section 33 order could be granted.[85] Disputes as to the application of section 33 of the Limitation Act are likely, therefore, to be postponed to the substantive hearing of the third party's claim against the restored company, although this will not always be the case.[86] It has been argued that it is inappropriate for the Companies Court hearing the application to restore to be required to consider limitation at all.[87]

[81] Section 141(4) Companies Act 1989 which provides, however, that applications cannot be made to restore companies dissolved more than twenty years before the commencement of that section (16th November 1989). At para 17.18 below, we seek consultees' views on whether this limitation should be removed.

[82] In most cases, the relevant provisions will be sections 11 and 33 of the Limitation Act 1980. See para 4.38 above.

[83] There is doubt as to the extent of the court's powers in Scotland under s 651(6). See para 4.43 below.

[84] [1992] 1 WLR 416. This case dealt with the exercise of the power to make such on order in relation to claims for personal injury. For its exercise in relation to other types of claim see Evans-Lombe J in *Re Mixhurst Ltd* [1994] 2 BCLC 19, 29.

[85] This was confirmed by our survey of applications to restore companies to the register. See para 4.44 below.

[86] See, however, *Re Philip Powis Ltd, The Times* 30 April 1997.

[87] See LCB Gower, *Principles of Modern Company Law* (5th ed 1992) p 781, n 62: "If the court should decide that the trial court would refuse to allow the action to proceed, it means that the intending plaintiff is deprived at an earlier stage of the possibility of pursuing his claim against the company or its insurers merely because the company has been dissolved through no fault of his; and if it decides the contrary, the trial court will have to consider the question all over again and at greater length".

4.43 There is doubt as to the extent of the courts' powers in Scotland under section 651(6). Courts have power under section 19A of the Prescription and Limitation (Scotland) Act 1973 to extend the limitation period for death or personal injury cases, but have no power to extend any prescriptive period.[88]

Procedures for restoring companies to the register

4.44 We now consider to what extent the procedure which the third party must go through to apply for a company to be restored to the register causes problems in practice. To enable us better to assess this issue, we conducted, in December 1996 to January 1997, a survey of applications to restore companies to the register made between 1994 and 1996.[89] A summary of the findings of this survey appears at Appendix C.

4.45 Third parties may be uncertain as to how to proceed because both sections 651 and 653 of the Companies Act 1985 provide for applications to be made for the restoration of companies to the register.[90] The requirements of each section are different, but it appears that, in some circumstances, the applicant can choose under which section he wishes to proceed.[91]

4.46 The third party must apply by originating summons or motion under RSC Order 102, a copy of which must be served on the Registrar of Companies. In some of the cases which we looked at, the insurer was also made a respondent to the application. A notice of the application must also be served on the Treasury Solicitor[92] (as the representative of the Crown).[93]

4.47 In many of the applications which we examined, applicants filed long affidavits setting out the particulars of their underlying claims against the company, as well as affidavits of service detailing the parties who had received notification of their applications.

4.48 These requirements are likely to lead to delay and to the third party incurring legal costs. The vast majority of the applications which we looked at were made by solicitors rather than by claimants themselves.

4.49 The hearing of the application is by a Companies Court Registrar and usually takes about fifteen minutes. It is normally only attended by the applicant, although

[88] We discuss the prescriptive periods governing the obligations of the insured and of the insurer at para 9.19-9.21 below.

[89] We would like to express our gratitude to Registrar Buckley and to others at the Companies Court for their assistance to us.

[90] See para 4.38, n 73 above. The wording of both sections is set out in Appendix A.

[91] *Re Thompson & Riches* Ltd [1981] 1 WLR 682; *Re M Belmont & Co Ltd* [1952] Ch 10; *Re Test Holdings (Clifton) Ltd* [1970] Ch 285; *Re Spottiswoode, Dixon and Hunting Ltd* [1912] 1 Ch 410. This uncertainty is criticised by Professor Gower. See LCB Gower, *Principles of Modern Company Law* (6th ed 1997) at p 849.

[92] Or, where appropriate, on the Duchy of Lancaster or the Duke of Cornwall.

[93] This is because, on dissolution, the assets of a dissolved company are deemed to vest in the Crown as *bona vacantia*. The applicant usually obtains a letter from the Treasury Solicitor confirming the Crown's consent to the restoration and exhibits this letter to his application.

a few of the applications which we examined were complicated by attempts by the dissolved company's insurers to intervene and to argue that, on the merits of the third party's underlying claim, an order to restore should not be made.[94] In the cases we surveyed, every application to restore was granted. The costs of the application (such as court costs and the costs of the Treasury Solicitor)[95] are awarded against the applicant who must also pay any costs incurred by the Register of Companies and, of course, any costs which he himself has incurred.[96]

4.50 Third parties whose applications to restore are granted will then have to apply for leave to proceed against the insolvent company,[97] and must then establish its liability. They may obtain judgment in default because there will be no-one to defend the restored company or they may find that the insured's defence is conducted by his insurer. Given that the restored company is unlikely to play any part in those proceedings, the question must be asked whether any real purpose is served in requiring third parties to restore the company to the register.[98]

4.51 In Scotland, an application under section 651 or 653 is made by way of petition intimated to the Lord Advocate and the Registrar of Companies in Scotland.[99] In *Percy v Garwin Ltd*,[100] it was suggested that a petition should be granted unless there were no prospects of the claim proceeding further. However, in *McShane v*

[94] Such intervention was rare, however. In one case, the court opposed the insurer's application on the ground that it had no locus standi. The insurer is likely instead to await the outcome of the application to restore and to conduct the defence of the insured in subsequent proceedings brought by the third party, either by exercising its rights under the insurance contract or by applying to the court to be joined. See *Wood v Perfection Travel* [1996] LRLR 233, discussed at para 4.25 above.

[95] The third party may have to undertake to inform the Register of proposed litigation against the restored company and on the conclusion of the proposed litigation so that the Register can start the procedure for striking the company off again. The Register's fees in such cases are usually assessed at £250.

[96] A third party who had started proceedings against the company before it was dissolved may already have incurred some costs. These costs are likely to be largely wasted as any such action ceases on the date of dissolution and cannot be revived even if the company is subsequently restored. See *Foster, Yates & Thorn Ltd v HW Edgehill Equipment Ltd* (1978) 122 SJ 860 and *In re Philip Powis Ltd The Times* 30 April 1997. The third party should, in most cases, have been able to delay dissolution until his action has finished. See ss 201 and 205 Insolvency Act 1986. The Treasury Solicitor estimates that straightforward applications cost an average of around £1,500 in legal fees and costs.

[97] Following the restoration of companies which have been compulsorily wound up, the Official Receiver will become liquidator ex officio and may be involved in administrative work for which he will not be remunerated. Sections 130(2) and 285 Insolvency Act 1986. In Scotland, leave is not required. See para 12.18, n 45 below.

[98] In the words of Lord Templeman in his dissenting judgment in the *Bradley* case, "To restore ... the company in these circumstances would do no more than authorise Mrs Bradley to make use of a name carved on a tombstone. The use of the name could not restore life to the skeleton". See para 4.7, n 13 above. We give our provisional view at para 12.23 below that a third party claimant under an amended Act should be able to proceed against the insurer alone in cases where the insured is a dissolved company which has been struck off the register.

[99] McBryde and Dowie, *Petition Procedure in the Court of Session* (2nd ed) pp 58-59.

[100] 6 December 1990, Lord Weir.

Comet Group plc,[101] a sheriff court petition under section 653 was refused on the ground that the company was merely a tenant of the property and could not be said to have been "in operation". This decision has been criticised[102] and is out of line with Court of Session practice.

[101] 1994 SCLR 1077.

[102] D P Sellar "Commercial Law Update", 1995 JLSS 267.

PART 5
THE RIGHT OF INSURERS TO RELY ON DEFENCES

5.1 As we saw in Part 4 the 1930 Act operates by transferring the insured's rights against the insurer to the third party. Subject to anti-avoidance provisions contained in the Act and to certain other exceptions, the insurer has, therefore, the same defences against the third party as he would have had against the insured. These might include rescission of the insurance contract for non-disclosure of material facts and a denial of liability on the grounds of a breach of a policy condition (for example, one requiring the insured to give timeous notice of the third party's claim or to keep insured premises secure).

5.2 An insured heading towards bankruptcy or winding up may be increasingly likely to breach policy terms because of his financial position. The nature of many of these terms may be such that they can only be met by the insured himself. Third parties may not be able to meet even those terms which, in principle, they could fulfil themselves (such as notice provisions) because they are not aware of them in time or lack the financial resources to do so.

5.3 In this Part, we consider first the nature of the rights transferred to third parties under the Act.[1] We then consider anti-avoidance provisions contained in sections 1(3) and 3 of the Act.[2] Next, we look at other statutory and non-statutory restrictions on the ability of insurers to rely on defences.[3] Finally, we look at defences commonly relied on by insurers and at the particular problems which these may cause to third party claimants under the Act.[4]

THE RIGHTS WHICH ARE TRANSFERRED TO THE THIRD PARTY ARE THOSE WHICH THE INSURED WOULD HAVE HAD AGAINST THE INSURER

5.4 As we have seen, section 1 of the Act transfers the rights of the insured against the insurer to the third party on the happening of one of the insolvency situations set out in the Act and on the incurrence of liability by the insured.[5] Section 1 has been interpreted as transferring those rights subject to the conditions and defences in the insurance policy: in the words of Harman LJ in *Post Office v Norwich Union Fire Insurance Society Ltd*,[6] the third party cannot "pick out the plums and leave the duff behind". The court has stressed that the Act operates to place the third party in the position of the insured. Lord Brandon, for example, in *The Fanti*,[7] said, "It is

[1] See paras 5.4 and 5.5 below.

[2] See paras 5.6-5.9 below.

[3] See paras 5.10-5.13 below.

[4] See paras 5.14-5.67 below.

[5] Interpreted as meaning the establishing of the insured's liability to the third party. See para 4.5 above.

[6] [1967] 2 QB 363, 376. See paras 4.3-4.5 above.

[7] [1991] 2 AC 1, at p 29.

abundantly clear from the express terms of the Act of 1930 that the legislature never intended, except as provided in section 1(3) ... to put a third party in any better position as against an insurer than that of the insured himself."

5.5 The Scottish courts have held that the transfer of the insured's rights against the insurer under section 1 of the 1930 Act is a statutory assignation.[8] The third party's rights are those of the insured and all the pleas open to the insurer against the insured are also available against the third party.[9]

ANTI-AVOIDANCE PROVISIONS

5.6 Those drafting the 1930 Act were aware of the possibility that insurers might seek to avoid or minimise their liability under the Act by making their liability conditional on the solvency of the insured or by settling their claim with the insured before the third party acquired rights under the Act. Provisions were, therefore, included in sections 1 and 3 of the Act making such terms and agreements of no effect.[10]

5.7 Section 1(3) makes void any contract of insurance insofar as it "purports, whether directly or indirectly, to avoid the contract or to alter the rights of the parties" on the happening of one of the insolvency events set out in the Act. Any term which purported, for example, to end or to restrict cover on a winding up or bankruptcy order being made against the insured would be of no effect.[11]

5.8 Section 3 provides that "no agreement made between the insurer and the insured after liability has been incurred to a third party and after the commencement of the bankruptcy or winding-up...shall be effective to defeat or affect the rights transferred to the third party under this Act, but those rights shall be the same as if no such agreement...had been made."[12]

5.9 Section 3 only prohibits agreements reached between the insurer and the insured after the happening of one of the insolvency events set out in the Act. It does not protect third parties where the agreement between the insurer and the insured was made before this point.[13] It is thought that a similar position would be adopted in

[8] *Greenlees v Port of Manchester Insurance Company* 1933 SC 383.

[9] In *Cunningham v Anglian Insurance Co Ltd* 1934 SLT 273, the third party was held to be bound by an arbitration clause in the policy. See also *Bell v Lothiansure Ltd* 19 January 1990, Lord Cameron of Lochbroom.

[10] Also, under section 2, any provision purporting to prohibit the disclosure of information under that section or to avoid or alter the insurance on such disclosure is of no effect. See para 3.2 above.

[11] Provisions in the rules of Protection and Indemnity Clubs making the insurer's duty to indemnify the insured conditional on the insured making prior payment to the third party have been held not to fall foul of s 1(3). See *The Fanti* [1991] 2 AC 1 (discussed at paras 5.59-5.62 below) where the House of Lords distinguished the inability of the insured to pay from the insolvency situations set out in the Act.

[12] The full wording of s 3 is set out in Appendix A. At common law, the insurer and insured could agree to limit the insurer's liability to the insured. See *Rowe v Kenway and United Friendly Insurance Co* (1921) 8 Ll LR.

[13] In *Normid Housing Association Ltd v Ralphs* [1989] 1 Lloyd's Rep 265, the Court of Appeal held that, while it was clearly arguable that an insured settling its claim with its insurer was

Scotland. It is possible, therefore, that some companies or individuals heading towards insolvency might be tempted to compromise their claims against insurers.[14]

OTHER RESTRICTIONS ON THE ABILITY OF INSURERS TO RELY ON DEFENCES AGAINST THIRD PARTIES

The Employers' Liability (Compulsory Insurance) Act 1969

5.10 As we discussed above, a number of statutes provide for compulsory insurance to be taken out by certain persons and in respect of certain activities.[15] These statutes include the Road Traffic Act 1988 and the Employers' Liability (Compulsory Insurance) Act 1969, both of which also prohibit insurers from relying, as against third party claimants, on certain defences which they would have against the insured under the insurance contract. Whereas the Road Traffic Act 1988 provides a specific regime of third party rights against insurers on the bankruptcy of an insured driver,[16] however, employees proceeding against the insurer of an insolvent employer must do so under the 1930 Act.

5.11 Regulation 2 of the Employers' Liability (Compulsory Insurance) General Regulations 1971, made under the Employers' Liability (Compulsory Insurance) Act 1969 provides as follows:

> (1) Any condition in a policy of insurance issued or renewed in accordance with the requirements of the Act after the coming into operation of this Regulation which provides (in whatever terms) that no liability (either generally or in respect of a particular claim) shall arise under the policy, or that any such liability so arising shall cease -
>
> (a) in the event of some specified thing being done or omitted to be done after the happening of the event giving rise to a claim under the policy;
>
> (b) unless the policy holder takes reasonable care to protect his employees against the risk of bodily injury or disease in the course of their employment;

giving up its rights under the policy for a consideration substantially below its true value, the third party plaintiff had no right to prevent the settlement. The third party had no rights until the happening of one of the insolvency events set out in the Act and, until then, the insured was free to deal with his assets. The Court of Appeal set aside a mareva injunction which the third party had obtained to restrain the insured from settling the claim.

[14] It is possible that third parties could persuade insolvency practitioners to exercise their powers to set aside transactions at an undervalue and transactions defrauding creditors under ss 238(4), 339(3), 242, 243 and 423 to 425 of the Insolvency Act 1986 and ss 34 and 36 of the Bankruptcy (Scotland) Act 1985. Insolvency practitioners would have to believe that this would be of benefit to the insured's estate, however, and we are not aware of any cases where this has happened. We seek consultees' views at para 12.47 below on whether the Act should provide for the avoidance of settlements reached by the insurer and the insured before the happening of one of the insolvency events set out in the current Act.

[15] See paras 2.4-2.5 above.

[16] Section 153 of the Road Traffic Act 1988. Where the insolvent driver is uninsured, the third party can recover from the Motor Insurers Bureau.

(c) unless the policy holder complies with the requirements of any enactment for the protection of employees against the risk of bodily injury or disease in the course of their employment; and

(d) unless the policy holder keeps specified records or provides the insurer with or makes available to him information therefrom, is hereby prohibited for the purposes of the Act.[17]

5.12 Insurers will not be able to rely, for example, on breaches of notice requirements which occur after the date of the event giving rise to the liability of the employer to the employee.[18]

Insurers' Codes of best practice

5.13 Insurers will not always insist on their strict rights where there has been non-disclosure, misrepresentation or breach of warranty. They may voluntarily choose not to rely on certain defences[19] or may be bound by codes of best practice, such as the Statement of General Insurance Practice issued by the Association of British Insurers in 1986.[20] It should be noted, however, that the Statement applies only to policyholders resident in the United Kingdom and insured in their private capacity and that paragraph 2(b) does not apply to Marine and Aviation policies.[21] Also, it is not clear whether insurers would consider themselves bound by the Statement when dealing with the claims of third parties under the Act. Most, but not all insurers submit to this or other voluntary codes. Paragraphs 2(a) and (b) of the Statement provide as follows:[22]

2(a) Under the conditions regarding notification of a claim, the policyholder shall not be asked to do more than report a claim and subsequent developments as soon as reasonably possible except in the case of legal processes and claims which a third party requires the

[17] Made under section 1(3)(a) of the 1969 Act. If implemented new draft regulations would, in the context of agreed excesses, also prohibit conditions requiring the first amount of any claim to be paid before the liability of the insurer was incurred. See para 2(2) of the draft Employers' Liability (Compulsory Insurance) General Regulations, annexed to a 1997 Consultative document published by the Department of the Environment, Transport and the Regions. We discuss the use of pay first conditions in the rules of Protection and Indemnity clubs at paras 5.58-5.65 below.

[18] We seek consultees' views at para 14.18 below on whether the ability of insurers to rely on defences against third parties under an amended Act should be restricted by reference to when those defences arose.

[19] Protection and Indemnity clubs usually refrain, for example, from relying on pay first clauses when the third party's claim relates to death or personal injury. See para 5.62 below.

[20] Revised in 1995. Some changes in insurance practice resulted from recommendations made by the Law Commission in its consultation paper and report on Non Disclosure and Breach of Warranty (1980) Law Com No 104. See para 1.16, above and para 14.1, n 1 below.

[21] See para 2.7 above. Also, the Codes may not always be followed by insurers. Some of the decisions of the Insurance Ombudsman against insurers have been made on the basis of the insurer having acted inconsistently with the Codes. See the Insurance Ombudsman Bureau's Digest of Annual Reports and Bulletins, 1981-1995 C.16-C.20.

[22] Similar provisions are contained in the Statement of Long-Term Insurance Practice 1986.

policyholder to notify within a fixed time where immediate advice may be required.

(b) An insurer will not repudiate liability to indemnify a policyholder:-

(i) on grounds of non-disclosure of a material fact which a policyholder could not reasonably be expected to have disclosed;

(ii) on grounds of misrepresentation unless it is a deliberate or negligent misrepresentation of a material fact;

(iii) on grounds of a breach of warranty or condition where the circumstances of the loss are unconnected with the breach unless fraud is involved.[23]

DEFENCES COMMONLY RELIED ON BY INSURERS

5.14 We look now at the following defences commonly relied on by insurers and at the particular problems which they cause to third party claimants:[24]

(i) misrepresentation and non-disclosure;

(ii) breaches of notice provisions;

(iii) arbitration clauses;

(iv) breaches of the duty to provide information and assistance;

(v) breaches of conditions relating to the duty of the insured to comply with safety and other regulations/preserve the assets/business insured eg to maintain security;

(vi) breaches of conditions relating to payment;

(vii) limitation.

(i) Misrepresentation and non-disclosure

5.15 The insurer may claim that the insured misrepresented his insurance position, fraudulently or otherwise, or failed to disclose all material facts when he applied for insurance cover. If the insurer was induced to enter into the insurance contract by misrepresentation or if material facts were not disclosed to him, the contract is voidable and the insurer may also have a remedy in damages.

5.16 Where an insurer raises defences based on misrepresentation or non-disclosure in proceedings where the rights of the insured have been transferred to a third party under the 1930 Act, the position of the third party may be a difficult one. He must

[23] At common law, a breach of warranty automatically terminates the liability of the insurer, whether or not there has been a loss.

[24] Arguments for and against preventing insurers from relying on such defences as against third parties are set out in Part 14.

raise arguments which would have been available to the insured[25] but is unlikely to know what information was provided by the insured to the insurer. It may be difficult for him to obtain information from an insolvent or bankrupt insured, who is unlikely to be concerned about the third party proceedings and who may, in any case, have a contractual duty under the insurance policy not to assist third party claimants.

(ii) Breaches of notice provisions

5.17 Most insurance polices contain notice clauses which require the insured to notify the insurer of matters such as knowledge of a claim or service of a writ immediately or within a specified period of time. Obtaining prompt notice may be vital if the insurer is to conduct the insured's defence. Notice conditions may also require the insured to give notice in a particular form, or at a particular place such as the insurer's head office. We look briefly here at the ability of insurers to insist on the strict observance of notice requirements and at whether third parties are able themselves to notify insurers of their claims.[26]

5.18 In *Hassett v Legal & General Assurance Society Ltd*,[27] a public liability insurance policy contained a condition that any communication relating to an accident should be forwarded to the insurer immediately. The plaintiff was injured in March 1934 while in the employment of the insured company against which he brought a claim and obtained a default judgment which remained unsatisfied as the company went into liquidation. The plaintiff commenced proceedings against the company's insurers who, although they had received notice of the claim, knew nothing of the legal proceedings against the insured. The insurer denied liability under the 1930 Act on the ground that the insured had been in breach of the notification condition. Atkinson J upheld this defence, observing that:

> the moment any proceedings were started there was an obligation imposed upon the insured by these conditions to bring it to the notice of the insurance company, so that the insurance company would be in a position to exercise the rights which these conditions give them ... it is implicit in every word of [the condition] that if proceedings are started, the insurance company must be told about them and be put into a position to exercise their rights. If it were not so, scope would be given for the exaggerated claims going through without any inquiry or testing, and insurance companies would be swindled in all directions. That condition, the performance of which was an essential condition and as it seems to me a condition precedent to the insurance company's liability, was never performed.

[25] See, for example, *Cleland v London General Insurance Company Ltd* (1935) 51 Ll LR 156 where, against a defence raised by an insurer based on non-disclosure, the third party plaintiff argued that the insured had had no duty to disclose his "past bad character" unless this was material. He also claimed that the court should consider that it was he rather than the insured who had suffered as a result of the insured incident. His arguments failed. See also *McCormick v National Motor and Accident Insurance Union Ltd* (1934) 40 Com Cas 76.

[26] See also the case of *Horne v The Prudential Co Ltd* 1997 SLT (Sh Ct) 75.

[27] (1939) 63 Ll L Rep 278.

5.19 The nature of notice requirements and whether such requirements can be met by the insurer receiving information from a source other than the insured were discussed in *Barrett Bros (Taxis) Ltd v Davies*,[28] a road traffic case. Conditions 1 and 13 of the policy read as follows:

> The insured shall give full particulars in writing to [the insurer] ... as soon as possible after the occurrence of any accident, loss or damage and shall forward immediately any letter, notice of intended prosecution, writ, summons or process relating thereto.
>
> The due observance and fulfilment of the terms, provisions, conditions and endorsements of this policy in so far as they can apply and the truth of the statements and answers in the proposal form shall be conditions precedent to any liability of the underwriters to make any payment under this policy.

5.20 The insured did not tell his insurer at once about the accident, but the solicitors of the third party victim did. The insurer was also informed of a notice of intended prosecution of the insured and of a summons for careless driving by the police.

5.21 Lord Denning MR and Danckwerts LJ held that it was unnecessary for the insured to send the documents to the insurer: they were absolved from doing so because the insurer had all the relevant information from the police.

5.22 Lord Denning MR suggested, obiter, that:

> This condition 1 was inserted in the policy so as to afford a protection to the insurers so that they should know in good time about the accident and any proceedings consequent on it. If they obtain all the material knowledge from another source so that they are not prejudiced at all by the failure of the insured himself to tell him, then they cannot rely on the condition to defend the claim.

5.23 Salmon LJ disagreed with this approach. In his view:

> there was a clear breach of condition 1 of the policy. This imposed an absolute obligation upon the motor-cyclist to forward the summons to the insurers when he received it and also to notify them about the intended prosecution. The observance of that obligation was by condition 13 made a condition precedent to the insurers' liability to pay. But for waiver, I should have felt obliged to hold that, although there is absolutely no merit in the defence - indeed, it is somewhat surprising to find insurers of this standing in circumstances such as these taking the point - they were entitled to succeed.

5.24 The nature of notice requirements was raised again in *Farrell v Federated Employers' Insurance Association*.[29] The case involved a failure to notify an insurer of the service of a writ in circumstances where the insurer had not received adequate notice from another source. The relevant policy conditions provided as follows:

[28] [1966] 1 WLR 1334.

[29] [1970] 2 Lloyd's Rep 170.

> Condition 1: Every ... writ ... served on the Employer shall be notified or forwarded to the [insurer] immediately on receipt ...
>
> Condition 7: The due observance ... of the ... conditions ... of this Policy in so far as they relate to anything to be done ... by the Employer and the truth of the statements and answers in the Proposal ... shall be conditions precedent to any liability of the [insurer].

5.25 The court held that a failure to notify the insurer immediately that the third party had served the insured was a breach of the insurance policy and entitled the insurer to rely on the breach as against the third party. Lord Denning said that the third party was,

> claiming the benefit of a policy which is issued to the employers. He must take it as he finds it. He cannot claim the advantages and reject the disadvantages. He cannot claim the benefit and reject the conditions of it.

5.26 In his view, the third party's solicitors should have notified the insurer of the service of the writ soon after they received a response from the receiver of the insured following service of proceedings on the insured.

5.27 The issue of whether the insurer needed to have suffered prejudice to be able to rely on the notice requirement was also raised. Lord Denning did not appear to view the question of whether the insurer had suffered prejudice or not as important. Megaw LJ held that there had been prejudice to the insurer.

5.28 The issue of whether or not the insurer needed to have suffered prejudice was considered again in *The Vainqueur Jose*[30] where Mocatta J reviewed *Barrett v Davies*[31] and *Farrell v Federated Employers' Insurance Association*.[32] Of *Farrell*, Mocatta J said:

> It is clear from this case that if prejudice is necessary to sustain a defence by an insurer against a claim against him by his assured or by someone standing in the shoes of his assured under the 1930 Act like the plaintiffs here when the assured has not given timeous notice of his claim as provided for in his policy or cover, relatively little prejudice has to be shown by the insurer in order for him to escape liability under the time clause.

5.29 In the context of P & I Clubs, Mocatta J discussed a number of other issues relating to notification. He held that notification to the club's representatives in New York was not sufficient as the representatives gave advice and assistance only; they were not the club's agents for the purpose of receiving notice of claims. He also suggested that notification should be by the member himself and that all relevant details should be notified to the club.

[30] *CVG Siderurgicia v London Steamship Owners Mutual* [1979] 1 Lloyd's Rep 557.

[31] [1966] 1 WLR 1334.

[32] [1970] 1 Lloyd's Rep 170.

5.30 The issue of prejudice was discussed again in *Pioneer Concrete (UK) Ltd v Employers Mutual Insurance Association*.[33] Bingham J held that, although the plaintiff third party had notified the defendant insurer of the accident, it had not given notice of proceedings as required by the policy. Bingham J held that notification was inadequate and that, even if the insurers had not been prejudiced by the failure to notify, they could rely on it because the condition was clearly worded as a condition precedent.[34] The insurer had, in any event, suffered prejudice in that it had been deprived of the opportunity to consider whether and how to defend the claim made against the insured. He also suggested that, if the insurer needed to show prejudice, "relatively little prejudice will suffice".[35]

5.31 The court may take a strict approach to notice requirements, allowing insurers to enforce such requirements even if they have suffered little or no prejudice. In practice, most insurers will not usually insist on strict observance of such conditions if the Statement of General Insurance Practice issued by the Association of British Insurers in 1986 applies.[36] Paragraph 2(a) of the Statement states that:

> Under the conditions regarding notification of a claim, the policyholder shall not be asked to do more than report a claim and subsequent developments as soon as reasonably possible except in the case of legal processes and claims which a third party requires the policyholder to notify with a fixed time where immediate advice may be required.

Can notice requirements be met by third parties?

5.32 It appears, from *Barrett Bros (Taxis) Ltd v Davies*,[37] that a notice requirement can be met if adequate information is received by the insured from another source, in that case, the police. However, some judges might adopt the approach taken by Salmon LJ in that case and hold that a notice requirement places an "absolute obligation" on the insured which cannot be met by another party. Where third parties do not have access to policy documentation, any notice they give may not fulfil the precise requirements of the insurance policy. As we have seen, a strict approach towards notification was taken by Mocatta J in *The Vainqueur Jose*, where

[33] [1985] 1 Lloyd's Rep 274.

[34] He said, at p 281: "I find no support in any later authority for the requirement of prejudice and, as a matter of general contractual principle, it appears to me that this cannot be required of an insurer before he relies on a breach of a condition precedent in the policy". See also *Aswan v Iron Trades* [1989] 1 Lloyd's Rep 289.

[35] Also at p 281. See also obiter dicta of Mance J in *TGL v AGF Insurance Ltd* [1997] 1 QB 599, 608 on a condition requiring that no liability be admitted without the insurer's consent. Referring to *Farrell* and *Pioneer Concrete*, he held, at p 17, that "The absence of prejudice would, on authority, also present no answer to what was otherwise a breach".

[36] As we have already noted, it is not clear whether or not insurers would apply the Statement when dealing with third party claims under the Act. See paras 2.7 and 5.13 above.

[37] [1966] 1 WLR 1334. See paras 5.19-5.23 above.

he suggested, in the context of claims against Protection and Indemnity Clubs, that notification should be by the member himself. [38]

5.33 In such cases, the insurer may be uncertain as to whether the notice it has received is valid or relates to a potential loss. If it incurs expense in investigating the circumstances in which the notice was given, it may claim that it has suffered prejudice and that it should be able to rely on the notice condition.[39]

5.34 In cases where insurers are entitled to adopt a strict approach to the fulfilment of notice requirements, third parties may face a number of problems. First, notice requirements may be breached before third parties have a right themselves to give notice. As the insured heads towards bankruptcy or insolvency, he is less likely to be concerned with meeting such requirements. Assuming that notice can be given by third parties, they may not be in a position themselves to meet the precise notice terms. Their situation is not made easier by the interpretation by the court of the information provisions in the 1930 Act in such a way as to require the third party actually to have established the liability of the insured before being entitled to discovery of insurance details.[40] The result may be that, again, either as a matter or law or of practice, third parties are unable to ensure that conditions in the insurance policy are met.[41]

(iii) Arbitration clauses[42]

5.35 Some arbitration clauses in insurance contracts govern disputes over liability but most provide only for the quantification of liability by arbitration.[43] It is possible that the fairness of arbitration clauses may be challenged under the Unfair Terms in Consumer Contracts Regulations.[44] Clauses which make the referral of a dispute

[38] See para 5.29 above.

[39] See para 5.30 above.

[40] See *Nigel Upchurch Associates v Aldridge Estates Investment Co Ltd* [1993] 1 Lloyd's Rep 535 and *Woolwich Building Society v Taylor, The Times* 17 May 1994 discussed at paras 4.13 to 4.17 above.

[41] We discuss in Part 14 whether third parties should be able to meet notice provisions and whether insurers should be prevented from relying on breaches of notice provisions in certain cases.

[42] Limitation problems faced by third parties seeking to commence arbitration proceedings against insurers under the Act or to substitute themselves in arbitration proceedings started by the insured within the limitation period are discussed in Parts 9 and 17 below.

[43] In a report published in 1957 (the Fifth Report on Conditions and Exceptions in Insurance Policies, Cmnd 62, para 13), the Law Reform Committee expressed concern that insurers might be abusing their position in certain cases by insisting upon arbitration. The Committee recommended no change in the law because of assurances from the Association of British Insurers and from Lloyd's that their members had agreed not to insist on arbitration against the wishes of the insured in disputes over liability, except with regard to reinsurance, marine insurance and, in some cases, aviation insurance. The ABI/Lloyd's arbitration agreement was confirmed in 1986. It provides that members will refrain from insisting on the enforcement of arbitration clauses in standard form policies if the insured prefers to have questions of liability (not quantum) determined by the court. It is unclear whether or not this agreement could be relied on by third party claimants under the Act.

[44] SI 1994 No 3159, implementing European Council Directive 93/13/EC. See Merkin on Arbitration Law, Service Issue No 16, 12 January 1997, 1.45 and Malcolm Clarke, *The Law of Insurance Contracts* (3rd ed 1997) p 518. Sections 89 and 90 of the Arbitration Act 1997

to an arbitrator a condition precedent to the liability of the insurer are known as *Scott v Avery* clauses, after the case of that name.[45] In Scotland, it is clear that arbitration conditions in the policy are binding on the third party.[46]

Scott v Avery clauses

5.36 The court in *Scott v Avery*[47] held that arbitration clauses are enforceable as conditions precedent provided that they do not purport to oust the ultimate jurisdiction of the court. Parties can, therefore, agree that no right of action shall accrue in respect of disputes between them until an arbitration award has been made and their agreement will be enforceable.[48]

5.37 The issue of the enforceability of arbitration clauses in insurance policies against third parties was considered in *Freshwater v Western Australia Assurance Co Ltd*.[49] The third party had been injured in a motor accident and had obtained judgment against the insured. The insured was declared bankrupt before judgment was satisfied and the plaintiff sought to sue the insurer under the Third Parties (Rights Against Insurers) Act 1930 and the Road Traffic Act 1930. The insurance policy contained an arbitration clause in the following terms:

> If any difference or dispute of any kind whatsoever shall arise between the insured or any claimant and the company in respect of this policy or in respect of any claim or any matter or thing or any liability arising or alleged to have arisen hereunder or otherwise connected herewith directly or indirectly the same shall be referred to the final determination and award of a single arbitrator to be agreed upon by both parties ... and the obtaining of the said award shall be a condition precedent to the liability of the company to make any payment under this policy.

5.38 The insurer sought a stay of the action, relying on section 4 of the Arbitration Act 1889 which enabled a party against whom legal proceedings are brought to apply

confirm that the regulations apply to arbitration agreements. Cf the Unfair Contract Terms Act 1977 and the Consumer Arbitration Agreements Act 1988 (which generally prohibits arbitration clauses in consumer contracts) which do not apply to insurance contracts.

45 Where the arbitration clause is not clearly expressed to be a condition precedent to the liability of the insurer, there may be a dispute as to whether or not the relevant clause is a condition precedent. See *Collins v Locke* (1879) 4 App Cas 674 and *Edwards v Minster Insurance Co Ltd* (unreported) 10 March 1994, where Saville LJ distinguished an arbitration clause in *Freshwater v Western Australia Assurance Co Ltd*, from conditions precedent which could not be met by third parties: the former, he said, was merely "an incident of the right to an indemnity". See paras 5.52-5.55 below.

46 *Cunningham v Anglian Insurance Co Ltd* 1934 SLT 273.

47 (1856) 5 HLC 810; 10 ER 1121, HL.

48 See *Heyman v Darwins Ltd* [1942] AC 356 at p 377 and Mustill & Boyd, *Commercial Arbitration* (2nd ed) pp 161-162. The Arbitration Act 1996 does not alter the general enforceability of *Scott v Avery* clauses, although section 9(5) of the Act makes it clear that the court will decide whether or not the clause binds the parties: "If the court refuses to stay the legal proceedings, any provision that an award is a condition precedent to the bringing of legal proceedings in respect of any matter is of no effect in relation to those proceedings".

49 [1933] 1 KB 515.

to court to stay those proceedings on the ground that the plaintiff was bound by an arbitration clause.

5.39 The Court of Appeal stayed the proceedings, Lord Hanworth MR saying:

> A third party such as the plaintiff cannot eliminate all the terms and conditions of the policy, but, if he wishes to rely upon the policy, he is bound by the terms and conditions therein written, in other words, he is bound by the clause which provides for arbitration.

5.40 The same approach was taken in *Dennehy v Bellamy*,[50] where the Court of Appeal upheld the argument of the insurer that proceedings started by a third party should be stayed. Greer LJ said:

> I think that it was a question of liability under the contract, and it would have been perfectly useless to anybody to allow the action to go on, because the action must necessarily fail, inasmuch as the plaintiff in the action was not in a position to prove that the condition precedent to his liability had in fact been performed.

Problems faced by third parties bound by arbitration clauses[51]

5.41 Third parties bound by arbitration clauses in the insurance contract may not be able to afford the expense of arbitration. Legal aid, which is available for legal proceedings, is not currently available for arbitration. The question of whether the insurer's ability to rely on arbitration clauses should depend on the personal circumstances of the third party has been raised in a number of cases.

5.42 *Smith v Pearl Assurance Co Ltd*[52] was a case involving the 1930 Act. The plaintiff was injured in a road accident caused by the negligence of the insured and had obtained judgment against him. The insured became insolvent and the plaintiff started proceedings against the insurer under the 1930 Act. The insurer applied for a stay of those proceedings on the ground that there was an arbitration clause in the insurance policy. The plaintiff contended that, owing to his poverty, he could not afford to start arbitration proceedings for which he could not receive financial assistance from the Poor Persons Committee.[53]

5.43 The Court of Appeal held that the plaintiff's poverty was not a sufficient ground for exercising any discretion which a court might have to refuse to order a stay. The discretion could not be exercised to interfere with the contract agreed between the insurer and the insured. Clauson LJ said that the plaintiff's poverty was:

> a personal disability under which the plaintiff finds himself, a personal disability in no way connected with the contractual rights or

[50] [1938] 2 All ER 262.

[51] We seek consultees' views at para 14.35 below on whether arbitration clauses should be enforceable against third parties.

[52] [1939] 1 All ER 95.

[53] A predecessor of the Legal Aid Board. He could have obtained financial assistance for court proceedings.

> obligations arising out of the contract in respect of which he has, or conceives himself to have, a cause of action.

5.44 He concluded his judgment by suggesting, however, that this position was unsatisfactory:

> I only wish to add that, should it become necessary in the future to deal further legislatively with the matter which was dealt with in the Third Parties (Rights Against Insurers) Act 1930, I trust that those who have to deal with the matter will carefully consider whether there are not weighty reasons why persons who have the advantage of some such legislative provision should not be freed from the restriction, which might otherwise fall upon them, of being driven to arbitration. That, however, is a matter of policy, upon which I should not be justified in expressing any view. Nevertheless, I do think, having regard to such experience as I have had in these matters, that I am justified in drawing attention to the desirability of that question being very carefully considered, should the occasion arise.

5.45 A sympathetic approach to those bound by arbitration clauses was taken by Lord Denning MR in *Fakes v Taylor Woodrow Construction Ltd*,[54] a case which did not involve the 1930 Act. He questioned the reasoning in *Smith v Pearl Assurance*:

> It is bad enough for a poor man to be faced with an arbitration clause, usually in a printed form which he has never read. It is much worse if the courts then insist that he is to go off to arbitration where there is no legal aid... .The poor man who cannot afford arbitration has no remedy. That will not do. If the poor man cannot afford arbitration, he should not be compelled to go there. He should be allowed to continue his action in the courts ...[55]

5.46 Megaw LJ dissented, on the basis that to allow the plaintiff to proceed with legal proceedings would prejudice the rights of the insurer. Referring to section 1(7) of the Legal Aid and Advice Act 1949, he said that:

> the rights conferred by this part of this Act on a person receiving legal aid shall not affect the rights or liabilities of other parties to the proceedings or the principles on which the discretion of any court or tribunal is normally exercised.

5.47 Sir Gordon Willmer referred to the following passage in Clauson LJ's judgment in *Smith v Pearl Assurance*:

> In my judgment, it can only be in some very exceptional case indeed that the court would be justified in holding that one party's mere personal disability of this character would be sufficient reason for the court to exercise the power, given by the Arbitration Act 1889, section 4 or overriding the contractual right of arbitration.[56]

[54] [1973] 1 QB 436.

[55] *Ibid*, at p 441.

[56] The court's approach to arbitration clauses has varied in subsequent cases. In *Goodman v Winchester and Alton Railway plc* [1985] 1 WLR 141 it was held that the poverty of the

5.48 The implications of allowing insurers to rely on arbitration clauses against impoverished third party claimants have been described as follows:

> While seeking to protect the third party from the poverty of the insured wrongdoer, Parliament showed no intention to protect him from his own.[57]

The court's power to stay legal proceedings

5.49 The discretion of the court to grant or refuse an application by an insurer for a stay of legal proceedings will, in any case, be removed by an amendment to the Arbitration Act 1996.[58] This Act does not apply to Scotland, where the courts must give effect to a valid agreement by the parties to refer matters to arbitration and will sist the proceedings before it.[59] Arbitration agreements caught by the Act will be governed by section 9, which provides that:

> On an application under this section, the court shall grant a stay unless satisfied that the arbitration agreement is null and void, inoperative or incapable of being performed.

5.50 One of the aims of the 1996 Act was to restrict the ability of the court to intervene in situations where the parties to an agreement have provided expressly that certain matters should be resolved by arbitration. There may be a number of reasons why arbitration clauses are included in insurance contracts. The insurer may believe that arbitration will be less costly and formal than court proceedings,

plaintiff was a material, but not necessarily decisive factor. In *Chrisphine Othieno v G Cooper & M Cooper* BLR 57 (1991) *Fakes* was applied and a stay refused. In *Edwin Jones v Thyssen (Great Britain) Ltd* 57 BLR 116 (1991), the Court of Appeal applied *Smith v Pearl Assurance* and *Goodman v Winchester and Alton Railway plc*. In *Connelly v RTZ Corp plc* [1996] QB 361, the Court of Appeal referred to *Fakes* but considered that particular considerations applied in deciding whether or not to grant a stay when applying the principles of forum non conveniens. In *Trustee of the Property of Andrews v Brock Builders (Kessingland) Ltd* [1997] 3 WLR 124, the Court of Appeal held that a plaintiff opposing an application to stay arbitration proceedings on the ground of impecuniosity had to show that he had a reasonable prospect of establishing that the defendant's inability to afford arbitration was a result of the defendant's breach of contract.

[57] See M Clarke, *The Law of Insurance Contracts* (3rd ed 1997) p 161. We discuss at para 5.35 above suggestions that the Unfair Terms in Consumer Contracts Regulations may be used to challenge the fairness of arbitration clauses in insurance contracts.

[58] Under ss 85-87 of the 1996 Act, the power of the court to order a stay would depend on whether the arbitration agreement is "domestic" or "non-domestic"; it has a wider discretion where the arbitration agreement is domestic. For example, it can consider whether there were "sufficient grounds for not requiring the parties to abide by the arbitration agreement". See s 86(2)(b) of the 1996 Act. The distinction between domestic and non-domestic agreements in the Consumer Arbitration Agreements Act 1988 was held to be contrary to EU law in *Philip Alexander Securities and Futures Ltd v Bamberger*, *The Times* 22 July 1996. Therefore ss 85-87 of the 1996 Act have not been brought into force. SI 1996\3146.

[59] *Sanderson and Son v Armour and Co Ltd* SC (HL) 117.

will better preserve confidentiality and will allow claims to be decided on a case by case basis, with less scope for the setting of precedents.[60]

(iv) Breaches of the duty to provide information and assistance

5.51 In many insurance contracts, the insurer has a right to defend any proceedings brought against the insured.[61] In many cases, the insurer will exercise this right and conduct the insured's defence, while reserving his right to rely on any defences which he himself may have under the insurance contract. To enable the insurer to investigate the claim against the insured and to prepare his defence as early as possible, the insurance contract will usually require the insured to provide information of any potential claim to the insurer as soon as he has knowledge of it and to assist the insurer as necessary. It will probably prohibit the insured from making any admissions of liability to the third party.

5.52 In *Edwards v Minster Insurance Co Ltd*,[62] the insurance contract required the insured to give all such information and assistance to the insurer as he might require. This requirement was stated to be a condition precedent to the liability of the insurer. The insurer defended proceedings brought by the plaintiff third party, claiming that the condition precedent had not been fulfilled. The third party argued that the condition was an "incident" of the right to an indemnity which had been transferred to him. It had not been suggested, he argued, that he had failed to comply with the condition and the failure of the insured to do so was not relevant.

5.53 Judgment was given by Lord Justice Saville, who rejected the plaintiff's argument, describing the effect of the condition precedent as follows:

> The Act operates a statutory transfer of the right of the insured to be indemnified. If the right to an indemnity is subject to a condition, it is a conditional right that is transferred to the third party. If the condition is not fulfilled, then there remains no right to an indemnity. Nothing in the Act transferred to the Plaintiff the performance of the condition ... .The condition imposed a requirement on the insured company that remained with the company and its failure to comply with it, albeit after the statutory transfer of the conditional right, meant that the right to an indemnity disappeared.[63]

5.54 Lord Justice Saville suggested that to accept the plaintiff's argument,

[60] These are some of the reasons why, for example, the rules of Protection and Indemnity Clubs generally provide for disputes between members to be resolved by arbitration. We discuss in Part 14 whether, against third party claimants under the Act, insurers should be able to rely on arbitration clauses.

[61] See, for example, the clause discussed in *Wood v Perfection Travel*. See paras 4.25-4.27 above.

[62] *Edwards v Minster Insurance Co Ltd* (unreported) 10 March 1994.

[63] Saville LJ (whose judgment at first instance in *The Padre Island* was subsequently followed by the House of Lords in that case) referred here to the principles on which he had based his judgment in that case. See paras 5.59-5.62 below.

would produce the ludicrous situation of the third party having to supply to the insurers information and assistance which in the nature of things the third party could hardly do.[64]

(v) Breaches of conditions relating to the duty of the insured to meet minimum safety requirements, to comply with safety and other regulations/preserve the assets/business insured (for example, to maintain the security of premises)[65]

5.55 Some conditions of this nature are more likely to be breached in the period leading up to insolvency when the insured is short of money. Even if they have been met by the insured, there may be problems when the insured's obligations are assumed by the liquidator or trustee in bankruptcy. Such conditions cannot be met by the third party as he has no right to intervene in the management of the insured's affairs.

(vi) Breaches of conditions relating to payment

5.56 Most insurance policies contain detailed provisions relating to the payment of premiums and of policy excesses. The rules of some mutual associations, including Protection and Indemnity Clubs providing insurance cover to shipowners, may provide for cover to be withdrawn when the insured is unable to pay premiums[66] and may also provide that the insurer shall not be liable to indemnify the insured until he has actually paid sums due to a third party in respect of his liability. We consider the effect which such clauses have on third party claims.

Payment of premiums and of policy excesses

5.57 In *Murray v Legal and General Assurance Society Ltd*,[67] the court held that the insurer could not set off unpaid premiums against the third party's claim because, in the wording of the policy in question, the right to recovery of premiums was "not a term of the policy which arose in respect of the liability of the insured to the third party."[68] The court appeared to suggest, however, that such a clause could be made a condition precedent which would bind third party claimants. Third party claims will be subject to a deduction of any excess which applies to claims under

[64] Saville LJ relied upon *Pioneer Concrete (UK) Ltd v National Employers Mutual General Insurance Association Ltd* [1985] 1 Lloyd's Rep 274, discussed at para 5.30 above. A different approach has been taken in the United States where courts are unlikely to accept as a defence by insurers to proceedings by third parties the lack of co-operation by the insured, unless this was "substantial": *Home Indemnity Co v Finley*, 261 F Supp 318, 321 (ED Ark, 1966). We discuss at paras 14.19-14.27 below whether insurers should only be able to rely on policy breaches if they have suffered prejudice.

[65] Policy conditions may also require the insured himself to hold a particular licence or to have a particular qualification. See para 14.37, n 69 below.

[66] Or "calls" as they are generally referred to in Club rules.

[67] [1970] 2 QB 495.

[68] Cf *Edwards v Minster Insurance Co Ltd* (unreported) 10 March 1997, discussed at paras 5.52-5.54 above.

the policy and of the insurer's defence costs if the insurance contract entitles the insurer to an indemnity for such costs.[69]

Pay first clauses

5.58 "Pay first" (or "pay to be paid") clauses require the insured actually to have paid sums due to third parties in respect of his liability before he is entitled to an indemnity from the insurer.[70] Such clauses are usually only found in the rules of Protection and Indemnity Clubs.[71] Historically, such clauses were included so that Club members could rely on the financial soundness of other members. It has been queried whether this argument can be used to justify the use of such clauses as most modern Clubs operate very similarly to insurance companies.[72]

The Fanti and The Padre Island

5.59 The ability of Clubs to rely, as against third party claimants, on pay first clauses was considered at length by the House of Lords in the joined cases of *The Fanti* and *The Padre Island*.[73] The clauses the subject of those proceedings provided as follows:

> Subject to the provisions of these Rules, the Member shall be protected and indemnified against all or any of the following claims and expenses which he shall become liable to pay and shall in fact have paid in respect of a ship entered in this class of the Association ...[74]
>
> [The Club shall] ... [p]rotect and indemnify members in respect of losses which they as owners of the entered vessel shall have become liable to pay and shall have in fact paid.[75]

5.60 The arguments raised by the parties centred on three main issues: the nature of rights transferred to third parties under the 1930 Act; the effect of the anti-

[69] See *Cox v Bankside* [1995] 2 Lloyd's Rep 437.

[70] In some cases, Club rules may allow an indemnity to be paid before actual payment by the member. For example, the committee of a Protection and Indemnity Club may exercise its discretion to make an out of court settlement possible or rules may provide that the Club will indemnify the member for sums which the member has been legally ordered to pay "or could be reasonably expected to pay".

[71] Hirst J in *The Italia Express* [1992] 2 Lloyd's Rep 281, at 298 suggested that a pay first clause "would be entirely inappropriate in the non-club environment of a commercial insurance contract". Concern has been voiced that pay to be paid clauses are being used more widely by mutual insurance companies: see Clive Boxer: Professional Liability Today, July 1990, p 4. The standard collision clause (clause 8 in the Institute Time Clauses, Hulls) does provide that the insured shall have paid sums due to a third party before being entitled to an indemnity.

[72] Sir Jonathan Mance "Insolvency at Sea" [1995] LMCLQ 34, at 46, doubts whether such clauses are essential to the operation of clubs: he suggests that "[c]lubs' security is in practice better served by ensuring that Club membership and Club management are of high quality". The House of Lords was prepared, however, to recognise the "special character" of Protection and Indemnity insurance in *The Fanti*. See dicta of Lord Goff, at p 39.

[73] [1991] 2 AC 1.

[74] *The Fanti*.

[75] *The Padre Island*.

avoidance provisions of section 1(3) of the Act; and whether equitable principles prevented Clubs from relying on pay to be paid clauses.[76]

5.61 The House of Lords held that, as the members had not paid sums due to the third parties, they had no accrued rights to be indemnified by the clubs. Third parties could not have transferred to them under section 1(1) of the Act any better or larger rights against the clubs than those which the members previously possessed.[77] The House of Lords also held that the clauses were not avoided by section 1(3) of the 1930 Act as the inability of the insured to pay resulted from impecuniosity, not from the winding up order itself. Finally, they held that the third parties could not rely on equitable principles when there had been express agreement between insurer and insured.

5.62 Following the House of Lords' decision, it seems clear that pay first clauses in Protection and Indemnity Club rules will bar recovery by third parties under the 1930 Act.[78] Third parties suing insured shipowners will be in the same position as other creditors unless the Club chooses to exercise its discretion and to allow recovery.[79] The House of Lords appeared to take comfort from the Clubs' assurance that they do not rely on pay to be paid clauses where the third party's claim relates to death or personal injury.[80] Clubs may not always follow best practice, however, especially if they themselves are in financial difficulties.[81]

Can third party claimants against Protection and Indemnity Clubs circumvent the House of Lords' decision in The Fanti or protect their position by other means?

5.63 It has been suggested that schemes could be devised which would enable third parties to circumvent the House of Lords' decision in *The Fanti*. The third party, it is suggested, (or his insurer, his bank or another person) could lend money to the

[76] See paras 5.4-5.9 and 5.58-5.62 above.

[77] See para 5.4 above.

[78] Cf the House of Lords' interpretation of ultimate nett loss clauses in reinsurance contracts in *Home & Overseas Insurance Co Ltd v Mentor Insurance Co (UK) Ltd* [1989] 1 Lloyd's Rep 473 and *Charter Reinsurance Co Ltd v Fagan* [1996] 2 WLR 726. Although these clauses provide for payment by the reinsured of sums in respect of an "ultimate net loss", described as the sum *actually paid* by the reinsured in settlement of losses or liability, the House of Lords has held that those sums need not actually have been paid before the liability of the reinsurer arose. The approach of the House of Lords in these cases does not mean that it would be likely to overturn its judgment in *The Fanti* were pay first clauses to come before it again: its approach to such clauses in P&I Club rules and to ultimate nett loss clauses followed consideration, in each case, of the historical reasons for the use of such clauses and relevant market practices. The ABI, the Institute of London Underwriters and LIRMA have recommended a new insolvency clause reflecting the approach taken by the House of Lords in *Charter Reinsurance Co Ltd v Fagan* for inclusion in reinsurance contracts. See Appendix D.

[79] See para 5.13, n 19 above.

[80] See the judgment of Lord Goff at p 38.

[81] See Sir Jonathan Mance "Insolvency at sea" [1995] LMCLQ 34, at 49. As a result of the House of Lords' decision in *The Fanti*, third party cargo owners may be more anxious to arrest vessels so as to obtain a club letter of undertaking in which the club itself guarantees the claim.

insured to enable him to pay the sums due and to fulfil the condition precedent[82] and the money could be paid back once the insured had been indemnified.[83] Some clubs have objected to such schemes, claiming that they offend the principle of indemnity, and have amended their rules stating not only that the member's liability must be discharged but that it must be discharged by the member's own funds.[84]

5.64 The success of such schemes is likely to depend on the co-operation of a lender and of the liquidator. The lender would need to be satisfied that the loan would ultimately be recovered from the insurance proceeds. The liquidator would need to be able to satisfy other creditors suspicious of such schemes. Problems might arise as to the capacity in which the liquidator held any monies advanced[85] and as to recovery of his fees for time spent on such schemes.

5.65 Another suggestion is that, if the insured can pay any amount at all to his creditors (including the third party), however small, he should be able to recover a corresponding amount from the P & I Club, which he can then pay over to his creditors again, with the process starting again. If the third party is the only creditor he will eventually be paid in full, otherwise he will receive shares of the money paid out.

Limitation and prescription

5.66 Problems relating to limitation periods governing claims under the 1930 Act are discussed in more detail below.[86] It is sufficient to note here that it is unclear whether the limitation period governing third parties' claims under the 1930 Act is

[82] See Sir Jonathan Mance "Insolvency at Sea" [1995] LMCLQ 34, at 47 and Smallwood "*The Fanti* and *The Padre Island* : the next step" P & I International Oct 1991 17. See also *MacGillivray and Parkington on Insurance Law* (8th ed) p 892 and Slade J, obiter, in *The Allobrogia* at p 197: "I am not certain, for example, that with the co-operation of the petitioners and a future liquidator of the company, a scheme could not be devised which enabled the liquidator to discharge the company's debt to the petitioners out of borrowed money, which in turn would in due course be paid directly or indirectly out of the proceeds of the claim against the association. It could perhaps be that such a scheme would achieve a sufficient compliance with the conditions precedent set out in rule 28 (the shall first have paid rule) to give rise to a right of recovery from the association."

[83] In *Home & Overseas v Mentor Insurance Co (UK) Ltd* [1989] 1 Lloyd's Rep 473, (a reinsurance case, discussed at n 78 above) approval of the Companies Court was obtained for a scheme allowing claims of insurance companies against Mentor (in liquidation) to be discharged by equivalent borrowings from such insurance companies. In an American case, *Liman v American Steamship Owners Mutual Protection and Indemnity Association Inc* (1969) AMC 1669, a US District Court held that a pay to be paid condition was satisfied when the member's liability was discharged by a court appointed trustee in bankruptcy. In many states in the USA, pay to be paid clauses are prohibited.

[84] An example of such a clause is as follows: "In the case of a liability, actual payment (which shall be made out of monies belonging to the member absolutely and not by way of loan or otherwise) by the member of the full amount of such liability shall, unless the committee otherwise decide, be a condition precedent to the right of a member to recover and the obligation of the club to satisfy and make good". See Hazelwood, *P & I Clubs Law and Practice* (2nd ed 1994) p 326.

[85] For example, complicated trust problems might arise.

[86] See Parts 9 and 17.

that which applies to the insured's right of action against the insurer or whether the third party's action is governed by a fresh limitation period. It is also unclear whether third parties can be substituted in arbitration proceedings started by the insured within the limitation period.

5.67 The position in Scottish law regarding prescription of the various obligations arising out of the policy is discussed in Part 7 below. Prescription of the third party's claim starts to run when the insurer becomes liable to indemnify the insured. Scottish law allows third parties to be substituted in proceedings started by the insured against the insurer.[87]

OVERVIEW OF THE RIGHT OF INSURERS TO RELY ON DEFENCES WHICH THEY WOULD HAVE HAD AGAINST THE INSURED TO DEFEAT THIRD PARTY CLAIMS

5.68 In interpreting sections 1 and 2 of the 1930 Act, the court has stressed that third parties should not acquire better rights against the insurer than the insured would have had. Third parties are already placed at a disadvantage by their inability to meet certain policy conditions which can only be fulfilled by the insured. They have been further disadvantaged by the court's interpretation of section 2 as they may not learn of the policy conditions which they could, in theory, have met until it is too late. As we have seen, the legal or practical effect of some insurance terms, such as pay first and arbitration clauses, may be that the third party has no enforceable rights under the Act. We consider in Part 14 below whether insurers should be prevented from relying on certain defences against third parties or whether they should be allowed to rely on the rights which they have against the insured under the insurance contract.

[87] See para 9.22 below.

PART 6
PROVISIONS RELATING TO WHO OWES A DUTY OF DISCLOSURE AND AS TO WHAT INFORMATION SHOULD BE DISCLOSED

6.1 In Part 4,[1] we considered the implications of the court's construction of section 2 of the Act in such a way as to require a third party claimant to have established the liability of the insured before acquiring a right to disclosure. In this Part, we consider the extent of the duty to disclose under section 2 and who owes that duty.

THE INFORMATION WHICH MUST BE DISCLOSED

6.2 Section 2(1) states that those under a duty to disclose must disclose to the third party:

> such information as may reasonably be required by him for the purposes of ascertaining whether any rights have been transferred to and vested in him by this Act and for the purpose of enforcing such rights, if any.

6.3 Section 2(3) does not give an exhaustive list of the information to which the third party is entitled. It provides that the duty to give information under section 2 includes a duty to allow:

> all contracts of insurance, receipts for premiums, and other relevant documents in the possession or power of the person on whom the duty is so imposed to be inspected and copies thereof to be taken.

6.4 The definition is not specific in relation to information about the insurance cover, by contrast with policy documentation.[2] We are not aware of the wording of section 2(3) having caused problems to third party claimants, but its vagueness has been criticised.[3]

6.5 Section 2(1) lists the following as having a duty to disclose information to the third party:

> the bankrupt, debtor, personal representative of the deceased debtor or company, and, as the case may be, of the trustee in bankruptcy, trustee, liquidator, administrator, receiver, or manager, or person in possession of [any property comprised in or subject to a charge].

[1] See paras 4.10-4.19.

[2] We discuss in Part 13 below whether the duty to disclose should extend, for example, to information about any purported repudiation by the insurer and about the grounds of repudiation.

[3] See Philip Rocher and Mark Pring, Insurance Day, 7 September 1995, p 6. We discuss in Part 13 whether the definition used in section 2(3) should be amended. This would be necessary in any case were the insured and the insurer to have a duty to disclose information which they would not generally be required to disclose in legal proceedings, such as the value of the insurance cover.

6.6 Section 2(2) imposes a duty on an insurer to disclose information if the information provided to the third party under section 2(1) "discloses reasonable ground for supposing that there have or may have been transferred to him under this Act" rights against that insurer.

THE DUTY TO DISCLOSE DOES NOT EXTEND TO BROKERS OR TO OTHERS AUTHORISED TO HOLD POLICY INFORMATION

6.7 The list of those with a duty to disclose policy information to third party claimants does not include insurance brokers or others authorised to hold policy information, such as managers of pools set up by a number of insurers or travel agents arranging cover for holidaymakers. In many instances, the third party may remember having dealt with such people who may be those best able to identify the insurer and the policy governing a particular claim.[4] Information held by them is likely to be discloseable by the insurer or the insured, but there might be advantages to their having an express duty themselves to provide such information to third parties under the Act.[5]

THE DUTIES OF THE INSURED AND OF THE INSURER TO DISCLOSE ARE NOT SIMULTANEOUS

6.8 The insurer's duty to disclose under section 2(2) only arises if the information disclosed by the insured or the officeholder under section 2(1) "discloses reasonable ground for supposing that there have or may have been transferred to him under this Act" rights against that insurer. The third party may face problems obtaining adequate information from the insured or the officeholder. An insolvent insured may not be willing or able to assist the third party and insurance records may not have been kept. If this is the case, the third party may not even acquire a right to disclosure from the insurer under section 2(2).[6]

THE POSITION OF OFFICEHOLDERS

6.9 The duty to disclose under section 2 may cause problems to officeholders.[7] Insolvency practitioners may have conflicting duties, in that they represent the insured, owe contractual duties to the insurer under the insurance contract and owe duties to the insured's creditors. Costs incurred in complying with the duty to disclose policy information to third parties will be charged to the insolvent estate, to the likely detriment of other creditors.[8] Other officeholders will owe duties to

[4] In the case of pool managers, insurance may have been pooled to facilitate the handling of insurance cover provided by foreign insurers: there may be particular advantages to a third party having a right to disclosure against a pool manager based in this country as well as against a foreign insurer.

[5] We discuss at paras 13.19-13.20 below whether the duty of disclosure under s 2 should extend to insurance brokers and other insurance intermediaries.

[6] We suggest, at para 13.17 below, that the duty to disclose should be simultaneous.

[7] See para 6.5 above.

[8] If a third party's claim is successful and he receives an indemnity from the insurer for all the loss which he has suffered, there may be advantages to the insured's other creditors as the third party will not then claim against the insolvent estate. If his claim is unsuccessful or if he receives less than his whole claim from the insurer (eg if there is an excess in the policy which cannot be recovered from the insurer or where the insurance fund has been

their appointors who will not want to pay the costs incurred by the officeholder in connection with proceedings under the Act.

6.10 We understand[9] that, in some cases, officeholders are uncertain as to their duties of disclosure under the Act. They may find themselves advising both the insurer and the third party as to their rights under the Act and be concerned at incurring personal liability to creditors. They may also be wary of breaching terms in the insurance contract which avoid cover where policy information is made available to third parties. Section 2(1) of the Act makes void any provision in an insurance contract which purports to avoid the contract or otherwise to prohibit the giving of such information once rights have transferred under the Act, but officeholders may be uncertain as to when their duties arise.[10] Officeholders may have to seek detailed legal advice on their duties to the insurer, to third parties and to the insured's other creditors. This may cause further delay and increase the amount deducted from the assets available to the insured's general creditors.[11]

CAN THE THIRD PARTY OBTAIN DISCLOSURE BY OTHER MEANS?

6.11 It is important, as we consider the adequacy of a third party's rights under section 2, to take into account other means by which he may obtain disclosure of policy information.

6.12 In many cases, the insurer may provide policy information to the third party voluntarily, particularly where it is clear that cover has been avoided. As the insurer will often be conducting the insured's defence, it may well be in his interests to disclose such information as early as possible to avoid the costs of defending unnecessary litigation. Voluntary disclosure of policy information will not always be made, however.

6.13 The procedural rules governing disclosure in proceedings in the High Court are set out in RSC O 24.[12] In general, an application for discovery can only be made against another party and only after proceedings have started. However, pre-action disclosure and disclosure against a non-party may be obtained under sections 33(2) and 34(2) of the Supreme Court Act 1981 (RSC O 7A) where the plaintiff's claim relates to death or personal injury.[13]

exhausted by prior claimants), the third party may still claim in the insolvency. See our discussion of *Cox v Bankside* in Part 7 below.

9 From solicitors who regularly advise insolvency practitioners.

10 We suggest in Part 13 that the duty to disclose should arise earlier and that, were this to be the case, the position of officeholders would be clarified.

11 The position of official receivers may be worse as there is no specific provision for an official receiver to be remunerated for managing third party claims. In any event, in many cases where an official receiver rather than an insolvency practitioner has been appointed, the insolvent estate is likely to have few if any assets. We consider the position of officeholders under an amended Act at Part 13 below and query, at para 13.18, whether an officeholder's duty of disclosure should be less onerous than that of insurers.

12 CCR, O 14.

13 We refer at para 6.19 below to recommendations in the Woolf Report which would increase the rights of claimants to disclosure of information.

6.14 The information sought by the plaintiff must be relevant to the issues in dispute, however. As the third party's rights against the insurer have been held not to transfer until he has established the liability of the insured, the insurer is likely to argue that its liability to indemnify the insured will not be relevant to the issues in dispute between the third party and the insured.[14]

6.15 In *Cox v Bankside Members Agency Ltd*,[15] some of the Lloyd's Names made an interlocutory application under RSC, O 24, r 7 for disclosure of insurance policies by underwriters of Lloyd's Agents. The Names requested discovery of the insurance policies, including all details of the limits to and amounts of the cover and the amount of any excess. The Names argued that the information requested was relevant to an issue in the matter in that unless they knew what funds were available they would not know whether any of the questions which the insurers were seeking to have answered in the action were hypothetical or futile, or what stance to take up with regard to those questions. Without information as to level of cover, they could not properly litigate the subsidiary action as they would not know the practical effect of a ruling one way or another.

6.16 The Court of Appeal held that, although the information requested could satisfy the requirements of RSC, O 24, r 8, in that disclosure of the information would be calculated to dispose fairly of the matter or would save costs, the requirement within r 7, that the information sought should relate to the matters in question, was not met. The arguments raised by the Names, could be used in any case where there was doubt as to the opposing party's ability to pay. The law clearly stated that this was not a reason for the discovery of assets.[16]

6.17 In Scotland, section 1 of the Administration of Justice (Scotland) Act 1972 confers power on the court to order the production and inspection of documents which appear to the court to be property as to which any question may relevantly arise in existing or likely proceedings.[17] The proceedings are not limited to actions involving death or personal injury. Because it is possible to seek declarator against the insurer in the action against the insured to establish the latter's liability[18] disclosure of the policy details at this stage seems competent.

6.18 The Insolvency Act 1986[19] and the Bankruptcy (Scotland) Act 1985[20] contain a number of provisions requiring bankrupts and the officers and employees of

[14] In *Bradley v Eagle Star Insurance Co Ltd*, [1989] AC 957 (see para 4.6 above), the House of Lords held that, as the third party's action against the insurer could not succeed, "it would therefore serve no useful purpose to make the order for pre-action discovery sought by her". It is interesting that the House of Lords did not suggest that the third party was not entitled, in any event, to pre-action disclosure of policy information because such disclosure was not relevant to the issues between the parties, the liability of the insured not having been established.

[15] [1995] 2 Lloyd's Rep 437. The facts of the case are set out at para 7.2 below.

[16] *Bekhor v Bilton* [1981] QB 923, 939 and 948.

[17] Before the proceedings are commenced, application is by way of petition under rule 64 of the Court of Session Rules; afterwards it is by motion in the proceedings under rule 35.

[18] See para 4.27 above.

[19] See, for example, ss 133, 155, 235-237, 291, 333 and 366.

companies which have been wound up to provide information to creditors and to insolvency practitioners and official receivers. We are not aware of these provisions having been used to obtain policy information to assist the claims of third parties.

OVERVIEW OF LIMITATIONS ON THIRD PARTIES' RIGHTS TO DISCLOSURE OF POLICY INFORMATION

6.19 As we have seen in this Part and in Part 4, the interpretation given to section 2 of the 1930 Act in the *Nigel Upchurch* and *Woolwich* cases has caused problems to third parties and to insolvency practitioners. Some of these problems may be alleviated if some of Lord Woolf's recommendations are implemented. The Woolf Report recommends that parties should be able to make pre-action applications for disclosure against potential defendants in all cases.[21] It also recommends the use of pre-action protocols setting out codes of practice for litigants in certain types of case, including those involving personal injury.[22] One of the specific purposes of the protocols is said to be to enable parties "to obtain the information they reasonably need in order to enter into an appropriate settlement".[23]

6.20 The draft pre-action protocol for personal injury cases[24] would provide for early notification of the defendant's insurer.[25] The Woolf Report suggests that employees face particular problems in identifying the insurers of their insolvent employers.[26] Members of the APIL and the ABI have also suggested that there should be a

[20] Sections 44-47 and s 64.

[21] *Access to Justice*, Recommendation 140.

[22] *Access to Justice*, Recommendation 99. Specific pre-action protocols are also proposed for medical negligence and housing cases.

[23] *Access to Justice*, Chapter 10, p 107, para 1.

[24] Agreed by members of the APIL and the ABI.

[25] *Access to Justice*, Chapter 10, p 109, para 8. The protocol provides as follows "The letter will be sent to the defendant (and, where known, the defendant's insurer) as soon as the claimant is aware of sufficient facts to show that there is a possible claim. It will contain enough information to enable the defendant to investigate and broadly value the claim. Where the claimant does not know the identity of the defendant's insurer, the defendant would be requested to forward a copy of the letter to his insurers and notify the claimant of their identity and his policy number within 28 days of receiving the notification. Within three months of receiving notification of a claim, the defendant must reply saying whether or not liability is accepted. If it is not, the defendant must give factual reasons for disputing liability and send copies of relevant documents. A list of the documents which should be automatically disclosed by the prospective parties in common types of personal injury cases has been drawn up. It is intended that, as recommended by the group, the exchange of these documents will be prescribed by practice direction. In most cases, this will obviate the need for any further disclosure after proceedings have begun. The group has also identified the documents that should be provided on request in particular circumstances".

[26] As we noted at Part 2 above, a significant number of claims under the 1930 Act involve employers' liability cases. Employers may have a duty to exhibit certificates of insurance at their place of business under Regulation 6(2) of the Employers' Liability (Compulsory Insurance) General Regulations 1971. If implemented, the draft Employers' Liability (Compulsory Insurance) General Regulations would maintain this requirement and make it clear that a certificate of insurance had to state either that the policy satisfies the minimum level of cover or, if it does not, what cover it does provide. See paras 4 and 5 of the draft Regulations.

central register of insurance policies to enable a claimant to identify a potential defendant's insurer in cases to which pre-action protocols would apply.[27]

6.21 We discuss in Part 13 below whether the 1930 Act should be amended to allow third parties increased rights to disclosure.[28]

[27] This suggestion is endorsed by Lord Woolf. See *Access to Justice*, Chapter 10, p 110, para 12.

[28] At para 13.4 we give our provisional conclusion that disclosure should be given within 14 days of the disclosing party becoming aware that a third party had a possible claim under the Act.

PART 7
THE DISTRIBUTION OF A LIMITED INSURANCE FUND TO MULTIPLE CLAIMANTS

7.1 In some cases, an insured's negligent act may cause him to incur liability to a number of third parties. If the value of the insurance is inadequate to meet all potential claims in full, the issue arises as to the basis on which the insurance fund should be distributed. This problem is not restricted to cases involving the 1930 Act but may be more serious for third parties in such cases as they are unlikely to recover much if anything from the insolvent insured. This issue is not addressed by the 1930 Act[1] but was raised in the context of the Lloyd's litigation. As we shall see, the Court of Appeal in *Cox v Bankside*[2] decided that the fund should be distributed to those third parties who established their cases first. In this Part, we discuss the background to this case, the grounds for the Court of Appeal's decision and the implications of that decision. We also consider whether a more equitable system of distribution could be achieved under the existing law.

COX V BANKSIDE

Background to the case: the Lloyd's litigation

7.2 Having suffered disastrous losses, many of the members of the Lloyd's syndicates (the so-called Names) started proceedings against their agents who had been contractually responsible for the Names' underwriting. They claimed damages for negligence and breach of contract, arguing that the agents had exposed them to unacceptable risks. Because of the mass of actions being brought by Names, the Commercial Court adopted a management plan in July, 1993. The actions were divided into categories and individual cases selected from each to determine preliminary issues of importance to all and to try various allegations of negligence.

7.3 It was clear that some agents were likely to go into insolvency and that Names would have to proceed against the agents' insurers under the 1930 Act. The agents sued by the Names were insured against errors and omissions ("E & O") liability,

[1] A reading of Hansard confirms that those passing the Act did not consider this issue, the Master of the Rolls suggested in *Cox v Bankside* [1995] 2 Lloyd's Rep 437 at 458. See para 7.12, n 11 below.

[2] [1995] 2 Lloyd's Rep 437. To seek an authoritative ruling on the basis on which the funds payable should be allocated, the E & O underwriters issued an originating summons joining as defendants all those agents and Names whom they wished to be bound by the decision of the court. When the summons was heard by Phillips J, actions brought by some of the Names had already proceeded to judgment and some agents had gone into liquidation (judgment on liability was given on April 13, 1994 in favour of two individual Names in *Brown v KMR Services, Sword-Daniels v Patel* [1994] 4 All ER 385 and on October 4, 1994, in favour of Names on a number of syndicates managed by the Gooda Walker agents in *Deeny v Gooda Walker Ltd* [1994] CLC 1244. Judgment was also about to be given in favour of the Feltrim Names). The successful Names were due soon to make applications for interim payments (in February 1995, Phillips J made an interim payment order under RSC O 29 for £230 million).

but the level of cover was capped and, clearly, would be insufficient to meet all potential claims. Of vital importance to all concerned was the basis on which the funds payable by the E & O underwriters would be allocated. One view was that funds should be allocated on a "first past the post" or "first come, first served" basis. The alternative view was that funds should be distributed pro rata to all Names who successfully established their claims.

7.4 The issue was heard first by Phillips J, who held that there was no legal basis for a rateable distribution. He suggested that "first past the post provides a relatively simple and practicable basis for distributing reinsurance recoveries".[3]

The judgment of the Court of Appeal

7.5 On appeal, the appellants argued again, unsuccessfully, that there was a legal basis for rateable distribution of the insurance fund, which they claimed should be held by a receiver and distributed according to directions from the court. The Court of Appeal rejected the applicability of the principle that equality is equity to allow all Names who had already established or would establish claims to share rateably in the fruits of the insurance cover[4] and held that there was no implied agreement to share the insurance proceeds. Nor was there anything to suggest that a trust of the policy or of its proceeds existed; the requisite certainties for the establishment of a trust were not satisfied.

7.6 The argument that the 1930 Act should not be construed in such a way as to make late coming plaintiffs worse off than they were before that Act was introduced was also rejected.[5] The court held that nothing in the 1930 Act or in any case decided under it supported a scheme of rateable allocation: the object of the Act was to avoid third party liability insurance money going into the general pool available for

[3] Phillips J also held that the contingent rights transferred to third parties were of no value until the liability of the insured had been established but held that an interim payment order satisfied the requirement laid down in *Post Office v Norwich Union Fire Insurance Society Ltd* [1967] 2 QB 363 for "establishment" of the liability. *Cox v Bankside* [1995] 2 Lloyd's Rep 437, 442. See para 4.5 above.

[4] It was held, however, in *Cox v Deeny* [1996] LRLR 288 that this principle might be applied to determine how reinstatement provisions should operate in cases involving multiple claimants against a limited insurance fund. Judge Diamond considered whether the same claim could be brought against original and reinstated cover where the per cause limit was not initially exceeded, but where the first layer cover was exhausted by subsequent claims. It was appreciated by third parties that their access to reinstated cover would be improved if they were able to structure their claims in such a way as to ensure that the reinstatement provisions were triggered. The insurers argued that they, rather than the insured or third parties, should be able to determine the order in which payments were made to claimants. Judge Diamond, at p 299 rejected the insurers' arguments, holding that the holder of a liability policy was entitled to decide the order in which claims were met by the insurer. Where the 1930 Act applied, this right passed to the third parties. Third parties in a group action would usually agree a sequence maximising recoveries. In other cases, "there might be nothing to govern the priority in which claims were to be paid save the maxim 'equality is equity'."

[5] The old law would have given third parties a rateable share in an insolvency fund swollen by the insurance proceeds. See para 7.12 below.

all creditors. It did not stipulate what was to happen if there was insufficient insurance money for all third party claimants.[6]

7.7 The appellants also argued that the court should not allow the Commercial Court's management plan to become a source of injustice. It suggested that the court had the power to antedate all judgments in favour of Names to the date of the first such judgment and that all agents or Names receiving insurance proceeds could be ordered to pay such sums to receivers.[7] Receivers would distribute these sums in accordance with directions from the court.

7.8 Although the Master of the Rolls[8] described this argument as "the most promising", it was still rejected by the court. The court held that the management plan was not designed to lay out in advance the timetable for the selected cases up to and including judgment and said that it was not persuaded that the plan itself had led to unforeseen results or to inequities which would not otherwise have existed.[9] The court did not rule on whether it had the power to antedate

[6] See paras 1.2 and 7.1, n 1 above.

[7] RSC, O 42, r 3 provides as follows: "(1) ... a judgment or order of the Court or of an official or special referee takes effect from the day of its date (2) Such a judgment or order shall be dated as of the day on which it is pronounced, given or made, unless the Court or referee, as the case may be, orders it to be dated as of some other earlier or later day, in which case it shall be dated as of that other day". The notes to O 42, r 3 state that the power of the court to ante-date a judgment ought only to be invoked on some good ground, where there is something exceptional on the facts. See RSC, O 42, r 3(3), *Borthwick v Elderslie SS Co* [1905] 2 KB 516 and *Belgian Grain etc Co Ltd v Cox & Co (France) Ltd* [1919] WN 317. Also, jurisdiction cannot be conferred by ante-dating an order where it does not otherwise exist. *Re Keystone Knitting Mills Trade Mark* [1929] 1 Ch 92. Reference was also made to *Banque Financiere de la Cite v Parc (Battersea) Ltd* (unreported) 20 April 1993 a case involving two rival creditors seeking charging orders over the property of a debtor company. The company was not yet in liquidation but its assets were not adequate to satisfy both creditors. Earlier in the proceedings, the court had unintentionally placed one of the creditors at a procedural disadvantage, preventing it from seeking a charging order ahead of the other creditor. Because of this special factor, the court synchronised the making of the charging orders so that they would rank equally. It was argued by analogy in *Cox v Bankside* that the Commercial Court's management plan was a special factor which justified the court approving a system of rateable distribution to claimants.

[8] At p 458.

[9] Saville LJ, as the judge in charge of the Commercial Court, commented at length on the effect of the management plan. He said that actual and potential claimants in the Lloyd's litigation had been warned by the court at an early stage that the question of rights to available resources was an issue which was likely to arise in the future. He also said that the cases which had been selected as test cases were those which had been "at a sufficiently advanced stage to enable them to be put into a timetable for hearings commencing almost immediately". He agreed that the effect of the plan might be to allow parties to pass the post in an order different to that which might otherwise have been the case but concluded that "the overall problem would have remained exactly the same, namely too many claimants chasing too few resources. In other words, it is the very nature of the Court process itself (planned or unplanned) which creates the lack of equal treatment where the first to judgment has priority over those that follow, for in the nature of thing not all cases can be heard at the same time. In these circumstances I am not persuaded that the management plan has itself led to unforeseen results, or to inequities in the sense of producing unequal treatment that would not otherwise have existed. At best what can be said is that some of those who may lose out may not be the same as those who would have lost out had no plan been made". Phillips J had suggested, at first instance, that the

judgments, but said that it would be slow to do so unless reasonably confident both that the objective of fair treatment would be achieved and that any directions designed to correct one injustice would not produce other and perhaps even greater injustices.[10]

7.9 Sir Thomas Bingham MR outlined some of the problems of a non-statutory scheme:

> It would have to take account of a multiplicity of plaintiffs, with claims based on different grounds, relating to different periods, against different defendants; it would have to take account of a multiplicity of defendants, some fully insured, some not, some solvent, some insolvent with different E & O cover for different underwriting years; it would have to remain in force for a period of years, during which period the receivers of each policy fund would have to seek the approval of the Court to make interim distributions, and would no doubt have to be paid out of the proceeds of the cover; and it would have to do all this without the authority of any statute or subordinate legislation.

THE IMPLICATIONS OF THE DECISION OF THE COURT OF APPEAL IN *COX V BANKSIDE*

7.10 As we have seen, the Court of Appeal in *Cox v Bankside* considered that there was no basis on which pro rata schemes of distribution of insurance proceeds to claimants under the 1930 Act could operate under the current law, at least with regard to cases brought as part of the Lloyd's litigation. The court also doubted the workability of such schemes.

7.11 Although many of the arguments raised in *Cox v Bankside* were particular to the Lloyd's litigation, similar issues might arise in other cases involving multiple claimants against a limited insurance fund.

7.12 The effect of the first past the post system may be that the position of subsequent claimants is worse than if the 1930 Act had not been passed. Before the 1930 Act was passed, the insurance proceeds would have gone into the general assets of the bankrupt individual or insolvent company. Creditors would have received a share of those assets in the form of a dividend representing the value of the debt owed to them by the insured as a percentage of the available fund. Under the 1930 Act, some third party creditors may get nothing. It has been suggested that, although Parliament did not appear to foresee the problems which might arise from multiple claims when passing the 1930 Act, "it is also safe to assume that it did not intend to create inequity between liability claimants or to reward the winners of a rush to judgment or execution".[11]

timetabling of cases by the Commercial court had meant that those whose claims succeeded first were not necessarily those who had acted most diligently.

[10] Saville J rejected the argument that the scheme for rateable distribution proposed would "avert more injustice than it would create, even assuming, which it is not necessary to decide, that the Court does have power to backdate judgments in such circumstances".

[11] Sir Jonathan Mance "Insolvency at Sea" [1995] LMCLQ 34. Responding to this argument in *Cox v Bankside* [1995] 2 Lloyd's Rep 437 at 458, the Master of the Rolls said, "I agree

7.13 Some might argue that those who have taken the risk and expense of obtaining judgment first should be in a better position than claimants who have taken no significant steps to advance their cases. There may, however, be a number of reasons why claimants have not taken such steps. As we have seen, in the Lloyd's litigation, one of the reasons why certain cases were heard first was the management plan laid down by the Commercial court. More generally, the hearing of third party actions and the date of judgment will depend partly on when cases are listed by the court and the speed at which they are heard.

7.14 Another reason for delay might be that third parties postpone starting or pursuing proceedings while settlement negotiations are in progress. As a matter of policy, we suggest that parties should not be discouraged from seeking a negotiated settlement of their disputes, which may be the effect of the "first past the post" system.[12]

7.15 The first past the post system of distribution may also prejudice the most needy third parties as impoverished claimants may have to delay pursuing their claims while they wait for legal aid applications to be approved.[13] It may also prejudice those who act slowly because they are unaware of their rights or have been badly advised as to how to enforce them.

7.16 A claimant may go to the expense of bringing proceedings only to discover that other claimants' cases have been listed first or have proceeded more quickly and that judgment in those cases[14] will mean that, even if his case succeeds, he will receive little or none of the insurance money. As we have seen, his problems may be exacerbated if he cannot obtain disclosure of the insured's insurance position.[15]

COULD A MORE EQUITABLE DISTRIBUTION OF INSURANCE PROCEEDS BE ACHIEVED UNDER THE EXISTING LAW?

7.17 We consider briefly below whether, despite the approach taken by the court in *Cox v Bankside*, a more equitable distribution of insurance proceeds could be achieved under existing law. We look at the procedural rules governing representative and group actions and at the power of the court to consolidate actions.[16]

Representative, group and consolidated actions

7.18 It is suggested that the rules on representative and group actions cannot be relied on to offer a solution to the problems raised in *Cox v Bankside*. English procedural rules allow but do not require proceedings affecting numerous persons with the

that Parliament cannot so have intended but that is because Parliament never considered such a situation at all". See para 7.1, n 1 above.

12 *Access to Justice*, Recommendation 229.

13 We discuss at paras 4.31-4.35 the funding problems which third party claimants may face.

14 Or an order for interim payments. See para 7.4, n 3 above.

15 See Part 6 above and Part 13 below. At para 13.4 we suggest that there should be a continuing duty of disclosure.

16 See also para 15.5 below.

same interest[17] to be brought or defended on their behalf by a single plaintiff or a number of plaintiffs.[18] The court may not of its own motion appoint a person or persons to represent an as yet unascertained class or persons who may be interested in the proceedings.[19]

7.19 The essence of such a claim is that the persons represented should be acting in concert to achieve the same remedy. The fact that all have suffered in different ways as a result of the same wrongful conduct is not sufficient. In personal injury litigation such a test calls for the drawing of very fine distinctions as to what constitutes the 'same' injury.[20] It appears that the only relief available in the representative proceedings is declaratory and that each party (representative or represented) must bring a separate action to recover damages. A representative plaintiff is free to conduct the case as he wishes and can discontinue or compromise the action as he chooses. The represented persons will not, however, be affected by either of these courses[21] and may bring further proceedings if the action does not proceed to judgment.[22]

7.20 In some cases, it may be appropriate for actions to be consolidated. By selecting 'lead actions' and adopting 'master pleadings' some duplication can be avoided and issues common to a number of actions settled "for the benefit of all."[23] In this kind of arrangement, the parties agree to abide by the court's findings on a small number of cases in so far as they affect the whole and may agree the distribution of

[17] 'Same interest' requires that the persons concerned should (1) have a common interest; (2) have a common grievance; and (3) be likely to benefit from any relief which could be obtained in the action: *Smith v Cardiff Corporation* [1954] 1 QB 210. There are no equivalent Scottish rules.

[18] RSC, O 15, rr 12 & 13 and CCR, O 5 rr 5 & 6.

[19] It may do so only in cases involving the estate of a deceased person, property subject to a trust, or the construction of a written document including a statute, if one or more of the conditions set out in RSC, O 15 r 13(2) is satisfied. See also CCR, O 5, r 6.

[20] RSC, O 15, r 12(3) states that the appointment of a representative party *may* be possible in an action in negligence, referring to *Campbell v Thompson* [1953] 1 QB 445. See also CCR O 5, r 5.

[21] *Handford v Storie* (1834) 2 S & S 196.

[22] Once a declaratory order has been made, though, the issues which it covers are *res judicata* as between members of the 'class' and the defendant or defendants. *Prudential Assurance Co Ltd v Newman Industries Ltd* [1981] Ch 229 and *Markt & Co Ltd v Knight Steamship* [1910] 2 KB 1021.

[23] See for example *Davies v Eli Lilly & Co* [1987] 1 WLR 1136 (the Opren litigation). RSC, O 4, r 9 provides that the court may consolidate matters or order that they be tried at the same time if it appears to the court that some common question of law or fact arises in them or that the rights to relief claimed are in respect of or arise out of the same transaction or that for some other reason it is desirable to make an order. See also *Phillips v Society of Lloyd's, The Times* 9 May 1997 where Colman J ordered that case to be heard at the same time as another case involving the Lloyd's reconstruction and renewal package and directed that, for case management purposes, all other Lloyd's Names who wished to commence proceedings relating to the package should do so by a certain date so that their cases could be joined and heard at the same time. The effect of cut off dates set by the court is discussed at n 25 below.

costs and damages between them.[24] There may be a role for the court and the Legal Aid Board in managing such schemes[25] and this may increase if recommendations contained in the Woolf Report are implemented.[26]

7.21 In a Scottish case, *Bell v Lothiansure Ltd*[27] a number of disappointed investors claimed against an insurance broker who had persuaded them to invest in bonds that turned out to be worthless. The broker went into liquidation and its indemnity insurers were brought into the action as potentially liable if the broker were to be found liable. The investors' actions were conjoined and decree was eventually granted for payment by the insurer to all of them. The claims would have abated rateably if the amount of cover under the policy had been insufficient to meet them in full.

7.22 A pursuer who considers that the defender is in financial difficulties may obtain a warrant from a Scottish court to arrest on the dependence of the action. This could be used to arrest the sums payable under the policy, so obtaining a preference over other pursuers in respect of sums eventually found to be payable by the insurer. This preference would not be lost if other pursuers obtained decree

[24] In lead action cases the courts have adopted a cost-sharing approach to plaintiffs' costs. In *Davies v Eli Lilly & Co & others* [1987] 1 WLR 1136 an order was approved whereby "where particular plaintiffs incurred costs either personally or through the legal aid fund in pursuing lead actions, or thereby became liable to pay costs to the defendants, every other plaintiff should contribute rateably on a per capita basis", but see *Access to Justice*, Chapter 17 paras 60-62 for some criticism of this approach, which caused non-assisted Plaintiffs in Opren to consider discontinuing because of the costs risks until a benefactor stepped in. See also *Chrzanowska v Glaxo Laboratories Ltd*, *The Times* 13 March 1990 for another cost-sharing approach.

[25] In litigation brought by victims of Benzodiazapine, for example, cut-off dates were set by the court (to serve proceedings) and the Legal Aid Board ("The LAB") (to apply). However, such cut-off dates have no statutory authority. See the Legal Aid Board, *Issues arising for the Legal Aid Board and Lord Chancellor's Department from Multi-Party Actions*, May 1994 and *AB v John Wyeth and Brother* [1993] 4 Med LR 1: court-set cut-off dates are not fatal to other claims and the status of those who 'miss' them is unclear. If further claimants form a second group, they can presumably pursue their own, entirely separate, litigation. Conduct of group actions will largely be a matter for individual firms of solicitors to agree between themselves. The LAB's power to award a group action contract to a single firm may simplify matters, but seems to be little used. See reg 152(3) Civil Legal Aid (General) Regs 1989, as amended in 1992. At paras 4.31-4.35 above, we discussed proposed changes to the funding of civil proceedings which minimise the role of the LAB.

[26] Since the Report the Lord Chancellor's Department has published a consultation paper *Multi-Party Situations: Proposed New Procedures*, which canvasses detailed proposals for multi-party situations. Where proceedings will or may require collective treatment either the parties or the LAB should make an application to the court (or the court may initiate one) for the creation of an MPS which the court will decide whether or not to certify. The court will discuss with parties a strategy for publicity to alert existing and potential claimants to the existence of the MPS. Cases will be assigned to a single judge, who will deal with them throughout. Cases outstanding at the time of certification will be transferred to the judge conducting the MPS and may be stayed pending directions in the course of the MPS. Views are sought as to whether claimants should actively register an interest in the action or whether the judge should be permitted to lay down an opt out system (under which the claimant would be taken to be covered unless they opt out). The former avoids limitation problems since entering on the register could be treated as bringing an action. The judge will give directions as to the criteria for joining the register so that a filter can be operated.

[27] (Unreported)19 January 1990, Lord Cameron of Lochbroom.

first, provided the arresting pursuer followed up his action without undue delay. However, arrestment is not competent if the insured defender is already insolvent and no preference is obtained if the arrestment is executed within 60 days prior to sequestration or liquidation. Where several pursuers arrest the same fund, their arrestments may be equalised if executed within certain times of each other.[28] Such pursuers would rank equally irrespective of the dates of their decrees.

7.23 At present there is no multi-party procedure in Scottish courts. The Scottish Law Commission's Report on *Multi-Party Actions*,[29] published in July 1996, made recommendations for the introduction of such procedures. The recommended procedure would be voluntary; a pursuer might elect to take part in a class action but could not be compelled to do so.

CONCLUSIONS

7.24 In situations where a number of third parties suffer loss as a result of the same event or series of events, they may choose to support representative proceedings or to take part in a group action. The court cannot currently require parties to take part in group actions but may be able to do so in some cases if recommendations in the Woolf Report are implemented. It may in some cases use its power to consolidate actions or to order cases to be heard at the same time. In Part 16, we consider whether any inadequacies in the existing law would justify the introduction of a statutory scheme providing for the rateable distribution of an insurance fund to third party claimants under the Act.

[28] Bankruptcy (Scotland) Act, Sch 7, para 24.

[29] Scot Law Com No 154.

PART 8
PRIVATE INTERNATIONAL LAW

8.1 Claims under the 1930 Act may raise a number of private international law questions if one or more of the third party, the insured or the insurer is domiciled abroad, if the act of the insured giving rise to liability occurred outside this jurisdiction or if the insurance policy is governed by foreign law. A third party claimant will wish to know whether there are any conflict of laws rules preventing him from relying on the 1930 Act or from suing the insurer in the United Kingdom. If the insured has not yet been declared bankrupt or wound up, the third party may also wish to know whether he can bring bankruptcy or insolvency proceedings against the insured in this country to enable him to proceed with his claim under the Act. Private international law issues are not addressed by the 1930 Act. The only judicial consideration of such issues, in *Irish Shipping Ltd v Commercial Union Assurance Company plc ("The Irish Rowan")*[1] was obiter and inconclusive.

8.2 In this Part, we look first at what rules may currently govern the applicability of the 1930 Act in cases with a foreign element. Next, we consider the circumstances in which a third party can bring bankruptcy or insolvency proceedings against the insured in the United Kingdom and whether the third party can proceed under the Act if the insured has been declared bankrupt or wound up in another jurisdiction. Finally, we consider the jurisdictional rules governing where a third party can sue the insurer.

WHAT RULES GOVERN THE APPLICABILITY OF THE 1930 ACT TO CASES WITH A FOREIGN ELEMENT?

8.3 There is little authority on the private international law rules governing the applicability of the 1930 Act or of other statutes which provide third parties with a right of direct action against insurers. The applicable law for deciding a contractual or tortious or delictual claim by the third party against the insured could be applied to decide whether or not the statutory rights could be exercised by the third party. It may not, however, be correct to classify the statutory right as contractual or tortious. The relationship between the insurer and the insured under the policy is contractual. The act by which the insured incurs liability to the third party is usually tortious, although it may be a breach of contract.[2] The third party's rights against the insurer are grounded in the Act. We look now at two cases in which the private international law rules applicable to statutes providing rights against insurers have been considered.[3]

[1] [1991] 2 QB 206.

[2] ABI statistics and our findings in our analysis of applications to restore companies to the register show that the majority of applications under the Act relate to claims in tort. See para 2.10 above and Appendix C.

[3] We discuss in Part 16 the views of legal commentators on which private international rules should apply in such cases and seek consultees' views on this issue.

The Irish Rowan

8.4 In *The Irish Rowan*, Staughton LJ spoke obiter on what he referred to as the territorial scope of the 1930 Act.[4] The other judges in the Court of Appeal[5] declined to comment on this issue. Staughton LJ said that where statutes did not contain provisions relating to their territorial scope, reference had to be made to conflict of law rules. He referred to the fact that the proper law of the contract of insurance was the preferred solution in Dicey & Morris then referred to another argument that the proper law should be the lex situs (in this context, the law of the place where the insurance proceeds are payable).[6]

8.5 He suggested that there was "a substantial argument against the proper law of the contract being the connecting factor" as section 1(3) of the Act was designed to override the contract of the parties and the intention of Parliament could be frustrated "if it were open to the parties to a contract of insurance to exclude the operation of section 1 by choosing a foreign proper law ... ." He concluded, however, that

> It is fairly arguable that the lex situs [the law of the place where relevant property is situated] governs the transfer of an obligation under section 1 of the Act, or the proper law of the contract (despite what I have just said) or the law governing the bankruptcy or liquidation.

Davenport v Corinthian Motor Policies at Lloyd's[7]

8.6 A different approach was taken by the Scottish court in *Davenport v Corinthian Motor Policies at Lloyd's*, which involved an action under section 151 of the Road Traffic Act 1988. Lord Prosser rejected the view that the matter related to delict, holding that it was "a claim based upon the statutory provisions and upon nothing else".[8]

8.7 Third party rights under the 1930 Act are somewhat different, however. Instead of creating a new right for third parties, which is the effect of the Road Traffic Act, the 1930 Act operates by transferring an insured's existing rights against the insurer under the insurance contract to a third party.

[4] [1991] 2 QB 206, at 219.

[5] Purchas LJ and Sir John Megaw.

[6] Referring to dicta of Jenkins and Romer LJJ in *Re United Railways of the Havana and Regal Warehouses Ltd* [1960] Ch 52 at 87. Reference would need to be made to the contract of insurance which will normally determine the place of payment. If the contract is silent, payment should probably take place where the debt "is properly recoverable and can be enforced", which will usually be the residence or place of business of the payee. See *Chitty on Contract* (27th ed 1994) and M Clarke *The Law of Insurance Contracts* (3rd ed 1997) p 804. Another view is that the insurer's liability could be classified as a debt, situated at the domicile of the debtor and subject to the laws prevailing there: Stromholm, *Torts in the Conflict of Laws* (1961) p 165. See also *New York Life Ins Co v Public Trustee* [1924] 2 Ch 101, 109 per Pollock MR.

[7] 1991 SLT 774.

[8] *Ibid,* at p 778.

8.8 The position is complicated by the fact that the 1930 Act transfers different types of rights to third parties. Staughton LJ's view in *The Irish Rowan*[9] was that each rule of law enacted by the 1930 Act should be examined separately. He suggested, for example, that the application of conflict of law rules to the transfer of rights under section 1 of the Act could theoretically produce different results from the rule creating the right to disclosure of information under section 2:

> Just because two rules of law are enacted in the same statute, it does not follow that the same connecting factor applies in each case. One cannot assume that the territorial application of the statute is wholly governed by the same test; one must examine each rule of law which it enacts.[10]

8.9 It is difficult to draw a conclusion as to the rules which govern the applicability of the 1930 Act. This issue may arise more often in the future with the development of the single market and increased cross border insurance. We discuss in Part 16 whether the Act should specifically address private international law issues and, if so, what criteria should determine its applicability. We consider next when third parties can bring insolvency proceedings against the insured in this country then consider the rules which will govern whether or not a UK court will have jurisdiction to hear an action under the 1930 Act.

WHEN CAN THE THIRD PARTY BRING BANKRUPTCY OR WINDING UP PROCEEDINGS AGAINST THE INSURED IN THE UNITED KINGDOM?

8.10 The third party's ability to petition for the bankruptcy or winding up of the insured may be important for two reasons. First, the happening of one of the insolvency situations set out in the Act is a precondition to his acquiring rights under it. Secondly, as Staughton LJ suggested,[11] the applicability of the Act may depend on whether or not the insured was declared bankrupt or wound up in the United Kingdom.

8.11 In some cases, the insured may be domiciled abroad and have no tangible assets in this country. We consider the powers of the court to grant bankruptcy and winding up petitions against foreign insureds and whether third parties can rely on the 1930 Act if the insured has been made bankrupt or wound up in a foreign jurisdiction

Petitioning for the bankruptcy or winding up of foreign debtors

8.12 Statutory provisions relating to bankruptcy and winding up are contained in the Insolvency Act 1986 and the Bankruptcy (Scotland) Act 1985.[12] Section 265(1) of the Insolvency Act 1986 provides that a petition for the bankruptcy of a foreign insured cannot be presented unless the debtor is domiciled[13] in England and

[9] [1991] 2 QB 206. See paras 8.4-8.5 above.

[10] *Ibid*, at p 149.

[11] See para 8.5 above.

[12] And in the Insolvency Rules and other statutory instruments.

[13] A person is "domiciled" in England and Wales if he is deemed by English law to have his permanent home there.

Wales, is personally present there on the day on which the petition is presented, or, at any time in the period of 3 years ending with that day, has been ordinarily resident,[14] or has had a place of residence or has carried on business there.[15] The debt need not have been incurred within the jurisdiction, nor need the petitioning creditor have any territorial connection with England and Wales.[16]

8.13 In Scotland, the Court of Session has jurisdiction to sequestrate the estates of an individual who was habitually resident in Scotland or had an established place of business there at any time in the year immediately preceding the presentation of the petition.[17] The estates of an entity may be sequestrated if it had an established place of business in Scotland in the year immediately preceding the presentation of the petition or was constituted or formed under Scottish law and at any time carried on business in Scotland.[18] A sheriff has similar jurisdiction in relation to individuals or entities in the sheriffdom.[19]

8.14 The Insolvency Act distinguishes between registered companies registered under the Companies Acts in England and Wales, Scotland and Northern Ireland and unregistered companies (which include foreign companies). Courts in England and Wales have exclusive jurisdiction to wind up companies registered there and Scottish courts have exclusive jurisdiction in relation to companies registered in Scotland.[20] Jurisdiction is exclusive even if the company has offices in another part of the United Kingdom. The courts of the place where an unregistered company has its principal place of business have jurisdiction to wind it up.[21] In some circumstances, Northern Irish companies may be wound up in England and Wales or Scotland if they have a principal place of business there.[22]

8.15 The provisions relating to the winding up of unregistered (including foreign) companies by the English or Scottish court are contained in sections 220 to 229 of

[14] He is "ordinarily resident" if he habitually and normally resides lawfully there from choice and for a settled purpose apart from temporary or occasional absences. See *Shah v Barnet London Borough Council* [1983] 2 AC 309.

[15] For these purposes, carrying on business is stated in section 265(2) to include: (a) the carrying on of business by a firm or partnership of which the individual is a member, and (b) the carrying on of business by an agent or manager for the individual or for such a firm or partnership. In other cases (for example, where the insured has carried on business himself or through an agent in this country for three years or more), a third party may be able to serve a bankruptcy petition on the insured abroad. A bankruptcy petition may, with the leave of the court, be served outside England and Wales in such manner as the court may direct: Insolvency Rules 1986 r 12.12(2).

[16] *Re Myer, ex p Pascal* (1876) 1 ChD 509.

[17] Bankruptcy (Scotland) Act 1985, s 9(1), (5).

[18] Bankruptcy (Scotland) Act 1985, s 9(2), (5).

[19] Bankruptcy (Scotland) Act 1985, s 4.

[20] The Insolvency Act 1986, s 120(1).

[21] The Insolvency Act 1986, s 221(3).

[22] Section 221(2) Insolvency Act 1986. See *Re a Company (No 007946 of 1993)* [1994] 1 BCLC 5651.

the Insolvency Act 1986. Under section 221(5), unregistered companies[23] may be wound up by the court[24] if the company is dissolved, or has ceased to carry on business, or is carrying on business only for the purpose of winding up its affairs, if it is unable to pay its debts, or if the court is of the opinion that it is just and equitable that the company should be wound up. Section 6 of the Bankruptcy (Scotland) Act 1985 provides for the sequestration of the estates of an entity which includes a body corporate (except a company registered under the Companies Acts or where sequestration is expressly or by implication excluded by an enactment). The estates of a foreign company could be sequestrated under this provision.

8.16 The Insolvency Act does not appear to restrict the wider jurisdiction of the court (as developed through case law) to wind up a foreign company which has assets in England.[25] The court has interpreted "assets" very widely and has held that it is not necessary for the company to have actual assets in the jurisdiction if there is a reasonable likelihood of benefit accruing to the creditors in the event of the winding up order being made.[26] In *Re Compania Merabello San Nicholas* SA,[27] Megarry J made a winding up order against an overseas company whose only asset was its claim against its insurer, a P & I Club.[28] In *Re Eloc Electro-Optieck and Communicatie BV,* the court granted a winding up order on the basis that the petitioner had a reasonable chance of obtaining a benefit from an outside source (the state redundancy fund) were such an order to be made.[29] In *Okeanos Maritime Corp*,[30] Peter Gibson LJ suggested that the petitioner need only show "a sufficiently close connection with the jurisdiction, and that there is no more appropriate jurisdiction for the winding-up of the company".[31] There is a lack of Scottish authority on this point. It is not clear whether Scottish courts have an equivalent

[23] Although the term "unregistered company" is not expressly defined to include foreign companies, it is well settled that such companies may be wound up under these provisions: *Re Mercantile Bank of Australia* [1892] 2 Ch 204.

[24] *Re Hibernian Merchants Ltd* [1958] Ch 76, 78. It should be noted that English courts can even wind up a foreign company which has already been dissolved or otherwise ceased to exist under the laws of the country where it was incorporated. See s 225 of the 1986 Act.

[25] See *Banque des Marchands de Moscou (Koupetschesky) v Kendersley* [1951] Ch 112.

[26] See Harman J in *Re a Company ex parte Nyckeln Finance* [1991] BCLC 539.

[27] [1973] Ch 75. See Dicey and Morris, *The Conflict of Laws* (12th ed 1993) p 1127.

[28] Referring to dicta in the *Banque des Marchands de Moscou* case. See also *The Allobrogia* [1979] 1 Lloyd's Rep 190, where Slade J held that where the only alleged asset was a right of action, the petitioners did not need to show that the action was one which was certain or likely to succeed; they needed merely to show that the action had a reasonable possibility of success.

[29] The company in that case carried on business in England but had no assets here.

[30] *Re a Company (No 00359 of 1987)*[1988] Ch 210.

[31] In that case, there was a reasonable possibility that a winding up would benefit creditors because of the possibility of the liquidator recovering contributions to the assets of the company under the fraudulent trading and wrongful trading provisions of the Insolvency Act 1986 (ss 213 and 214). See also n 22 above. Dicey & Morris, *The Conflict of Laws* (12th ed 1993) pp 1120-1123 suggests that the main alternative forum would normally be the country where the company is incorporated or where it holds assets. See also *Re Mid East Trading* [1997] 3 All ER 480.

jurisdiction to wind up a foreign company, but sequestration may be possible if a Scottish court has jurisdiction.[32]

8.17 As well as considering whether or not another forum would be more appropriate, the court may also consider whether the insurance proceeds are payable in this country so that the third party is likely to receive a benefit here if the order is made. It is unlikely that an order would be made in respect of an overseas company which was insured by an English or Scottish insurer under a contract whose proper law was English or Scottish law but which did not provide for payment in England or Scotland and which had no other assets within the jurisdiction. The situs of the payment obligation may be vital to establish a sufficiently close connection with the jurisdiction.[33]

8.18 In the context of the 1930 Act, it might be argued that there is no possibility of the third party receiving any benefit from the winding up of the insured if it is claimed by the insurer that certain conditions precedent to the liability of the insurer have not been met.[34] The court hearing an application for winding up might, however, be reluctant to consider the merits of any possible defence in a future claim against an insurer under the Act.[35]

CAN THIRD PARTIES RELY ON THE ACT WHERE THE INSURED HAS BEEN MADE BANKRUPT OR WOUND UP IN A FOREIGN JURISDICTION?

8.19 The provisions of the 1930 Act refer only to insolvency proceedings brought within the United Kingdom and it is assumed that a winding up order against the insured made in a foreign jurisdiction is unlikely to be sufficient to found jurisdiction under the Act.[36] However, it is possible in some circumstances for a company which has already been wound up in another jurisdiction also to be wound up in this country.[37]

8.20 Were the EU Convention on Insolvency Proceedings ever to come into force, it might limit the situations in which bankruptcy or winding up proceedings could be

[32] See para 8.15 above.

[33] See *Re a Company (No 00359 of 1987)(Okeanos Maritime Corp)* [1988] Ch 210, discussed at para 8.16.

[34] See, for example, the decision of the House of Lords in *The Fanti* that pay to be paid provisions in P & I Club rules were conditions precedent to the liability of the club which had to be met by the insured. See para 5.61 above. At first instance in *The Padre Island* [1987] 2 Lloyd's Rep 529, 537 Saville J doubted the decision reached in *The Allobrogia* (see para 8.16, n 28): "In *The Allobrogia* Mr Justice Slade was only concerned with the question whether or not the point was well arguable. He concluded that it was - which could hardly be denied, since generations of commercial lawyers have advised on the point and their views sharply differ".

[35] Were it to do so, parties would be exposed to the costs and delay of a preliminary hearing of an issue which would be tried again in subsequent proceedings.

[36] See Michel "The Third Parties (Rights Against Insurers) Act 1930, in a Modern Context" [1987] LMCLQ 228, 232. The Law Society's Joint Insolvency Law Sub Committee has suggested that the Act could be amended to allow for this possibility, while recognising that, "the amendment would need to take account of any limitations in other member states on the ability to make an individual bankrupt".

[37] Under s 221(5)(a) of the Insolvency Act 1986.

brought against some foreign insureds[38] and, if the ability of third parties to rely on the 1930 Act depends on whether the insured was made bankrupt or wound up in this country, limit the circumstances in which third parties could rely on the Act.[39]

WHERE CAN THE INSURER BE SUED?

8.21 Whatever the basis for the applicability of the Act, a third party will only be able to proceed against the insurer if the court has jurisdiction over the insurer. The jurisdictional rules governing where a claimant can pursue his claim will depend on the nature of his claim, on where the defendant is domiciled and, in some cases, on his identity. The EC Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters ("the Brussels Convention")[40] has altered the common law conflicts rules in the case of disputes in jurisdictions which are signatories to the Convention.[41]

The Brussels Convention

8.22 The Brussels Convention lays down common jurisdictional rules for all states bound by it. The court first seised of an action has exclusive jurisdiction over it[42] and the courts of each state are required to recognise and enforce the judgments of courts in other states.[43]

8.23 Insolvency proceedings are excluded from the Brussels Convention: subsection 2 of Article 1 of the Brussels Convention provides that the Convention does not apply to "[b]ankrupty, proceedings relating to the winding-up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings". If a claim under the 1930 Act is viewed as relating to UK insolvency law, it might be held to fall outside the scope of the Convention.[44] This question has not yet come before the court and it is not clear what approach the courts might take to it.[45]

[38] The Convention would only have effect within the European Union.

[39] We outline the provisions of the draft Convention in Appendix A.

[40] Implemented in the UK by the Civil Jurisdiction and Judgments Act 1982.

[41] Members of the European Free Trade Association ("EFTA") who are signatories of the Lugano Convention, 1991 are also bound by these rules, although most of these (bar Iceland, Norway and Switzerland) have joined the EU and therefore adhere to the Brussels Convention itself.

[42] Article 21.

[43] Articles 25-49.

[44] If the insurer was not present in England then the jurisdiction of the court would depend on whether the third party could serve a writ on the insurer under RSC O 11, r 1. See paras 8.25-8.26 below.

[45] In *Gourdain v Nadler* [1979] ECR 733, it was held that a claim against a director of an insolvent company that he should contribute to the assets of the insolvent company fell outside the Convention. Cf *Re Hayward* [1997] Ch 45, where it was held that an action by a trustee in bankruptcy to recover from a third party property which belonged to a bankrupt did not fall outside the Convention. As voluntary winding ups (which are covered by the 1930 Act) are not "proceedings", they are probably not excluded from the Convention in any event. See Briggs and Rees, *Civil Jurisdiction and Judgments* (2nd ed 1997) pp 32-33.

8.24 Under Article 2 of the Brussels Convention, an action must generally be brought in the courts of the jurisdiction in which the defendant is domiciled. There are a number of exceptions to this, however. Articles 7 to 12A lay down special rules for "matters relating to insurance" on the basis that the insured's bargaining power is likely to have been weaker than that of his insurer.[46] Under Article 8, a policyholder can sue his insurer in the place of his own or his insurer's domicile.[47] Article 9 provides that, in respect of liability insurance, the insurer can also be sued in the courts of the place where the harmful event occurred.[48] Article 10 provides that the insurer may be joined into proceedings brought by a third party against the insured, if the law of the court allows it. It also provides that Articles 7, 8 and 9 shall apply to actions brought by the injured party directly against the insurer, where such direct actions are permitted and that, if the law governing such direct actions provides that the insured may be joined, the same court shall have jurisdiction. Article 10 appears to suggest that the third party can use the special rules in Articles 7 to 9 and that the court hearing the action against the insurer shall also have jurisdiction if the third party can join the insured into those proceedings.[49]

Claims not governed by the Brussels Convention

8.25 Under RSC, Order 11, rule 1(2), an English writ may be served outside the jurisdiction without the leave of the court provided that the English court has jurisdiction under the Civil Jurisdiction and Judgments Act 1982. If the Act does not apply, a defendant can only be sued in England if the court gives leave under RSC Order 11. A Scottish court cannot acquire jurisdiction by service of writs outside Scotland.

[46] Briggs and Rees, *Civil Jurisdiction and Judgments* (2nd ed 1997) p 120, n 630. These rules do not apply to reinsurance, but apply to all forms of insurance, whatever the status and strength of the insured. See *New Hampshire Co v Strabag Bau AG* [1992] 1 Lloyd's Rep 361. In the case of other contractual disputes, Article 5(1) provides for the dispute to be heard by the courts of the jurisdiction where the disputed contractual term was to have been performed. Article 5(3) provides that tortious disputes may be referred to the courts of the jurisdiction "where the harmful event occurred".

[47] The insurer can only sue the insured in the place of the insured's domicile. Under Article 12, the ability of the parties to contract out of these rules is restricted: they can only do so in contracts of marine and aviation insurance or after the dispute under the policy has arisen.

[48] The draft Fourth Motor Insurance Directive, which requires member states to ensure that the injured party has a direct claim against the insurer of the party liable to pay compensation (art 1), requires insurers to have claims representatives in each member state (art 2). This is to ensure that third parties claiming against the insurer of a foreign driver have someone in their own state who will deal with their claims. The draft Directive is currently under review. See DTI Consultation Document January 1997; Insurance Law Monthly, April 1997, p 6; Post Magazine, 21 November 1996. If the directive is implemented, third party victims of motor accidents will always be able to bring proceedings against the insurer in their own state.

[49] We discuss in Part 12 below whether or not the 1930 Act should be amended to allow third party claimants to claim against the insurer alone or to claim against both insurer and insured in one action.

8.26 Before granting leave, the court must be satisfied that the case falls within one of the paragraphs of RSC Order 11, rule 1(1),[50] that the plaintiff has a good arguable case, that there is a serious issue to be tried and that it is proper for it to exercise its discretion to grant leave to serve out. The court will also consider whether it is clearly the appropriate court (the "forum conveniens") to hear the case, being the most suitable for the interests of all the parties and for the end of justice.[51]

[50] Set out in Appendix B.

[51] See *Kuwait Asia Bank EC v National Mutual Life Nominees Ltd* [1991] 1 AC 187 and *Spiliada Maritime Corp v Consulex Ltd* [1986] AC 460.

PART 9
LIMITATION[1] AND PRESCRIPTION

9.1 Rules limiting the period in which actions can be brought against defendants and providing for obligations to prescribe after a specified period of time are imposed on the basis that it is unreasonable for potential defendants to live indefinitely with the threat of litigation and because actions become increasingly difficult to try when events are no longer clearly remembered and evidence is lost.[2] In this Part, we look briefly at English and Scottish rules on limitation and prescription. We consider how these rules operate to limit the period in which third parties can proceed against insurers under the 1930 Act. We also look at whether, where proceedings against the insurer have been started by the insured within the period during which he can proceed against the insurer, third parties can be substituted in those proceedings. We look first at the position under English law,[3] then at Scottish law.[4]

ENGLISH LAW

The limitation period applicable to disputes arising under contracts of indemnity

9.2 Actions founded on contract have a time limit of six years and usually run from the date at which the breach occurred. There has been some debate as to when the six year limitation period should begin to run with regard to contracts providing liability insurance cover.[5] The better view is that the cause of action arises when the insured has suffered loss as a result of the insured event.[6] As we have seen, following *Post Office v Norwich Union Fire Insurance Society Ltd*,[7] "loss" in the

[1] Limitation statutes were consolidated in the Limitation Act 1980 which applies to arbitration as well as to actions in the High Court. See s 34(1) of the 1980 Act. "Prescription" refers to Scottish law.

[2] See dicta of Best CJ in *A'Court v Cross* (1825) 3 Bing 329 and of Lord Atkinson in *Board of Trade v Cayzer, Irvine & Co* [1927] AC 610.

[3] See paras 9.2-9.17. As we shall see, it is difficult to draw conclusions on these issues from relevant English case law. This may be partly due to the fact that *London SS Owners Mutual Insurance Association Ltd v Bombay Trading Co Ltd (The "Felicie")* [1990] 2 Lloyd's Rep 21, *Lefevre v White* [1990] 1 Lloyd's Rep 569 and *The Jordan Nicolov Montedipe SpA v JTP-RO Jugotanker (The "Jordan Nicolov")* [1990] 2 Lloyd's Rep 11, decided respectively in 1987, October and December 1989 were all reported in 1990. It is not clear whether the court in the second and third of these decisions was fully aware of the earlier cases. *The Felicie* was not referred to in *Lefevre v White* and *Lefevre v White* was not referred to in *The Jordan Nicolov*.

[4] See para 9.18 below. In Part 17, we discuss whether our suggested reforms of the Act would have any implications for the English and Scottish rules on limitation and prescription and whether these rules should be amended or clarified.

[5] T Prime and G P Scanlan, *The Modern Law of Limitation* (1993) p 91.

[6] See the consideration of this issue in Malcolm Clarke *The Law of Insurance Contracts* (3rd ed 1997) pp 739-740.

[7] [1967] 2 QB 363. See also *Bradley v Eagle Star Insurance Company Ltd* and *The Fanti*. See Parts 4 and 5 above.

context of liability insurance is incurred when liability has been established.[8] The limitation period governing the insured's right of action against the insurer will, therefore, run from the date when the third party has established the liability of the insured.

9.3 The limitation period may start to run earlier if there has been a purported repudiation of the insurance contract by the insurer and if the insured has accepted the fact of repudiation by the insurer, but not its validity.[9] The basic rule is that, where there has been a repudiation, a right of action accrues as soon as the repudiation has occurred even if, at that time, the plaintiff has suffered no loss.[10]

Limitation and the 1930 Act

Lefevre v White

9.4 In *Lefevre v White*,[11] the third party plaintiff had suffered severe injuries when, on 22 July 1972, the car in which he was being driven by the insured went out of control.[12] The plaintiff first brought proceedings in France, claiming damages for personal injury, but these were unsuccessful and, in 1977, he started proceedings in England. The proceedings were settled before the court on 16 December 1981 and judgment was given in favour of the plaintiff against the insured. On 8 December 1987, the insured issued a writ against the insurer claiming an indemnity. On 9 December 1987, the insured was made bankrupt by the plaintiff. On 3 June 1988 (nearly six and a half years after he had settled his claim against the insured), the plaintiff started proceedings against the insurer based on the 1930 Act.

[8] Contrast a case not involving liability insurance, *Callaghan v Dominion Insurance Company* [1997] 2 Lloyd's Rep 541, the court held that under the indemnity policy the loss occurred and the limitation period started to run at the date when the event insured against occurred, not at the date of the repudiation of the policy. The limitation period would only be postponed if the policy prevented the insured's contractual right to seek an indemnity from arising until a particular date. See para 4.5, n 7 and para 4.7, n 13 as to when the right to an indemnity from the insurer arises.

[9] So that the insured claims damages instead of performance of the contract. See para 9.17, n 25 below. If the insured chooses not to accept repudiation by the insurer, the rights and obligations of both, including the insurer's duty to indemnify, will continue. A new right of action (governed by a fresh limitation period) will accrue when the insurer breaches the insurance contract by refusing to indemnify the insured when liability has been established and payment is due. This was the case in *Lefevre v White* [1990] 1 Lloyd's Rep 569. The defendant insurer had repudiated liability on the ground that the car driven by the insured was not roadworthy, a breach of one of the policy conditions. The insurer argued that the insured had accepted its repudiation of liability and that his claim to enforce the policy was statute barred six years from the date of the acceptance of the repudiation. Popplewell J reviewed the contacts between the insured and the insurer and held that the insured had not accepted the repudiation. Other aspects of this case are discussed further at paras 9.4-9.7 below.

[10] See *Gibbs v Guild* (1881) 8 QBD 296.

[11] [1990] 1 Lloyd's Rep 569.

[12] At the time, there was no compulsory insurance for passengers, so the plaintiff could not rely on the regime of third party rights laid down by the Road Traffic Acts.

9.5 The plaintiff raised two arguments as to why his action was not time barred. First, the insured had himself issued a writ against the insurer within the limitation period and the plaintiff, standing in the shoes of the insured, was merely continuing in his own name a claim which was not statute barred. Alternatively, the rights of the insured were transferred to him on the bankruptcy of the insured and it was at that moment that his right to sue came into existence and that the limitation period with regard to his claim against the insurer should run.

9.6 Popplewell J rejected both these arguments, holding that the plaintiff's claim was statute barred. The plaintiff could not rely on the proceedings started by the insured as his claim under the 1930 Act was one

> in his own name which gives him the benefit of the *whole* of a successful judgment...the third party ... has his own cause of action direct against the insurance company, namely to exercise his right to claim all the benefits which attached to the insured. He is not carrying on proceedings in the sense envisaged by O 15, r 7; he is merely exercising the rights to claim which previously existed in the insured. To do so, *he* must issue proceedings within six years of the cause of the action arising.

9.7 In rejecting the argument that the third party had no cause of action until the bankruptcy of the insured, Popplewell J said:

> I confess that I find neither logic nor sense in that argument. It would enable a plaintiff to bring an action under the 1930 Act years outside any limitation period contemplated by the Limitation Acts. It would undermine totally the concept that liability under the policy is the starting point for determining when the cause of action arises.[13] Finally it gets no support that I can see from the wording of the Act - indeed, such authorities as there are and the terminology of the Act itself are to the contrary sense.

***The Felicie*[14]**

9.8 A different approach to these issues appears to have been taken two years earlier by Phillips J in *The Felicie*, a decision not referred to in *Lefevre v White*. In September 1976, the insured wrongfully failed to carry a cargo owned by the third party. On 21 July 1981, the High Court of Singapore gave judgment in favour of the third party against the insured. The insured's claim for an indemnity from its P & I Club was rejected on 21 April 1982. On 24 June 1987, on the petition of the

[13] [1990] 1 Lloyd's Rep 569, 578, Popplewell J also suggested that allowing the plaintiff's view to prevail would have meant "grossly extending the limitation period" if, for example, the determination of the insured's claim and his bankruptcy had been delayed by another two or three years. This view accords with the principle, upheld in many earlier cases, that: "where in an action in the English courts the plaintiff seeks relief and the defendant pleads limitation, the issue which an English court has to determine is whether the action before the court, *and not some other action*, has been instituted within the relevant limitation period" per Roskill J in *Compania Colombiana de Seguros v Pacific Steam Navigation Co* [1965] 1 QB 101 at 125. Emphasis added. That case involved the assignment of a cause of action by the insured to an underwriter.

[14] [1990] 2 Lloyd's Rep 21.

third party, the Companies Court appointed the Official Receiver as provisional liquidator of the insured. The Club rules contained a *Scott v Avery* arbitration clause[15] and, on 17 July 1987, an arbitrator was appointed by the provisional liquidator on behalf of the insured. Following the making of a winding up order on 29 July 1987 the third party appointed an arbitrator on that day.

9.9 At the hearing on 13 November 1987, the third party sought a declaration that, included in the rights of the insured against the Club transferred to it on that date, was the right to continue the arbitration commenced on behalf of the insured on 21 July. It also claimed that it was entitled to continue the arbitration which it had commenced on 29 July in its own name.

9.10 The Club argued that the obligation to arbitrate was a qualification upon the right to recover an indemnity and that the obligation did not constitute one of the rights of the insured under the contract of insurance.[16] If, contrary to this submission, the entitlement to pursue an arbitration was a right under the contract of insurance, the effect of the 1930 Act was not to substitute the third party for the insured in existing legal proceedings: in the case of litigation; substitution could only occur pursuant to court rules and, in the case of arbitration, there was no mechanism for substitution. Practical problems would arise if third parties were substituted in existing proceedings. The third party's claim was time barred because the valid appointment of an arbitrator by the third party on 29 July was outside the limitation period which started to run when the third party obtained judgment against the insured on 21 July 1981.

9.11 Phillips J reviewed previous case law and said that:-

> Having considered these authorities, I am driven to the conclusion that there is no wholly satisfactory explanation for the basis upon which, whether by assignment inter partes or by transfer under the 1930 Act, the transferee acquires the right and obligation to arbitrate in his own name. That under the 1930 Act the right to commence and pursue an arbitration does vest in the third party, together with the substantive rights under the contract of insurance is, however, beyond dispute.

9.12 He held that the argument that third party claimants under the 1930 Act were automatically substituted in arbitration proceedings begun by the insured within the limitation period was "unsound in law and impossible in practice". Among the problems which he suggested automatic substitution would cause were disputes as to the liability for existing costs[17] and one or more third parties becoming party to the arbitration without notice.[18]

[15] See paras 5.36-5.40 above.

[16] Similar issues were raised in *Edwards v Minster* (unreported) 10 March 1994. See paras 5.52- 5.54 above.

[17] To find otherwise, he said, would mean that a third party would be a party to a dispute which was none of his making. Also, some of the rights and obligations arising out of the arbitration were personal to the parties and could not be transferred to third parties under the 1930 Act: "For example, prior to the winding up of the insured, both the insured and the insurer may have incurred costs in the arbitration. The 1930 Act cannot operate in such a way as to transfer to the third party the right to recover costs expended by the insured.

9.13 Phillips J allowed the third party to continue the arbitration proceedings commenced in its own name, however, although the legal basis of his decision is not clear.[19] He said that:

> Had I felt that my decision would have the effect that [the third party] would be faced with a time bar that would not have been applicable to [the insured], I would have felt it necessary to reconsider my conclusion. It would be absurd if the effect of the 1930 Act, in circumstances such as those of this case, were to be to defeat what might otherwise have been a good claim by the insured. Such a result would be diametrically opposed to the purpose of the Act.

The Jordan Nicolov[20]

9.14 Similar issues arose in *The Jordan Nicolov,* which did not involve the 1930 Act but which related to the right of a legal assignee of a right of action under a charterparty to be substituted in arbitration proceedings started by the assignor. The shipowners argued that the assignee must start a fresh arbitration, relying on *The Felicie.*[21] The plaintiff charterers and insurer argued that the assignee took the cause of action subject to the obligation to arbitrate and with the benefit of the legal remedy in the arbitration, including the appointment of the arbitrator. They referred to section 136 of the Law of Property Act 1925 which provides that "all legal and other remedies" pass on assignment.

9.15 Hobhouse J distinguished *The Felicie* on the basis that it had been decided under the 1930 Act. He suggested that it was the claim that substitution occurred automatically under the 1930 Act which had most concerned Phillips J and that, where there was a legal assignment under the Law of Property Act, the position was different in that notice would have been given to the other parties. He held

Nor would it seem right that the third party would automatically find himself potentially liable for costs already incurred by the insurer - nor that the insurer should be constrained to accept a substitute for the party initially liable for his costs. Even in liquidation the insured may offer better security than the substituted third party".

18 This was, he said, "a startling concept and one that cannot operate in practice. Some procedural mechanism is required to substitute one party for another, whether in arbitration or in litigation". Practical complications would arise, he suggested, if "claims had been advanced in respect of liabilities to more than one third party, or in respect of both third party liability and another head of loss suffered by the insured. Automatic transfer would in those circumstances seem to result in different claimants with different interests being compulsorily joined in the same arbitration, a situation which is without precedent under English arbitration procedure".

19 Sir Jonathan Mance has suggested that: "Since the fresh arbitration would have been outside the six year period, this must mean that he took the view, opposite to that taken by Popplewell J, that the insured's commencement of proceedings within the limitation period sufficed to enable fresh proceedings to be commenced by the third party outside the limitation period". See "Insolvency at Sea" [1995] LMCLQ 34, at 50.

20 *Montedipe SpA v JTP-RO Jugotanker (The Jordan Nicolov)* [1990] 2 Lloyd's Rep 11.

21 And on *Cottage Club Estates Ltd v Woodside Estates Co Ltd* [1928] 2 KB 463.

that an assignee could rely on the appointment of an arbitrator by the assignor and had the right to intervene in the pending arbitration started by his assignor.[22]

9.16 The approach of Hobhouse J was endorsed by the Court of Appeal in *Baytur SA v Finagro Holding SA*.[23] The Court of Appeal agreed that assignees can join pending proceedings but held that assignees do not automatically become parties: they must first apply to court for an order under RSC, O 15, r 7(2) or, in the case of arbitration, give notice to the other party and submit to the jurisdiction of the arbitrator.[24]

The position of third party claimants

9.17 It is not clear from the cases we have discussed whether the limitation period governing third parties' claims under the 1930 Act will be based on that applying to the insured's right of action against the insurer. It is also unclear whether third parties can substitute themselves for the insured in court or arbitration proceedings, although this may be more likely following *The Jordan Nicolov* and *Baytur South Africa v Finagro Holding SA*. If the approach taken by Popplewell J in *Lefevre v White* is followed, third parties may find their right of action statute barred before it has accrued.[25] In most cases, however, third parties will be able to

[22] However, on the facts of the case, there was no evidence before the arbitrators to enable them to decide which was entitled to the award and the charterers had failed to anticipate the need to prove title to sue. The appeal was, therefore, dismissed.

[23] [1992] 1 Lloyd's Rep 134.

[24] Because this had not occurred, the arbitration lapsed and arbitration proceedings would have to be started again. See also dicta of Mance J in *ICIC v Tsavliris Maritime Co* [1996] 1 WLR 774 at 785, a case involving the rights of an Italian company succeeding to the rights and obligations of another company. Mance J said of RSC O 15, r 7 (CCR O 5, r 11) that "it should be irrelevant whether or not the limitation period had expired prior to the assignment, transmission or devolution in question. All that should matter is that the original litigation was commenced in time".

[25] Particularly if there has been a purported repudiation of the insurance contract by the insured. See para 9.3 above. This supposes that the insured's right to damages in respect of the repudiation is transferred to the third party under the Act. See Peter Goldsmith QC's speech to the British Insurance Law Association, 3 February 1995. In *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827, Lord Diplock held that the primary right to an indemnity and a right to damages against an insurer in breach are both "rights under the contract". It appears that, under the general law, limitation periods may run, notwithstanding that the plaintiff's right of action has not accrued. See *Sevcon v Lucas* [1986] 1 WLR 462, where the House of Lords held that a plaintiff's cause of action relating to an alleged patent infringement by the defendant accrued as soon as there was an infringement, notwithstanding the fact that the plaintiff could not have sued until the patent application had been granted, rather than filed. See also *O'Connor v Isaacs* [1956] 2 QB 288 and *Coburn v Colledge* [1897] 1 QB 702. Cf *Musurus Bey v Gadban* [1894] 2 QB 352 which involved an action against a defendant who had been the Turkish Ambassador in London, with diplomatic immunity. The Court of Appeal held that the limitation period ran from the date when the defendant ceased to be immune rather than from when the wrong was committed. The House of Lords' decision in *Sevcon v Lucas* has been described as "neither necessary nor desirable" and it has been suggested that: "it is surely objectionable in principle to hold that time runs against the plaintiff although he cannot yet bring an action".

bring bankruptcy or winding up proceedings against the insured to ensure that their actions are not statute barred.[26]

SCOTTISH LAW

9.18 The Prescription and Limitation (Scotland) Act 1973[27] provides for a three year limitation period for claims based on death[28]or personal injury.[29] The period runs from the date of the injury or, if later, the date on which it was reasonably practicable for the pursuer to have become aware of the fact that the injuries were sufficiently serious to bring an action, and that the injuries were attributable to an act or omission of the defender (or his employee or agent). Any period during which the pursuer is incapable or under the age of 16 is not counted. The court has a discretion to allow an action to proceed notwithstanding these time limits.[30]

Prescription and contracts of indemnity

9.19 Obligations arising out of a contract generally prescribe five years after they become enforceable if no relevant claim has been made or the subsistence of the obligation relevantly acknowledged within that period.[31] The obligation under a contract of insurance will, therefore, prescribe five years after the date when the obligation became enforceable.[32] The obligation becomes enforceable when the insurer becomes liable to indemnify the insured under the policy. As we have seen, the Scottish courts have held that section 1 of the 1930 Act provides for the statutory assignation of the insured's rights to the third party.[33] If the insurer's obligation to pay under the policy has prescribed against the insured, it will, therefore, also have prescribed against the third party.

9.20 Section 7 of the 1973 Act provides for a long-stop prescriptive period of twenty years which cuts off any rights that survive the five year period.[34] The insured's

[26] Although they may be tempted to delay bringing proceedings, if the insured claims that he will recover soon from the insurer or if arbitration proceedings are taking place. Section 34(5) of the Limitation Act 1980 provides that where the High Court orders that an arbitration award be set aside or, after an arbitration begins, orders that the arbitration remit should cease to have effect, it may also order that the period between the commencement of the arbitration and the date of the court order be excluded in calculating the limitation period applicable to the dispute.

[27] Amended by s 2 of the Prescription and Limitation (Scotland) Act 1984.

[28] Section 17 of the 1973 Act.

[29] Section 18 of the 1973 Act.

[30] Section 19A of the 1973 Act, added by s 23(a) of the Law Reform (Miscellaneous Provisions)(Scotland) Act 1985.

[31] Prescription and Limitation (Scotland) Act 1973, s 6 and Sch 1, para 1(g). Section 6 provides for any time during which the creditor in the obligation was induced to refrain from making a relevant claim due to fraud or error by the debtor to be excluded from the five year period. Any period during which the third party claimant was under a legal disability is also not counted, but this applies only to the original creditor (the insured in the context of claims under the 1930 Act) and not to any statutory assignee.

[32] *Scott Lithgow v Secretary of State for Defence* 1989 SLT, Lord Keith of Kinkel, at p 238E.

[33] *Greenlees v Port of Manchester Insurance Company* 1933 SC 383. See para 5.5, n 8 above.

[34] Because of the various circumstances extending that period. See para 9.18 above.

claim against the insurer under the policy[35] will therefore prescribe in any event if it has subsisted for a continuous period of 20 years without any relevant claim having been made or the subsistence of the obligation having been relevantly acknowledged.

9.21 The insurer may purport to repudiate the policy. If the repudiation is accepted by the insured, the policy lapses and there are no rights under it that could be transferred to the third party. Section 3 of the 1930 Act renders void any agreement between the insurer and the insured after liability has been incurred to the third party and after insolvency has occurred so as to defeat or affect the rights that would be transferred to the third party under the Act. If the repudiation is not accepted, any dispute as to the continued existence of the obligation under the policy may have to be the subject of legal proceedings. The effect of these would be to confirm or deny the existence of the obligation rather than altering the date at which the prescriptive period starts to run.

Substitution of the third party in proceedings started by the insured

9.22 If the insured had commenced proceedings against the insurer in relation to the policy then the third party as statutory assignee under the 1930 Act is entitled to be sisted (to be added as a party) to the proceedings.[36] The same rule seems to apply to arbitrations,[37] although the insured would remain bound by the submission to arbitration.

[35] With certain exceptions which are not relevant here.

[36] *Fearn v Cowper* 1899 7 SLT 86.

[37] Irons and Melville, *Law of Arbitration in Scotland* (1903), p 349; *Henry v Hepburn* (1835) 13 S 361.

PART 10
REFORM: APPROACH TO REFORM

THE STRUCTURE OF THIS REFORM SECTION

10.1 In Parts 11 to 17, we consider a number of options for reforming the 1930 Act and seek consultees' views on the extent to which those reform options might address some of the problems which we have identified as arising from current law and practice. In this Part, we set out principles governing our approach to reform and consider the impact of Lord Woolf's report on the Civil Justice System.[1] In Part 11, we consider whether the scope of the Act should be extended or restricted. In Part 12, we consider what rights third parties should have under an amended Act and when those rights should arise. In Part 13, we suggest reforms to the Act's disclosure provisions and, in Part 14, possible limitations on the ability of insurers to rely on defences against third party claimants. In Part 15, we consider whether a statutory system of rateable distribution should be introduced to replace the current "first come first served" system. In Part 16, we consider whether the private international law aspects of the Act should be clarified. In Part 17 we seek consultees' views on the limitation of claims under the Act. A summary of our provisional conclusions and consultation questions is set out in Part 18.

10.2 As we have seen, several of the problems which we discussed in Parts 4 to 9 are inter-related as they have a common source, namely the judicial construction of sections 1 and 2 of the Act in such a way as to require a third party to establish the liability of the insured before acquiring rights under it. We set out below our provisional conclusion that the transfer of rights under the Act should not be conditional on the third party first establishing the liability of the insured.[2] We suggest that the third party should acquire rights once two events have occurred; the incident giving rise to the liability of the insured and one of the insolvency events set out in the Act. His right of action would be against both the insurer and the insured. We suggest that such a reform would itself alleviate a number of the problems faced by third parties under the current Act.

PRINCIPLES GOVERNING OUR APPROACH TO REFORM

10.3 We set out our general approach to reform in Part 1.[3] The following are some of the more specific principles which have guided our approach to the reform of particular issues, although, as will be seen, it has often been necessary to seek a balance between those principles.

Freedom of contract

10.4 We do not consider that it is within the scope of our review of the Act to examine when insurance should be in place, nor to determine the terms on which insurance

[1] *Access to Justice*, July 1996.

[2] See para 12.6 below.

[3] See paras 1.13-1.19 above.

should be available. Subject to the provisions of particular legislation in this field,[4] it is for the insured and insurer to determine these matters. In general, the insurer should be in no better or worse position as a result of the insured's insolvency nor under any greater liability to the third party than he would have been under to the insured. On the other hand, the insurer should not be placed in a better position.

10.5 Where we have suggested restrictions on the rights of insurers (for example on their ability to rely on defences)[5] or extensions to their duties under the Act (for example their duty to disclose policy information),[6] this has usually been in response to problems associated with the insolvency or pending insolvency of the insured or because the third party is in a worse position than the insured would have been had he been seeking an indemnity against the insurer.

In general, the courts should be able to resolve disputes between all relevant parties in one set of proceedings

10.6 One of the great objects of the Judicature Acts was "to bring all parties to disputes relating to one subject-matter before the Court at the same time so that the disputes may be determined without the delay, inconvenience and expense of separate actions and trials."[7] We consider that this approach remains the correct one. In so far as it may be unfair in a particular case, or undesirable from a case management point of view, to have all the issues tried at the same time, an order can be made for some issues to be tried separately, but still in the context of a single set of proceedings.[8]

Relevant information relating to potential disputes should be available at an early stage

10.7 Consistent with the aims and approach of the Woolf Report,[9] it is generally desirable that parties should be in possession of all relevant information about potential claims at an early stage so that they can make an informed assessment of the strength of their case and enter into realistic settlement negotiations.

Competing claims to limited insurance funds should be dealt with in a manner which seeks to achieve fairness, certainty and cost efficiency

10.8 Where the insurance monies available are insufficient to meet all the claims to them brought by third parties, they should be distributed in a manner which seeks to achieve fairness between the respective claimants, but which is also, so far as possible, certain, predictable and cost efficient.[10]

[4] Where Parliament has decided that insurance should be compulsory.

[5] See Part 14 below.

[6] See Part 13 below.

[7] RSC O 15, r 6(1).

[8] See Part 12 below.

[9] See, for example, *Access to Justice*, Chapter 10, para 4 and Chapter 12, paras 47 and 53. See Part 13 below.

[10] See Part 15 below.

THE IMPACT OF LORD WOOLF'S REPORT ON THE CIVIL JUSTICE SYSTEM ON OUR PROPOSED REFORMS

10.9 In March 1994, Lord Woolf was asked by the Lord Chancellor to review the current rules and procedures of the civil courts in England and Wales. Lord Woolf published his final report, *Access to Justice*, in July 1996, recommending fundamental changes to the civil legal system in England and Wales. He has proposed a "three tier system" of legal proceedings[11] and new Civil Procedure Rules, intended to replace the Rules of the Supreme Court 1965 and the County Court Rules 1981, have been drafted. The proposals do not affect the separate legal system in Scotland, where Lord Cullen recommended changes to the procedures in the Outer House of the Court of Session.[12]

10.10 We refer in this paper to a number of Lord Woolf's proposals and suggest how they might affect proceedings under the current 1930 Act and under an amended Act. We mention, for example, Lord Woolf's proposals to improve parties' rights to pre-action and non-party disclosure,[13] to require parties to abide by pre-action protocols setting out codes of practice in certain areas of litigation[14] and to lay down new procedures for expedited hearings[15] and multi-party actions.[16]

10.11 One of Lord Woolf's main objectives is increased openness and co-operation between parties,[17] an approach building on recent procedural reforms such as the use of witness statements, skeleton arguments and pre-trial hearings.[18] In our view, many of our provisional conclusions are in line with his approach to reform.

[11] An expanded small claims court would take claims up to £5000, personal injury claims of up to £1000 would remain within this ceiling (The Lord Chancellor on 18 October 1997 announced the increase to £5000 from £3000 at the Law Society Conference). Claims of between £5,000 and £10,000 would be dealt with under a fast-track procedure, unless certain factors made it more appropriate for them to be dealt with by the multi-track procedure. Claims of over £10,000 (and smaller claims considered more appropriately dealt with by a more complex procedure) would be dealt with under a multi-track procedure.

[12] Review of Business of the Outer House of the Court of Session, The Hon Lord Cullen, December 1995.

[13] See para 6.19 above.

[14] See para 6.20 above.

[15] See para 12.11, n 30.

[16] See para 7.20, n 26 above and para 15.5, n 9 below.

[17] See *Access to Justice*, Section 1, page 4, para 9.

[18] See para 12.11, n 33 and para 13.2, n 12 below.

PART 11
THE SCOPE OF THE ACT

11.1 In Part 1, we considered whether the aim of liability insurance is to protect the interests of third parties to whom the insured incurs liability as well as to protect the financial interests of the insured.[1] We asked whether the claims of third parties currently able to proceed under the 1930 Act should be preferred in all cases to those of the insured's other creditors and suggested that consideration should be given to the effect of amending the Act on insurers, the insured and officeholders as well.[2] In Part 2, we looked at developments in insurance law and practice since 1930 and noted how much insurance markets have changed since the Act was introduced. We raised the possibility of the Act being extended to cover reinsurance policies or restricted to certain types of claim.

11.2 In this Part, we consider first whether the Act should be extended to reinsurance policies. We then consider arguments for the Act continuing to apply to all liability insurance policies and discuss options for limiting its scope to risks covered by compulsory insurance, to claims in respect of death or personal injury, to consumer as opposed to commercial type claims or to tortious or delictual, as opposed to contractual claims. In Part 12, we consider whether a third party's right of action under the Act should continue to be conditional on the happening of one of the insolvency situations set out in the Act.[3]

SHOULD THE ACT BE EXTENDED TO REINSURANCE POLICIES?

11.3 As we have seen, section 1(5) of the Act excludes reinsurance from its provisions. Given the growth in the use of reinsurance, we need to consider whether this exclusion should be removed so that third parties would have a right of recourse against reinsurers when the insurer is insolvent and unable to meet their claims.[4] We consider briefly first the regulation of insolvent insurers.

The Policyholders Protection Act 1975[5]

11.4 The Policyholders Protection Act 1975 allows policyholders of insolvent UK or EU insurers carrying on business in the UK[6] to recover from a fund paid for by the

1 See paras 1.10-1.11.

2 See para 1.15 above.

3 We set out our provisional view, at para 12.10 below, that this should be the case. We also seek consultees' views at para 12.49 below on whether third parties should acquire rights against insurers on the disappearance of the insured.

4 The likelihood of insurers facing financial problems because of pay first clauses in reinsurance contracts may be reduced by the decision of the House of Lords in *Charter Reinsurance Co Ltd v Fagan* [1996] 2 WLR 726 and the insolvency clause recommended by the ABI, the Institute of London Underwriters and LIRMA following that decision. See para 5.62, n 78 above. The recommended clause is set out in Appendix D.

5 The 1975 Act will be amended by the Policyholders Protection Act 1997 which is likely to be brought into force early in 1998.

6 The Act originally applied only to policyholders under UK policies issued by insurers authorised to carry on business under the Insurance Companies Act 1982. Section 3 of the

insurance industry and administered by the Policyholders Protection Board.[7] Reinsurance is excluded from the scope of the Act.[8]

11.5 It appears that third parties may fall within the definition of policyholder in the 1975 Act.[9] However, the position is not clear and we understand that the Board has not yet had to decide on this point. Were third parties to have rights under the 1975 Act, those meeting the Act's eligibility criteria would not need a right of recourse against reinsurers.[10]

The problems of extending the Act to reinsurance policies

11.6 As we have already noted, reinsurance arrangements have become increasingly complex.[11] Simple, facultative reinsurance, where the duty to indemnify a particular liability can be traced through the insurer to a particular reinsurance policy is increasingly rare[12] and a risk may be reinsured a number of times.[13]

amended Act extends protection to the policyholders of any UK authorised or EU company carrying on business in the UK or selling directly into the UK.

7 A private policyholder can recover 90% of the amount owed to him by the insurer under the policy in the case of certain classes of non-compulsory insurance. A policyholder (whether a private policyholder or not) may recover 100% of such amount in the case of certain types of compulsory insurance. Any policyholder who does not qualify for full payment under the 1975 Act may prove for his loss in the insurer's liquidation. Sections 6(8A) and 8(2A), to be inserted by the 1997 Act, provide that the duty of the Board "shall not apply unless the liability is in respect of a protected risk". Protected risks are defined by reference to their geographical location within the European Union. See s 4(3) of the amended Act, which does not affect contracts entered into before the commencement of that section. The Board is entitled to require the policyholder to assign to it 100% of his rights against the insurer under the policy. The Board then stands in the shoes of the policyholder and receives any dividends paid in the liquidation. In the unlikely event that a dividend of more than the 90% paid to the policyholder is paid, the excess is kept by the Board.

8 Section 32 of the Act.

9 In *Ackman and Scher v Policyholders Protection Board (No 2)*[1994] 2 AC 57, the House of Lords held that "a person who is not the legal holder of the policy may, nevertheless, be a policyholder if a sum is due to him under the policy before the beginning of the liquidation. A sum ... is due to him if all the preconditions to the liability of the insurance company have been satisfied even if it is not yet payable". Lord Mustill, obiter, at p 1045, raised the possibility that the term "policyholder" might apply to a claimant under the 1930 Act. See also Merkin, *Compendium of Insurance Law*, para 1.101.16. Section 16 of the Policyholders Protection Act 1997 will insert a relevant new subsection into the 1975 legislation. Section 32(2ZA) states that the term "policyholder" includes a person to whom a sum is contingently due as well as a person to whom a sum is actually due.

10 Although it could be argued that the third party's remedy should be from the reinsurer liable to indemnify the insurer in respect of the particular insurance policy rather than from the fund administered by the Policyholders Protection Board, to which reinsurers do not contribute.

11 See paras 2.13-2.17 above.

12 Where reinsurance is not specifically earmarked but covers a range of policies in the underwriter's whole account, it may be inappropriate for a particular third party to have priority over others who may be entitled to reinsurance funds under different policies. See Sir Jonathan Mance "Insolvency at Sea" [1995] LMCLQ 34, at 51.

11.7 It may be easier to trace a path of liability to a reinsurer where the contract between insurer and reinsurer contains a "cut-through clause". In such clauses, the insurer and reinsurer contract to allow the insured to claim against the reinsurer directly on the insolvency of the insurer. There is a clear link between the reinsurance policy and a specific risk.[14] However, the validity of such clauses in English law may be doubtful.[15]

11.8 Other problems are the different rules of interpretation which may be applied to insurance and reinsurance contracts[16] and the different market practice of insurers and reinsurers. Insurers are likely to be dealing with inexperienced insureds and have different duties towards them than will reinsurers dealing with insurers. A third party claiming under the 1930 Act pursuing a reinsurer might find that he had to raise certain arguments against the insurer, then different arguments against the reinsurer. The reinsurance contract, like the insurance contract, is likely to lay down a number of preconditions (requiring, for example, notification of claims, claims co-operation or control or arbitration of the dispute) which must be met before the liability of the reinsurer arises.[17] Our provisional view is that the Act should not be extended to reinsurance policies.

Do consultees agree with our provisional conclusion that the Act should not be extended to reinsurance policies? If they do not, to what types of reinsurance policy should the Act apply?

SHOULD THE ACT CONTINUE TO APPLY TO ALL LIABILITY INSURANCE POLICIES?

11.9 The Act currently applies to all liability insurance policies. Relatively few cases involving the 1930 Act reach the court, however, and it could not be argued that the applicability of the Act to all liability policies has opened the floodgates of

[13] There may also be debate as to whether a particular type of cover is provided as insurance or reinsurance. See the comments of Hobhouse LJ in *Toomey v Eagle Star* [1994] 1 Lloyd's Rep 516, 518 and Sir Jonathan Mance, "Insolvency at Sea" [1995] LMCLQ 35, at 51.

[14] See Sir Jonathan Mance, "Insolvency at Sea" [1995] LMCLQ 35, at 51, on the scope of the Act: "There seems to me a case for extending its operation to specific facultative reinsurances; one possibility could be to limit the extension to circumstances where the parties to the insurance/reinsurance arrangements have specifically agreed upon a 'cut-through' clause."

[15] See Flynn and Hanson "Cutting Through Confusion?: The Rights of Third Parties under Insurance and Reinsurance Contracts" [1997] IJIL 50 who suggest that such clauses are currently caught by the privity rule but that they might be enforceable were the Law Commission's proposals for the reform of this rule to be implemented. They also suggest that, were such clauses to be enforceable, the reinsurer should probably be treated as carrying on insurance business and be subject to the same regulatory regime as other insurers. See also C Braithwaite "Cut-through clauses" [1997] BILA Journal 22.

[16] In interpreting reinsurance contracts, the court has referred to concepts such as those applied to gentlemen's agreements. One example of this is the different approach taken towards requirements in reinsurance contracts for insurers to have "paid" to that taken towards similar requirements used in the rules of Protection and Indemnity Clubs. See para 5.62, n 78 above.

[17] The ability of insurers to rely on defences is discussed in Part 5 above.

litigation.[18] We provisionally conclude that the scope of the Act should not be limited and suggest that the number of cases under an amended Act might actually increase as parties sought to establish the meaning of any statutory definitions used to limit the categories of potential claimants. Some consultees may consider, however, that the scope of the Act should be limited.[19]

The purpose of liability insurance

11.10 Consultees' views on what the scope of the Act should be are likely to vary according to whether or not they see liability insurance as purely a contractual arrangement protecting the interests of the insured. In some jurisdictions, the law looks beyond the insurance contract and views the main aim of liability insurance as being the protection of those to whom the insured is liable.[20] It could be argued that, as the insurance fund has come into existence because of the insured's wrongful act, the third party should have access to that earmarked fund.[21] Even where the third party is not a victim of a tort or delict committed by an unknown insured but has chosen to contract with the insured, the insurance fund exists because of the foreseen event giving rise to the liability of the insured to the third party. The third party may have chosen to deal with the insured because he was insured.

11.11 Consultees may believe that the interests of third parties should be protected, but only in certain circumstances. They may take the view, for example, that a third party should have rights under the Act when he has suffered personal injury, but not when his claim is for financial loss suffered as a result of the insured's breach of contract, in which case the insured's other creditors should be preferred.

Compulsory insurance

11.12 The view could be taken that third parties' rights should be protected if they have suffered as a result of activities which Parliament has decided should be subject to a regime of compulsory insurance.[22] Some might also argue that the 1930 Act was

[18] We have suggested that the Act currently promotes settlement between insurers and third parties. See para 1.18 above. We appreciate, however, that more cases might be brought were some of our other provisional recommendations weakening the position of insurers to be introduced in an amended Act. See our proposals to extend the duty of disclosure and to limit the ability of insurers to rely on defences against third parties in Parts 13 and 14.

[19] See, for example, the outline provisions of an amended 1930 Act drafted by the City of London Law Society Insurance Sub-Committee which would limit the scope of an amended Act to compulsory liability insurance. The draft provisions are set out at Appendix E.

[20] See, for example, the Louisiana Direct Action Statute, which provides that "all liability policies ... are executed for the benefit of all injured persons ... to whom the insured is liable" and see para 1.10 above and para 1.24 of Appendix F.

[21] See para 1.11, n 25 above. This was the view of the Attorney General in 1929 when the Act was before Parliament.

[22] See the approach taken by the City of London Law Society Insurance Sub-Committee, referred to at n 19 above. See also *Compulsory Insurance in OECD Countries*, a report prepared by the Insurance Committee of the Directorate for Financial, Fiscal and Enterprise Affairs of the Organisation for Economic Co-operation and Development, May 1996, which reviewed compulsory insurance across OECD countries as a guide to countries in Central and Eastern Europe. The report comments as follows on the purposes

intended to deal mainly with compulsory insurance type situations and should only do this now.[23]

11.13 Compulsory insurance may be criticised as a basis for a system of third party rights, however, as it is often introduced as a reaction to a particular incident and provides a haphazard scheme of protection.[24] In many cases, the insurance market reacts quickly to demand, covering activities long before consideration has been given to whether or not there should be compulsory insurance.

11.14 Consideration needs to be given to whether third parties should only have rights in respect of activities expressly required by Parliament to be subject to compulsory insurance,[25] or whether they should also have rights where, for example, the insured is a member of a trade or professional body which requires its members to carry insurance.[26] In some cases, legislation will require such bodies to make

for compulsory insurance (although it concludes that systems are arbitrary): "The major compulsory insurances, which are also the most widespread, have given rise to much explanatory comment on the reasons why such cover has to be compulsory. This is especially true in the case of third party motor vehicle insurance - the number of road traffic accidents and the severity of the injuries that may result make it imperative to protect victims by ensuring, through compulsory insurance, that they will be indemnified. Compulsory insurance also protects the negligent party against the risk to assets to which such party may be exposed ... In general compulsory personal insurance or compulsory liability insurance is intended, even where this is not explicitly stated, to protect victims against the risk of accidents that are especially frequent or serious, and (in the case of liability insurance) to protect the assets of the negligent party. The priority given to protection of victims is sometimes evident from the measures designed to address it, such as provision for direct proceedings by the victim against the insurer, accompanied by a procedure whereby exclusions the insurers may apply to the insured are void against the victim (such direct proceedings form part of third party motor vehicle cover in most of the countries considered except the United Kingdom)".

[23] See paras 2.4-2.5 above.

[24] It is not within the scope of this Paper to suggest when compulsory insurance should be in place but to consider whether it would be appropriate to limit third party rights under the 1930 Act to activities which are so covered. The OECD Report, referred to at n 22 above, states: "It is noteworthy that in no country does the provision of compulsory insurance seem to be the outcome of consistent legislative policy. Laws are adopted in response to social or political pressure, seemingly provoked by events that have caught public attention, which may explain the considerable differences in date sometimes found in laws introducing compulsory insurance in different countries ...". We note, however, the guidance given by the OECD Report on when compulsory insurance should be introduced: "compulsory insurance should only be provided if deemed indispensable on the basis of the following criteria ... whenever a grave risk is involved, one that is sufficiently widespread to represent a major social problem. Insurance against third party risks entailed by the use of motor vehicles and occupational accidents are the most evident examples ... where the risk involved is very serious even though less widespread. This criterion applies to shooting game and to accident cover for motor racing ... when the law increases the extent of liability, since without compulsion such provisions would be unenforceable".

[25] Whether directly or by making insurance a condition of a compulsory licence requirement eg the Road Traffic Act 1988, the Nuclear Installations Act 1965, the Employers' Liability (Compulsory Insurance) Act 1969, the Riding Establishments Act 1964, the Dangerous Wild Animals Act 1976.

[26] Some might argue that where insurance is voluntary, its aim should be seen as protecting the insured and his business, not third parties. In some cases, Parliament may have required persons to be members of such bodies before they could take part in a certain activity, in

arrangements for insurance cover;[27] in others, it will provide that they may do so.[28] To avoid uncertainty as to whether or not a particular scheme came within the ambit of an amended Act, the Act could contain a schedule of such schemes, which could be amended as necessary by statutory instrument.[29]

Claims involving death or personal injury

11.15 Another view might be that there are good public policy reasons for restricting third party rights under the Act to cases where they have suffered death or personal injury. Some statutes already provide rights only to those who have suffered in this way.[30] In some cases, the insured may have caused the third party personal injury and property damage. Should the third party only have rights under the Act in respect of some of his loss and be required to proceed as a creditor in the main insolvency to recover the rest of his loss? It could be argued that there has been a move away from distinguishing personal injury claims from other claims and that the problems caused to victims by damage to their property or by financial hardship should also be recognised. For example, road traffic legislation has been amended to allow third parties to recover from insurers sums due to them in respect of property damage.[31]

11.16 In many cases, third parties pursuing claims for personal injury or death will already have alternative remedies which are not available to other claimants. They may be able to rely, for example, on the Road Traffic Act 1988 or on rights under

which case the compulsory insurance could be said to have been indirectly required by Parliament.

27 Eg the Solicitors Act 1974, the Solicitors (Scotland) Act 1980, the Credit Unions Act 1979, the Estate Agents Act 1979 (in respect of client money).

28 Eg the Insurance Brokers (Registration) Act 1977. The possibility of increased regulation of insurance brokers is referred to at Part 6 above.

29 Section 6 of the Policyholders Protection Act 1975, which provides a full indemnity in the case of a policy of compulsory liability insurance and a 90% indemnity in other cases, lists statutory provisions requiring compulsory insurance cover.

30 Some statutes deliberately limit rights to compensation to situations involving death or personal injury or provide increased rights to those (or the representatives of those) who have suffered death or personal injury. For example, s 2 of the Maritime Conventions Act 1911 provides that the liability of shipowners for collisions at sea in respect of damage to property is several whereas, in respect of death or personal injury, it is joint and several. Section 11 of the Animals Act 1971 and s 1 of the Animals (Scotland) Act 1987 make the keeper of any animal causing death or personal injury strictly liable for that damage. This is not the case in respect of any other damage done by the animal.

31 Section 145 of the Road Traffic Act 1988 requires the users of motor vehicles to be insured against liability for the death of or injury to third parties and for £250,000 for property damage. The provision relating to property damage is additional to the requirements of EC Council Directive 84/5 which covers only personal injury and death. See also s 13 of the Sea Fisheries Act 1968 which provides that if a person is convicted of an offence under that Act and it appears to the court that personal injury or damage to property has been caused by the offence, the court may order the offender to pay compensation to the person suffering injury or damage.

social security legislation. Also, they may benefit from more lenient insurance practices.[32]

Consumer, as opposed to commercial, claims or claims by an individual

11.17 A distinction which has been used in some legislation is that between consumer and non consumer claims, or claims brought by an individual claimant.[33] The rationale for such a distinction is that consumers are in a weaker bargaining position and should be treated more leniently than those with commercial claims. In the case of claimants under the 1930 Act, it could be argued that those with a commercial claim against the insured should be treated in the same way as any other commercial creditor and be entitled to a dividend out of the estate. The fairness of such distinctions is disputed, however; it has been suggested, for example, that owners of small businesses may be in equal need of protection as consumers.[34]

11.18 In the insurance context, definitions based on the capacity in which a claimant dealt with a defendant may be less appropriate, particularly where third party claims are concerned. The claimant is statistically more likely[35] to have a claim in tort or delict against the insured and not to have chosen to deal with him as a consumer does, for example, when he purchases something in a shop. Insurance regulation has sought to distinguish individual policyholders. The Policyholder's Protection Act 1975 does not distinguish between consumers and non consumers as such, but uses the term "private policyholders".[36] Similarly, the jurisdiction of the Insurance Ombudsman Bureau ("the IOB") is limited to policies "taken out by or on behalf of or for an individual".[37] The Insurance Ombudsman has suggested that the IOB's jurisdiction should be extended to small commercial

[32] See, for example, our discussion at para 5.62 of the practice of P&I Clubs not to rely, as against personal injury claimants, on pay to be paid clauses.

[33] See, for example, the Consumer Protection Act 1987, the Unfair Contract Terms Act 1977 (which does not apply to insurance contracts) and the Unfair Terms in Consumer Contracts Regulations 1994.

[34] See Law Commission Report on Non-disclosure and Breach of Warranty, para 4.42: "it seems to us that any separate regime for consumers and non-consumers would lead to anomalous results in practice. This can again be illustrated by a shopkeeper who lives above his shop. He applies for fire and burglary cover in respect of both his shop and his flat at the same time: the former application would be made in the course of a business, but the latter would not. It would be odd, to say the least, if the resulting contracts were subject to different vitiating factors. We are persuaded by all these cumulative considerations that there should be no special category of consumer insurance to which more lenient rules should apply". The jurisdiction of the Banking Ombudsman was extended in 1993 to cover "small" companies, defined as companies with an annual turnover of less than £1 million. The Australian Insurance Contracts Act 1984 removed the distinction between consumer and commercial insurance and the protection provided by the Act applies to all types of insurance, except marine, reinsurance and statutory health insurance.

[35] See para 2.10 above where we discuss the types of claim typically brought under the 1930 Act.

[36] Section 6(7) of the Policyholders Protection Act 1975 defines a private policyholder as one who is either an individual or a partnership or other unincorporated body of persons all of whom are individuals ie those who do not have limited liability.

[37] Insurance Ombudsman Terms of Reference, January 1996.

claims. The ABI Code of Insurance Practice applies to "policyholders resident in the UK and insured in their private capacity only".

Tortious or delictual, as opposed to contractual claims.[38]

11.19 Most claims under the 1930 Act are based on tort or delict rather than contract.[39] Some cases may, however, be based on a third party's contractual rights against the insured and it might be argued that the protection of the Act should not extend to those who have chosen to deal with the insured.[40] It could also be argued, however, that the insurance fund relates to the particular liability incurred by the insured to the third party and that third parties should not be deprived of the Act's protection in such cases. Should third parties be deprived of protection if they chose to deal with the insured because he was insured? Third parties may, for example, choose to deal with a particular travel agency because it is bonded.[41]

11.20 One of the problems of using a distinction between claims in tort or delict and contract is that some claims may be based in both. For example, an injured employee may have a claim against his employer under his employment contract as well as in tort or delict and a person in receipt of negligent professional advice may also have claims against his adviser in contract and tort or delict.[42] Another problem which may arise from distinguishing between contractual and other causes of action is that one policy may cover all causes of action. Complexities would arise as a result of endeavouring to distinguish between them in applying the 1930 Act. Our provisional view is that not only would it be unjust[43] to make such a distinction but that the complexities that would arise from it militate against any such distinction.

Consultees' views are sought on our provisional conclusion that the Act should continue to apply to all liability insurance policies, regardless of the nature of the third party claimant or of his claim.

If consultees disagree, they are asked to specify how the applicability of the Act should be restricted.

[38] The text under this heading does not apply to claims for breach of contract where the insurance expressly covers only the parties to the transaction from which the damage arose.

[39] See para 2.10 above.

[40] See also paras 11.17-11.18 above.

[41] It has been suggested that the Act does not apply, in any event, to legal expenses insurance as such insurance is classed under the Insurance Companies Act 1982 as a contract of first party pecuniary loss insurance rather than as liability insurance and as the failure of the insured to pay his legal adviser is distinguishable from other breaches of contract and from other events leading to the incurring of liability. See N Stanbury "Legal Expenses Insurance: beware of insolvent insureds" [1996] 92 BILA Journal 26.

[42] In the Lloyd's litigation, the claims brought by Names were in contract and tort. In some cases, third parties may not have rights against insurers in respect of contract claims in any event, as the liability insurance policy may exclude contractual liability. See M Clarke *The Law of Insurance Contracts* (3rd ed 1997) p 414.

[43] For the reasons in para 11.19.

PART 12
THIRD PARTY RIGHTS UNDER AN AMENDED ACT

12.1 The rights which are transferred to third parties under the current Act are the insured's "rights against the insurer under the contract in respect of the liability",[1] which include the insured's right to an indemnity from the insurer. As we have seen, the Court of Appeal held, in *Post Office v Norwich Union Fire Insurance Society Ltd*,[2] that, as the insured's right to an indemnity does not arise until his liability has been established, this right does not transfer to the third party until then.[3] Nor, as a result of judicial construction of section 2, does the duty to disclose policy information under that section arise until the liability of the insured has been established.[4] In Scotland, a third party can obtain information for the purpose of his action against the insurer for a declarator.[5]

12.2 We suggest in this Part that a third party's rights against an insurer under an amended Act should not be dependant on his first establishing the liability of the insured, but should arise once two events have occurred: the incident giving rise to the liability of the insured and the happening of one of the insolvency events set out in the Act.[6] We consider what rights the third party should acquire once these two events have occurred.[7] He would continue to have, as under the current Act,

1 Section 1 of the Act. See paras 4.2 and 5.4 above. As we have seen, however, s 1(3) of the Act invalidates terms in the insurance contract which seek to make the liability of the insurer conditional on the solvency of the insured and s 3 of the Act prohibits agreements between the insurer and the insured reached after the happening of one of the insolvency events set out in the Act and purporting to alter the rights transferred to the third party. See paras 5.8-5.9 above. We have also considered other restrictions on the ability of insurers to rely on certain policy conditions imposed by the Employers' Liability (Compulsory Insurance) General Regulations 1971 and by insurers' codes of practice. See paras 5.10-5.13 above.

2 [1967] 2 QB 363.

3 See para 4.5 above. It was suggested in the *Post Office* case that the insured may have an earlier contractual right to sue the insurer for a declaration if, for example, the policy has been repudiated, but this was rejected in *Nigel Upchurch Associates v Aldridge Estates Investment Co Ltd* [1993] 1 Lloyd's Rep 535. See para 4.13 above. Third parties have a procedural right to seek a declarator against an insurer under Scottish law, but it is unclear whether they have a similar right under English procedural rules. See paras 4.21-4.29 above.

4 See para 4.10-4.12 above. Reform of the Act's disclosure provisions is the reform most commonly urged by commentators and is discussed in Part 13 below. We suggest in para 12.6 below that the duty to disclose policy information should not be dependant on the third party first establishing the liability of the insured. We provisionally recommend that the duty should arise following one of the insolvency events set out in the Act and within 14 days of the disclosing party becoming aware of the third party's claim.

5 See para 4.18 above.

6 See para 12.10 below.

7 See para 12.33 below.

the insured's right to be indemnified by the insurer.[8] We suggest that the third party should also have a right to seek a declaration or declarator that, on the liability of the insured being established, the insurer will be liable to indemnify the third party.[9] This would mean that the liability of the insured and of the insurer would be dealt with in one set of proceedings.

12.3 We consider below the nature of third party rights against insurers in other jurisdictions and seek consultees' views on what the nature of the third party's rights should be under an amended Act.[10] We consider whether the third party's right of action against the insurer should be subject to a leave requirement.[11] Also in this Part, we seek consultees' views on whether third parties should be able to set aside settlements reached between the insurer and the insured prior to the happening of one of the insolvency events set out in the Act,[12] on whether the insurer should be required to pay insurance monies due to the third party directly to him[13] and on whether third parties should have rights against the insurers of disappeared insureds.[14]

12.4 First, we consider the implications of the liability of the insured and of the insurer being resolved in the same proceedings[15] and consider whether both insurer and insured should be parties to the third party's action.[16]

SHOULD THE THIRD PARTY'S RIGHTS AGAINST THE INSURER ARISE ONLY ONCE HE HAS ESTABLISHED THE LIABILITY OF THE INSURED?

12.5 As under the current Act, there would be a transfer to the third party of the insured's rights against the insurer. The issue which needs to be addressed is whether or not the liability of the insured should continue to be established in separate proceedings between the third party and the insured or in proceedings involving and binding on the insurer. In many cases, the insurer will conduct the defence of the insured in any event, but some might argue that the insurer should not be forced to be a party in proceedings to establish the liability of the insured as this is an issue between the third party and the insured alone.

[8] The right would, as with the insured, be subject to establishment of the liability of the insured and to compliance with policy terms (subject to any reforms such as those canvassed in Part 14 below).

[9] The insurer would defend these proceedings if he was able to rely on policy or other defences. As we have already discussed, it is uncertain whether or not the third party may already be able to seek such a declaration under English law. He may do so under Scottish law. See para 4.19, n 36 above.

[10] See paras 12.24-12.33 below.

[11] See paras 12.35-12.44 below.

[12] See paras 12.45-12.47 below.

[13] See para 12.48 below.

[14] See para 12.49 below.

[15] See paras 12.11-12.13 below.

[16] See paras 12.14-12.24 below.

12.6 In Parts 4 and 5, we discussed some of the problems arising from the requirement that the third party establish the liability of the insured before acquiring a right of action under the Act, including the fact that parties may have to bear the expense of two or more sets of proceedings.[17] Having considered these problems, we take the provisional view that the third party's right to sue the insurer should arise before he has established the liability of the insured. In our view, the third party should be able to establish the liability of both the insured and the insurer in the same proceedings.[18]

SHOULD THE THIRD PARTY'S RIGHTS ONLY ARISE ON THE HAPPENING OF ONE OF THE INSOLVENCY EVENTS SET OUT IN THE ACT?

Should third parties have rights against insurers, regardless of the solvency of the insured?

12.7 In some jurisdictions, third parties are given rights against insurers referable to the date of the incident giving rise to the liability of the insured, regardless of his solvency.[19] Our provisional view is that a third party's rights should initially be against a solvent wrongdoer, rather than against his insurer.[20] Although the insured will often seek an indemnity from his insurer, he may prefer to pay the claim himself to avoid a rise in his insurance premiums. Were third parties to have a right against insurers whether or not the insured had been declared bankrupt or wound up, there might also be a rise in the number of speculative actions and insurers might need to reassess their claims handling procedures and policy premiums, causing disruption to the insurance market.

12.8 Where the insured is insolvent, the third party may be likely to recover little or nothing from the insured. In such cases, it is more important, therefore, to safeguard the interests of the third party.[21] The aim of the 1930 Act was to provide a remedy to third parties of which they had been deprived by the insured's insolvency[22] and our provisional view is that the original scheme of the Act should be respected.

[17] See paras 4.31-4.35 above.

[18] We discuss at paras 12.14-12.24 below whether the insurer and the insured should both be parties to the third party's action.

[19] See, for example, our discussion of third party rights against insurers in France, Belgium and Louisiana in Appendix F.

[20] Legislation introduced in New Zealand, New South Wales and the Australian Capital Territory provides third parties with a right of direct action against insurers, but the right is subject to a leave requirement unless the insured is insolvent. It appears that leave will not be granted if the third party could proceed instead against the insured. See para 1.12 of Appendix F.

[21] At paras 1.15 and 11.1 we raised the issue of the extent to which the interest of other creditors of the insured should be safeguarded. In Part 11 we sought consultees' views on whether only certain types of claim should be pursued under the Act.

[22] As we noted at para 1.2 above, the long title of the Act states that its aim is "to confer on third parties rights against insurers of third-party risks in the event of the insured becoming insolvent, and in certain other events".

Should third parties have rights against insurers when the insured is in financial difficulties, but before the happening of one of the insolvency events set out in the Act?

12.9 We do not take the view that the third party should acquire rights under the Act when the insured is in financial difficulties prior to the happening of one of the insolvency situations set out in the Act.[23] The concept of apparent insolvency in the Bankruptcy (Scotland) Act 1985[24] and definitions in the Insolvency Act 1986[25] are used to provide a basis for a petition for an award of sequestration or an application for a bankruptcy or winding up order. They do not themselves trigger the transfer of rights to creditors. Creditors' rights are affected by the award or order and their position in any insolvency is set out in primary and subordinate legislation.[26] Providing for the provisions of the 1930 Act to be triggered before the occurrence of an event specified in the Act could create uncertainty and undermine the insolvency legislation. Our provisional view is that the third party's rights should continue to be conditional on the happening of one of the insolvency events set out in the Act. His rights would arise, therefore, once two events had occurred: the incident giving rise to the liability of the insured and one of the insolvency events set out in the Act.

12.10 Sections 1 and 2 of the Act use the term "becoming bankrupt", a term not used in Scottish law, which risks being confused with apparent insolvency.[27] We suggest that, in its application to Scotland, the amended Act should instead use the phrase "person's estates being sequestrated."

Do consultees agree that a third party's rights under an amended Act should arise once two events have occurred: the incident giving rise to the liability of the insured and one of the insolvency events set out in the Act?[28]

If consultees consider that the third party's rights should arise before or after this point, when do they think they should arise? For example, should they arise:-

(i) after close of pleadings in the proceedings brought by the third party against an insured who has been declared bankrupt or wound up;[29]

[23] Although it should be noted that s 1(1)(a) provides that the Act applies to situations where the insured makes a "composition or arrangement" with his creditors. We suggested in Part 5 that the insured may be increasingly likely to breach policy conditions during this period.

[24] Section 7.

[25] For example, s 123 of the Insolvency Act defines when a company is deemed unable to pay its debts and may be wound up by the court eg if a statutory demand has not been met (s 123(1)(a)); if it is proved to the satisfaction of the court that the company is unable to pay its debts as they fall due (s 123(1)(e), or if it is proved to the satisfaction of the court that the value of the company's assets is less than the amount of its liabilities (s 123(2)).

[26] See the Bankruptcy (Scotland) Act, the Insolvency Act and the Insolvency Rules.

[27] Which was formerly known as notour bankruptcy.

[28] We discuss at paras 14.15-14.18 below whether insurers should be prevented from relying on certain defences arising after a certain point in time, whether before or after the relevant insolvency situation.

(ii) on the happening of the event giving rise to the liability of the insured, regardless of the solvency or otherwise of the insured; or

(iii) when an insured who has incurred liability to the third party is in financial difficulties prior to the happening of one of the insolvency events set out in the Act? Consultees who favour this option are requested to suggest a trigger for the third party's rights.

Do consultees agree that, in its application to Scotland, the amended Act should use the phrase "person's estates being sequestrated" instead of "becoming bankrupt"?

THE IMPLICATIONS OF THE LIABILITY OF INSURER AND INSURED BEING RESOLVED IN THE SAME PROCEEDINGS

The early identification of issues in dispute

12.11 The number of preliminary issues which might need to be dealt with by the court may vary greatly, depending, for example, on whether the insurer is conducting the defence of the insured, on whether disclosure has been voluntarily made and on whether the insurer is disputing cover.[30] There could be costs[31] and time advantages to issues between the parties being resolved in the same proceedings.[32] The effect of such a reform might be that costs were incurred earlier on in the proceedings than would otherwise be the case. A more open approach to the

[29] Ie not until the issues in the underlying claim have been made apparent. We discuss the rules on the joinder of parties at paras 12.22-12.23 below. Under Rule 24.2 of the Draft Civil Proceedings Rules the court would allocate the third party's case to a particular track following the filing of the defence. One of the matters relevant to the allocation of a track would be the number of parties or likely parties. It would be convenient if at that stage the court were aware of the identity of the parties to the action.

[30] See our discussion at paras 12.34-12.40 of issues which might be discussed at any leave hearing and of the ability of the court to direct that issues be heard in an appropriate order. Some of these issues may already be dealt with separately under the existing law. The Woolf Report, ch 5, para 14 suggests that "the identification and rolling disposal of the issues is a key element in the reforms". Cf Lord Scarman's reference to the resolution of legal issues without findings of fact under RSC O 33 in *Tilling v Whiteman* [1980] AC 1 as a "too often treacherous short-cut". As we have already seen, Scottish law may already allow the liability of the insured and the insurer to be determined in the same proceedings and allow pre-action disclosure to third party claimants. See para 4.18 above.

[31] Costs savings might also result were third parties not required to restore dissolved companies to the register. The costs problems faced by third parties are discussed at paras 4.31-4.35 above.

[32] In the debate of the Bill in Standing Committee, the Attorney General appears to have contemplated the liability of the insured and of the insurer being dealt with in the same proceedings: "It will be perfectly easy to provide that, if a defendant against whom an action has been started goes bankrupt, you can carry on the action by adding the insurance company instead of, or in addition to, that defendant. I certainly contemplate, and I hope, that rules will be made in which there will be the widest latitude given in order that at one and the same time you might shoot your arrow both at the insurance company and at the wrong-doer, if it is material any longer to consider the claim against the wrong-doer". Hansard (HC) 28 November - 5 December 1929, cols 45-116. See para 1.11, n 25.

resolution of disputes between all relevant parties is in line with the recent "cards on the table" approach to litigation[33] and may encourage settlement.

Possibility of prejudice to the insured or the insurer

12.12 If the insurer has to contest cover in proceedings in which the liability of the insured is also being tried, the defence of the insured (which will often be conducted by the insurer) might be prejudiced. Prejudice might be caused, for example, if a third party suing for injuries suffered in a night club fire alleged that the insured owner of the premises failed to exercise due care in providing safe premises. The insurer might be seeking to repudiate cover on the basis that the owner had failed to disclose, when seeking insurance cover, that he had had three previous night clubs which had burnt down. Were the third party to know of the reason for the insurer denying cover, the insured's defence might be prejudiced. It is not unusual, however, for those defending civil actions to plead conflicting arguments and it is also possible that the court's power to determine the order in which issues are tried could be used to balance the interests of the parties and to achieve the fairest trial possible.[34]

12.13 Allowing the liability of the insured and of the insurer to be resolved in the same proceedings may also avoid some of the problems faced by insurers who are concerned that the insured's defence will not be adequately argued in proceedings between the third party and the insured which are not conducted by the insurer. As we have seen, however, insurers may be concerned, in some cases, that if they defend proceedings brought by a third party against the insured, they will waive their right to claim that they are not liable under the insurance contract.[35] In our view, insurers should not risk waiving their rights in this way.

Consultees' views are sought on our provisional conclusion that insurers conducting the defence of their insured under the Act should be able to do so without prejudice to their right to repudiate their liability to the insured under the insurance contract.

SHOULD THE THIRD PARTY PROCEED AGAINST BOTH INSURER AND INSURED?[36]

12.14 Having considered the advantages and disadvantages of the liability of the insurer and the insured being resolved in the same proceedings, we now consider whether the insured should be a party to those proceedings. We consider first whether there

[33] Including, for example, developments in the use of witness statements, interrogatories and skeleton arguments. See para 10.11 above.

[34] The powers of the court to order preliminary issues to be tried first (RSC O 33, r 3, CCR O 13, r 2(2)(c) and the Draft Civil Proceedings Rules, rule 1.3(e)) and to order split trials (RSC O 15, r 5 and CCR O 5, r 3) are set out in Appendix B. We discuss at paras 13.9-13.10 below the possibility that the interests of the insurer or of the insured might be prejudiced were the duty to disclose policy information under the Act to extend to the grounds for repudiation.

[35] See the discussion of *Wood v Perfection Travel* [1996] LRLR 233 at paras 4.25-4.26 above.

[36] We consider the jurisdictional implications of third parties having a right to join the insurer into proceedings against the insured or to proceed against the insurer alone in Parts 8 and 16.

could be advantages for the third party, the insured or the insurer were the insured to be a party or whether the liability of the insured is an issue which could be resolved in proceedings between the third party and the insurer alone. Next, we consider whether current procedural rules would allow the insured to be joined to such proceedings in appropriate cases.

Advantages and disadvantages of the liability of insurer and insured being resolved in the same proceedings and of both insurer and insured being party to the third party's action[37]

Evidence

12.15 Although in many cases there may be little information which the insured[38] is willing or able to disclose, he may have some information relevant to the issue of liability to the third party. Whatever amendments are made to the rules on disclosure,[39] parties will continue to have better rights against other parties than against non-parties. There may, therefore, be evidential advantages for both the third party and the insurer if the insured is a party to the proceedings.

Binding the insured

12.16 In some cases, it may be in the interests of the third party, the insurer and the insured that the insured is a party to the third party's action and can take part in the proceedings and be bound by the court's judgment.[40] A third party who does not recover the totality of his claim from the insurer has a right of recourse against the insured under the Act[41] and could seek that remedy in the same proceedings. We suggest below that, should an insurer be deprived of certain contractual rights against the third party which he would have had against the insured, he might be able to seek an indemnity from the insured. Were this to be the case, it may also be in the interests of the insurer for the insured to be a party to the action.[42]

12.17 The insured himself may also have an interest in being a party to the action if any allegations or findings are made against him which might have implications beyond

[37] See also paras 12.12-12.13 above. Some of these advantages have been recognised in other jurisdictions which give third parties a right of direct action but require them to join the insured into those proceedings in certain circumstances. In France and Belgium, third parties have a right to proceed directly against insurers but usually proceed against both insurer and insured. See paras 1.29 and 1.32 of Appendix F.

[38] Or the officeholder.

[39] See our discussion of recommendations in the Woolf Report at paras 6.19-6.20 and 10.9-10.11 above.

[40] The insurer will usually have a contractual right to conduct the insurer's defence, but may not in all cases. See also para 12.18 below.

[41] Section 1(4)(b) of the Act provides: "if the liability of the insurer to the insured is less than the liability of the insured to the third party, nothing in this Act shall affect the rights of the third party against the insured in respect of the balance". It is possible that the insolvency practitioner or the third party may discover in the course of proceedings that the insured has more assets than was originally thought and is worth pursuing.

[42] So that the insured is bound by the findings in the case, although we doubt whether such a right would be of much use to insurers in practice. See para 14.42 below.

the immediate proceedings[43] or if he may be entitled to claim from the insurer any sums in excess of those payable to the third party.[44]

12.18 In many cases under the 1930 Act, however, the insured (or his insolvency practitioner) is likely to play little part in the proceedings. The insured will be the nominal defendant or defender but his interests will be represented by his insurer who will have the right to conduct the insured's defence under the insurance contract. Requiring the third party to proceed against the insured may involve all parties in unnecessary costs.[45]

12.19 We query, in particular, whether third parties should be required to restore a dissolved company to the register so that the company can be a party to proceedings under an amended Act.[46]

12.20 Were a third party to have a right to proceed against the insurer alone, we suggest that the third party should be able to proceed against the insured as well and that a third party who had already started proceedings against the insured when he acquired rights under the Act might wish to join the insurer into those proceedings,[47] rather than to apply for the insurer to be substituted in them.

12.21 We also suggest that the insurer should be able to apply to join the insured and that the insured should be able to intervene in the proceedings started by the third party.[48] Before seeking consultees' views on whether the third party's right of action should be against the insurer alone or against the insurer and the insured, we consider briefly the procedural rules on joinder and substitution as they might apply to an amended Act.[49]

[43] For example, an employer found liable to an employee in negligence may also be guilty of a criminal offence under common law or under health and safety legislation. The insured may also have an interest in monitoring how his defence is being conducted by the insurer. In *Cox v Bankside* [1995] 2 Lloyd's Rep 437, the court held that the insurers had an obligation to conduct the defence of claims in good faith and in a way which would not cause prejudice to the insured.

[44] Section 1(4)(a) of the Act. This is rarely likely to be the case.

[45] The third party will also have to apply for leave to proceed against an insolvent defendant under English law: ss 130(2) and 285 of the Insolvency Act 1986, although leave will almost invariably be granted. In Scotland, third parties do not need leave before proceeding against insolvent defendants.

[46] Although it is possible that evidence could still be obtained from directors or employees of the company. We set out our provisional conclusion at para 12.23 below that third parties should be able to proceed directly against the insurer if the insured is a dissolved company which has been struck off the register.

[47] RSC O 15, rule 6(2) set out in Appendix B. Alternatively, he might wish to start an action against the insurer under the Act and to consolidate that action with his action against the insured. RSC O 4, r 9 (O 13, r 9 CCR) also set out in Appendix B.

[48] In Belgium, the insurer and the insured can apply by a "requete en intervention volontaire" for a court order that the insured be joined to the third party's action.

[49] See also paras 4.21-4.30 above and Appendix B, where we set out relevant Rules of the Supreme Court, County Court Rules, Court of Session Rules and Draft Civil Proceedings Rules.

JOINDER AND SUBSTITUTION

12.22 We discussed above[50] the interests which the third party, the insured or the insurer may wish to safeguard by ensuring that the insured is a party to proceedings under the Act. To avoid multiplicity of proceedings, RSC Orders 15 and 16 give the court a discretion to order the joinder or substitution of parties. Among the criteria which the court will consider is whether joinder is necessary to ensure that "all matters in dispute may be effectually and completely determined and adjudicated upon."[51] So, for example, if the insured had evidence relevant to the case which, in breach of the policy terms, he refused to hand to his insurer the latter might seek to join him to the proceedings.[52]

12.23 The court would probably make an order for joinder if the third party or the insurer had a right of recourse against the insured in respect of payments he might be required to make to the third party[53] or if the insured was entitled to any sums under the insurance contract which were not payable to the third party[54] or would be adversely affected by a finding of liability against him.[55] We suggest, however, that current procedural rules would not necessarily allow joinder in all the circumstances in which joinder might be sought under an amended Act. We seek consultees' views on whether an amended Act should provide expressly for the joinder of the insured were the third party not required by the Act to proceed against the insured as well as the insurer.

1. We have reached the provisional conclusion that the insured[56] and the insurer[57] should be parties to the third party's action unless the insured is a dissolved company which has been struck off the Register of

[50] See paras 12.12-12.21 above.

[51] RSC O 15, r 6(2)(b). Rule 24.1(2)(d) of the Rules of the Scottish Court of Session provides that insurers can apply to become (or be sisted as) parties to the proceedings in respect of any interest they have. The court might order a party to be joined even if there is no cause of action against him but might refuse joinder if it did not consider the presence of the insured to be necessary or if joinder would have the effect of adding a new cause of action. Under rule 18.1(2)(a) of the Draft Civil Proceedings Rules the relevant test for adding parties is that the court can resolve the matters in dispute in the proceedings more effectively by adding the new party. These rules and relevant caselaw are set out in Appendix B.

[52] See also para 12.38 and n 98 below.

[53] See para 12.16 above.

[54] See s 1(4)(a) of the Act.

[55] See para 12.17 and RSC O 15, r 6(8). Were the only reason for joining the insured to be to facilitate the provision of evidence, the parties could rely instead on any right they might have to disclosure against non-parties in the case of a personal injury claim (RSC O 24, r 7A) and on the use of subpoenas (RSC O 38).

[56] (Represented by the officeholder).

[57] We discuss at paras 12.35-12.41 below whether the third party should be required to apply for leave before proceeding against the insurer.

Companies,[58] in which case the third party should have a right to proceed against the insurer alone.[59] Do consultees agree?

Consultees' views are sought on the adequacy of existing procedures under sections 651 and 653 of the Companies Act 1985 and on whether and, if so, how the existing procedures should be simplified if, contrary to our provisional view, third parties continue to be required to restore a dissolved company to the register.[60]

2. Alternatively, do consultees consider that a third party should have a right to proceed against the insurer alone:

(i) in all cases;

(ii) in other limited cases (for example, where insurance was compulsory).

3. Do consultees agree with our provisional view that, if a third party had a right to proceed against the insurer alone, he should, if he chose, be able to proceed against the insured as well and, if he had already started proceedings against the insured, be able to join the insurer into those proceedings?[61]

4. If the insured was not a party to the proceedings brought by the third party, do consultees believe that the insurer should be able to join the insured into the proceedings and that the insured should be able to intervene in those proceedings?

If so, do consultees consider that the existing rules on joinder and substitution are adequate or do they think that specific provision should be made in the amended Act?

THE NATURE OF A THIRD PARTY'S RIGHTS UNDER AN AMENDED ACT

12.24 As we have seen, the rights which are transferred to third parties under the current Act are the insured's "rights against the insurer under the contract in respect of the liability",[62] which include the insured's right to an indemnity from the insurer. We consider here the nature of third party rights against insurers in other jurisdictions and consider what the nature of a third party's rights might be under an amended 1930 Act.

[58] Or unless the liability of the insured has already been established, when the third party would not need to join the insured under an amended Act or under the current Act.

[59] If the insurer wished the insured to be joined to those proceedings, he should be entitled to apply for order for joinder and for orders restoring the company to the register.

[60] The current procedure for the restoration of companies to the register is discussed at paras 4.44-4.51 above.

[61] He would not have to apply for the insurer to be substituted in those proceedings, although he might choose to do so. See para 12.20 above.

[62] Section 1 of the Act. See paras 4.2 and 5.4 above.

Third party rights against insurers in other jurisdictions

12.25 The nature of third party rights against insurers in other jurisdictions varies.[63] Third parties may have a right to enforce their rights against the insured directly against the insurer[64] or to enforce a charge over the insurance proceeds.[65] In some jurisdictions, rights are treated as procedural; in others as substantive. Third parties may be required to proceed against both insurer and insured or may be able to proceed against the insurer alone. Whatever the nature of the third party rights are said to be, the insurer is usually able to rely on some, if not all, of the defences which he would have had against the insured, although the insurer's ability to rely on defences varies greatly.

12.26 In some jurisdictions, a third party's right to proceed against both insurer and insured has evolved through case law and has been justified by the court on the basis that the right of action is merely a procedural innovation. In Florida, for example, it has been said of a reform of the law to enable third parties to join insurers into their proceedings against the insured where previously they were not entitled to do so, that it "did not effect a change in the substantive law of this state dealing with liability of insurers. It merely innovated a procedure which permits the joinder of an insurance carrier in a suit against the insured."[66] Under this rule,

[63] It is important to stress that schemes used in other jurisdictions may operate in a very different insurance and legal context. For example, there is a state compensation scheme for accidents in New Zealand and many of the schemes which we discuss below give third parties general rights against insurers which are not dependant on the insolvency of the insured. Summaries of schemes of third party rights in other jurisdictions are set out at Appendix F.

[64] This is the case in France, Belgium and Louisiana. See also s 165(1) of the Merchant Shipping Act 1995, which confers upon the victims of oil pollution a right to bring direct proceedings against the shipowner's liability insurer, Workmen's Compensation Acts (discussed at para 2.5 above) and s 83 of the Fire Prevention (Metropolis) Act 1774. In the USA, such statutes have been held to create a separate and distinct cause of action against the insurer. See *Lumbermen's Mutual Casualty Co v Elbert*, 348 US 48 (1954). See also s 156 of the South African Insolvency Act 1936, discussed at paras 1.16-1.19 of Appendix F.

[65] As is the case in New Zealand, the Australian Capital Territory and New South Wales. Another option for reforming the 1930 Act would be to require the insured's insolvency practitioner to pay any sums received in respect of the insured's liability to a third party to that third party, in priority to the insured's other debts. The third party would still proceed against the insured then wait for the insolvency practitioner to pursue the insurer for the indemnity. See s 117 of the Australian Bankruptcy Act 1966, set out at para 1.3 of Appendix F. We query whether such an approach would have many advantages over the current Act. There would still be two or more sets of proceedings and the third party would not be in control of the litigation against the insurer.

[66] *Russell v Orange County* 237 So 2d 192 (Florida Court of Appeal, 1970). In *Shingleton v Bussey*, 223 So 2d 713 (Florida Court of Appeal, 1969), where the Supreme Court of Florida disallowed the insurer's assertion of "no joinder" clauses, the court said that, "the time has arrived when the legal reasons advanced in favour of joinder and direct action against an insurer outweigh and preponderate over the traditional notions asserted to justify precluding an injured third party from enjoying such rights". Reference was made to rule 1.210 (a), 30 Florida Rules of Civil Procedure which provides that: "any person may be made a defendant who has or claims an interest adverse to the plaintiff". It should be noted, however, that the joinder of insurers is only permissible in cases involving "liability" as opposed to "indemnity" policies. See *Metropolitan Life Insurance Co v McCarson*, 467 So 2d 277, at p 279 (Fla 1985) and *Weeks v Beryl Shipping Inc and London Steamship Owners Mutual Insurance Association Ltd. et al* (1988) 845 F2d 304. This distinction is discussed at

the insurer may not, therefore, be sued alone,[67] although the courts have the power to order separate trials[68] which they may do to determine a dispute over cover.[69]

12.27 A third party's right to a declarator against the insurer under Scottish law is also seen as a procedural, rather than a substantive right. As we have seen, it is unclear whether the English court will allow third parties to join insurers into proceedings against the insured to obtain a declaration as to the liability of the insurer.[70]

12.28 Where legislation has been introduced providing third parties with rights of direct action against insurers, views have varied as to whether the rights enforceable by third parties are procedural or substantive in nature. Section 68 of the Nigerian Insurance Decree of 1997,[71] which allows a third party to join the insurer to his action against the insured once he has given the insurer at least 30 days notice of the pending action and of his intention to bring the application,[72] has been interpreted as providing third parties with a procedural right to enforce their existing substantive rights against insurers.[73]

12.29 In South Africa, a third party has a statutory right to claim directly against the insurer of an insolvent insured and invariably proceeds against the insurer alone. His right is "to recover from the insurer the amount of the insured's liability" towards him.[74] The insurer may rely on any defence which he would have had against the insured.[75]

para 1.22 of Appendix F. See also *Beta Eta House Corp, Inc of Tallahassee v Gregory* 237 So 2d 163 (Florida Supreme Court, 1970).

67 *Kephart v Pickens*, 276 So 2d 168 (Florida Supreme Court, 1973).

68 Under rule 1.270(b).

69 In *Stecher v Pomeroy* 244 So 2d 488 (Florida Court of Appeal, 1971) the court said that: "absent a justiciable issue relating to *insurance*, such as a question of coverage or of the applicability or interpretation of the insurance policy or other such valid dispute on the matter of insurance coverage, there is no valid reason for a severance and it should not be granted".

70 See para 4.20-4.28 above.

71 Replacing s 58 of the Insurance Decree 1991 and s 11 of the Insurance (Special Provisions) Decree of 1988.

72 It appears that the court will grant the application automatically. See para 1.20, n 30 of Appendix F.

73 The effect of this provision has been described to us as follows by the Nigerian Law Reform Commission which recommended the reform: "The net effect of section 58 is that it gives the third party a legal right to join the insurers of the insured but it does not give him a direct right of action against the insurer since he has no cause of action against the insurer until he obtains judgment against the insured. The advantage of section 58 is that it makes it relatively easy to bring the insurers into the action. Once the insurers are brought into the action ... the third party, we believe, will now be free to claim against the insurers the right to have any judgment they may obtain against their insured satisfied by them".

74 Section 156 Insolvency Act 1936.

75 See para 1.18 of Appendix F. Cf the Louisiana Direct Action Statute, LA Rev Stat Ann, para 22:655(B)(1)(a)-(f)(West Supp 1993), which requires third parties to proceed against both the insurer and the insured, or against the insurer alone if the insured is insolvent or dead. The insurer can rely on some but not all of the defences which he would have had against the insured.

12.30 In New Zealand and two states in Australia,[76] third parties have a statutory right to enforce a charge over the insurance proceeds against the insurer, regardless of the solvency of the insured. The charge attaches "on the happening of the event giving rise to the claim for damages or compensation, and notwithstanding that the amount of such liability may not then have been determined."[77] It is enforceable by the third party against the insurer "in the same way ... as if the action were an action to recover damages or compensation from the insured"[78] but is subject to a leave requirement.[79] The third party may join the insurer into proceedings against the insured or proceed against the insurer alone.

12.31 Direct action schemes based on third parties enforcing the rights which they had against the insured directly against the insurer and those providing for the enforcement of a statutory charge over the insurance proceeds address the same problems in slightly different ways. Both types of scheme have raised questions as to the enforceability of defences against third parties.[80] Where schemes impose a leave requirement, questions have been raised as to the nature of that requirement and as to its effect on limitation.[81]

Third party rights under an amended 1930 Act

12.32 We have given our provisional view that the third party should acquire rights under an amended Act before he has established the liability of the insured and that his rights should accrue once two events have occurred: the incident giving rise to the liability of the insured and the happening of one of the insolvency events set out in the Act.[82] Like the insured's own right, the third party's right to an indemnity

[76] The Australian Capital Territory and New South Wales.

[77] Section 9(1) of the New Zealand legislation; s 6(1) of the New South Wales legislation; s 25(1) of the Australian Capital Territory legislation. The appropriateness of the third party's right of action being through the enforcement of a charge over the insurance fund has been questioned on the ground that the charge attaches to, as yet, unascertained property. See R D Giles "Reflections on Section 6" 7(1996) Insurance Law Journal (New South Wales), p 152. Were third party rights under an amended 1930 Act to be enforceable through a statutory charge, the charge would, we suggest, attach once two events had occurred the incident giving rise to the liability of the insured and one of the insolvency situations set out in the Act. See our provisional conclusion at para 12.10 above.

[78] Section 9(4) of the New Zealand legislation; s 6(4) of the New South Wales legislation; s 26(1) of the Australian Capital Territory legislation.

[79] In *FAI (NZ) General Insurance v Blundell* [1994] 1 NZLR, Hardie Boys J suggested that: "Until liability of insured to plaintiff, and of insurer to insured, is established, the charge remains in a sense conditional". There is no leave requirement if the insured has been declared bankrupt or wound up.

[80] In France and Belgium, there are bars on insurers relying on such defences. We discuss in Part 14 whether restrictions should be placed on the ability of insurers to rely on defences against third parties.

[81] We discuss limitation and prescription in Part 17 below.

[82] See para 12.10 above.

would be subject to the liability of the insured being established and to policy terms being satisfied.[83]

12.33 We suggest that the third party should also have a right to seek a declaration or declarator[84] that, on the liability of the insured being established, the insurer will be liable to indemnify the third party.[85] The aim of such an amendment would be to preserve the third party's existing rights under the Act, being those of the insured assigned to him,[86] and to ensure that that he also had an immediate right of action against the insurer on the happening of one of the insolvency events set out in the Act.[87]

We have reached the provisional view that once two events have occurred: the event giving rise to the liability of the insured and one of the insolvency events set out in the Act, the third party should acquire the insured's rights under the insurance policy. The third party should in addition have a right to seek a declaration or declarator that, on the liability of the insured being established, the insurer will be liable to indemnify the third party.

Do consultees agree with this provisional view? If not, what rights do they think third parties should acquire under an amended Act?

SHOULD THE THIRD PARTY'S RIGHT OF ACTION AGAINST THE INSURER BE SUBJECT TO A LEAVE REQUIREMENT?

12.34 As we have seen, in some jurisdictions, a third party's right of action against an insurer is subject to a leave requirement. We now consider whether the third party's right to proceed against the insurer under an amended Act should be automatic[88] or conditional on the third party obtaining leave from the court. We consider the advantages and disadvantages of a leave requirement, looking in particular at whether a leave requirement would prevent unnecessary actions by third parties or solve any of the problems which might stem from allowing third parties to proceed against insurers without having first established the liability of the insured. We also consider what the timing of any leave application should be, possible grounds for leave and leave procedures.

[83] Third parties may already acquire some contingent rights under the Act before they have established the liability of the insured. See para 4.18 above. We discuss in Part 14 whether restrictions should be placed on the ability of insurers to rely on defences.

[84] Third parties may already join the insurer for a declarator under Scottish law. It is not clear whether or not third parties can seek a declaration against insurers in this way under English procedural rules. See para 4.19 above.

[85] Sums might not, of course, be payable under the insurance contract if the insurer is able to rely on policy or other defences to the claim against him.

[86] Although we suggest that further restrictions should be placed on the ability of insurers to rely on defences. See Part 14 below.

[87] This appears to have been contemplated when the Act was passed. See para 12.11, n 32 above.

[88] Subject to the ability of an insurer to apply to stay the proceedings against him. See Part 5 above.

Advantages and disadvantages of a leave requirement

Is a leave requirement necessary to deter speculative actions by third parties whose case against the insured is weak or hopeless but who are pursuing the case because of the existence of insurance cover?

12.35 Insurers who conduct the defence of their insured are used to facing speculative claims and are usually well able to deal with them. The third party would still have to establish the merits of his claim that the insured was liable to him under an amended Act. Were there to be no leave requirement, the insured or the insurer could apply to strike out the claim on the ground that it disclosed no reasonable cause of action under English procedural rules.[89] Such an application might be unlikely to succeed, however, as the court does not consider the factual merits of the case on such applications. The Draft Civil Procedure Rules might, however, allow the insured or the insurer to apply for summary judgment against the third party in such cases.[90]

Is a leave requirement necessary to deter proceedings by third parties in which the liability of the insurer and of the insured will be in issue when those proceedings are unlikely to succeed because of the insurer's ability to rely on cover points?

12.36 Under current procedural rules, if the court is persuaded that the factual dispute over cover is separate from that over the insured's liability, it can order the cover issue to be tried as a preliminary issue to avoid wasted costs being incurred on the liability issue.[91]

Is a leave requirement necessary to prevent the insured's case being prejudiced and to protect the insurer[92] from having to run conflicting cases?

12.37 We have already given an example of the prejudice which an insurer might suffer were the liability of the insurer and of the insured to be resolved in the same proceedings.[93] We suggested that it is not unusual for those defending civil actions to plead conflicting arguments and that the court could use its powers to

[89] RSC O 18, r 19(1)(a). In Scotland, claims cannot be struck out on the ground that they disclose no reasonable cause of action.

[90] On the ground that the claimant had no realistic prospect of success: Draft Civil Proceedings Rules, Part 14, which would replace RSC Orders 14 and 18. This provision would not apply to cases allocated to the small claims track, although rule 26.9 of the Draft Civil Proceedings Rules allows a small claims arbitrator to hold a preliminary appointment to dispose of such claims.

[91] RSC O 33, r 3 and *Caspian Basin Specialised Emergency Salvage Administration and Another v Bouygus Offshore South Africa and Others*, *The Times* 3 July 1997, discussed in Appendix B. Under rule 1.3(e) of the Draft Civil Proceedings Rules, the court's duty to further the overriding objective of dealing with cases justly (rule 1.1) includes the duty to decide the order in which issues are to be resolved. Its powers of case management also include the power to decide the order in which issues are to be tried and to direct a separate trial of any issue, (rule 5.1 (1) (f), (g)). These rules are set out in Appendix B as are rules 22.3 and 36.1 of the Court of Session Rules which permit parts of the proof to be heard separately.

[92] Who will usually conduct the defence of the insured. See also para 12.5 above.

[93] See para 12.12 above.

determine the order in which issues are tried to balance the interests of the parties and to achieve the fairest trial possible.[94]

Is a leave requirement necessary to provide the court with an opportunity to consider whether the insured should be a defendant or defender to the proceedings (where the insurer believes that its ability to conduct the insured's defence would otherwise be prejudiced)[95]

12.38 Usually, the insurance contract will require the insured to provide information and assistance to the insurer.[96] We understand from insurers, however, that it is likely to be easier to obtain the insured's co-operation if he is a party to the proceedings. We have already given our provisional view that, for this and other reasons, the insured should normally be a party to any proceedings brought under the 1930 Act. Insurers may, in any case, be able to join the insured to proceedings brought by the third party[97] and to obtain information from him under existing procedural rules.[98]

Provisional conclusions on the advantages of a leave requirement

12.39 It is our provisional conclusion that a leave requirement would bring few, if any, of the possible advantages set out above. Inevitably, there would be duplication of the issues considered at the leave stage and at trial, which would involve the parties in additional cost and delay. In appropriate cases, preliminary issues could be dealt with by applications for striking out or summary judgment or, in Scotland, for summary decree.[99] In Scotland, pursuers rarely have to seek leave from the court to bring an action and the courts are reluctant to evaluate the strength of a case without hearing the evidence.[100] We believe that to allow third parties an automatic

[94] See para 12.12 above.

[95] This would only be an issue were the amended Act, by contrast with the position contemplated in para 12.23 above, to permit the third party to sue the insurer without joining the insured in the proceedings.

[96] See paras 5.51-5.54 above.

[97] See paras 4.24-4.26 and 12.18 above.

[98] RSC O 24, r 7A (CCR O 13, r 7(1)(g)) could be used in personal injury actions. There are also powers to issue subpoenas under RSC O 38, r 14. See paras 6.11-6.18 above.

[99] Court of Session Rules, rule 21. The Scottish court has the power to grant a summary decree on the grounds that the defences disclose no defence. The court has to be satisfied that no defence is disclosed and has regard to questions of law, documentary evidence, and the parties' pleadings. The criterion for satisfying the court has been stated in various ways, for example: no valid stateable defence (*McAlinden v Bearsden and Milngavie District Council*, 26 March 1985, Lord McDonald); defences must be relevant, genuine and proper, (*Frimokar (UK) Ltd v Mobile Technical Plant (International) Ltd* 1990 SLT 180); near certainty as to the absence of a defence (*P&M Sinclair v The Bamber Gray Partnership* 1987 SC 203).

[100] For example, section 2 of the Law Reform (Husband and Wife) Act 1962 gives the court a discretionary power to dismiss at an early stage an action by one spouse against the other based on contract or delict if no substantial benefit would accrue. The power is never exercised and its repeal has been recommended: Report on Family Law, Scot Law Com No 135, para 10.8.

right of action against insurers on the happening of one of the insolvency situations set out in the Act would respect the original intention of those passing the Act.[101]

12.40 Another option would be to require the third party to notify the insurer of his intention to proceed against it.[102] In our view, the only reason for requiring notification to be given to the insurer would be if the insurer were to be given the opportunity to object. For the same reasons as we provisionally conclude that a third party's right of action under an amended Act should not be subject to a leave requirement, we suggest that a third party should not be required to give notice to the insurer of his intention to proceed under the Act.

We seek consultees' views on our provisional conclusion that a third party's right to proceed against insurers under the Act should not be subject to a leave requirement nor to a requirement that he notify the insurer of his intention to proceed against it.

When should leave be sought?

12.41 A leave requirement would be intended to deal, in part, with speculative actions. The court would need, therefore, to consider the merits of the third party's case and would need to have sufficient information to enable it to do this.[103] Leave could be sought, for example, upon service of the third party's points of claim or following close of pleadings or, in Scotland, after closing the record.

Possible leave criteria

12.42 A variety of threshold tests are used as leave criteria in cases where the merits are to be considered at the leave stage.[104] One option would be for the plaintiff or pursuer to establish that there is an issue or question in dispute which ought to be tried or, in other words, that there is a fairly arguable case.[105] Points of law and the construction of documentary evidence would be considered at the leave stage[106] but disputes over fact, unless they were obviously totally without merit, would be left until trial.

[101] See para 1.11, n 25.

[102] As is required by the Nigerian Insurance Decree. See para 1.19 of Appendix F

[103] The test for leave for a defendant to issue a third party notice under O 16 r 2 would be inadequate for this purpose as the merits of the defendant's claim are not considered at the leave stage but are left over to be dealt with in subsequent applications for directions. See *Furness v Pickering* [1908] 2 Ch 204, *Edison v Holland* (1886) 33 Ch.D 497.

[104] The "labels" attached to these tests are not helpful in explaining the nature of the findings which the court is expected to make at the leave stage. See n 108 below.

[105] By analogy with the burden on the defendant in an application for summary judgment under RSC O 14. See RSC O 14, r 3 to O 14, r 8 for the variety of phrases that have been used to describe this test eg "triable issue", "a dispute as to facts or law which raises a reasonable doubt that the plaintiff is entitled to judgment", "where the defence can be described as more than shadowy but less than probable leave to defend should be given".

[106] See Goff LJ in *European Asian Bank AG v Punjab and Sind Bank (No 2)* [1983] 1 WLR 642, 654. See also RSC O 14, r 3 to r 4(2).

12.43 Another option, which would place a greater burden on the plaintiff or pursuer, would be to require him to prove that he had a realistic prospect of success. Were this criterion to be used, the court would be required to consider the merits of the case, including relevant available facts, at the leave stage.[107]

The procedure for leave

12.44 One option would be for the leave application to be made ex parte.[108] Although this might avoid some of the cost and delay of an inter partes application, the court might be ignorant of the case of the insured or the insurer if prior disclosure of any repudiation and of the grounds for repudiation had not been made. Even if some disclosure of the grounds had already been made, the underwriter might subsequently have acquired additional information which would be useful to the court. Our provisional view is, therefore, that any leave application should be inter partes and that the insured and/or the insurer should be able to make representations both on the merits of the third party's case against the insured and on any cover points.

If, contrary to our provisional conclusion, consultees consider that a third party's right of action under the Act should be subject to a leave requirement, their views are sought on:-

(i) when the leave application should be made;

(ii) what the leave criteria should be; and

[107] See the distinction made by Sir Roger Ormrod between the O 14 burden and that applicable where a defendant seeks to set aside judgment in default of defence in *The Saudi Eagle* [1996] 2 Lloyd's Rep 221, 223; "the primary consideration is whether the defendant "has merits to which the Court should pay heed..., not as a rule of law but as a matter of common sense"; "the Court must form a provisional view of the probable outcome". (See also *Allen v Taylor* 1992 1 PIQR 255). In *Smith v Cosworth Casting CA 1985, The Times* 28 March 1997 Lord Woolf MR gave some general guidance as to applications for leave to appeal and applications to set aside such leave as follows "1. The court will only refuse leave if satisfied that the applicant has no realistic prospect of succeeding on the appeal. This test is not meant to be any different from that which is sometimes used, which is that the applicant has no arguable case. Why however this court has decided to adopt the former phrase is because the use of the word "realistic" makes it clear that a fanciful prospect or an unrealistic argument is not sufficient". This guidance suggests that the distinction drawn by Sir Roger Ormrod between an arguable case and a realistic case is not correct. If we were to create a leave stage as part of our reforms it would we think be incumbent upon us to set out with some precision the nature of the test to be satisfied by the plaintiff. This is why the text in paras 12.42-12.43 above attempts to distinguish between the findings which the court is expected to make on facts and law at the leave stage in addition to referring to the labels of "arguable" and "realistic". Section 6(4) of the New South Wales Law Reform (Miscellaneous Provisions) Act 1946 and s 25 of the Australian Capital Territories Law Reform (Miscellaneous Provisions) Act 1955, which both make a third party's right of action subject to a leave requirement provide that "leave shall not be granted in any case where the court is satisfied that the insurer is entitled under the terms of the contract of insurance to disclaim liability, and that any proceedings, including arbitration proceedings, necessary to establish that the insurer is so entitled to disclaim, have been taken". See para 1.12 of Appendix F.

[108] As is the case under RSC O 11 which applies to applications by plaintiffs seeking leave to serve a writ overseas.

(iii) whether the leave application should be made ex parte or inter partes and whether any other specific procedural requirements should apply.[109]

Should a third party have a right to set aside settlements made between the insurer and the insured prior to the happening of one of the insolvency situations set out in the Act?

12.45 As we discussed above,[110] section 3 of the Act prohibits agreements reached between the insurer and the insured after, but not before, the happening of one of the insolvency situations set out in the Act. It is possible that, in some cases, insured parties heading towards insolvency may be tempted to compromise their claims against insurers.[111] We have suggested that officeholders may be reluctant to use their powers to set aside transactions at an undervalue and transactions defrauding creditors.[112]

12.46 We have already set out our provisional conclusion that rights under the Act should not transfer to third parties until the happening of one of the insolvency events set out in the Act.[113] We have also discussed the problems of defining rights by reference to an earlier period.[114] Were section 3 to be amended to allow settlements reached before this point to be set aside, it might cause uncertainty to insurers and to their insured as to when they could settle claims.

12.47 An amended section 3 allowing third parties to apply to set aside such settlements would, we suggest, have to provide that they could do so only in respect of settlements reached within a certain period before the insolvency event.[115] Before granting such an application, the court would need to consider the merits of the third party's case under the Act. It would need to consider the strength of the third party's claim against the insured as well as the likelihood of the insurer being liable to the third party under the insurance contract.

We seek consultees' views on whether settlements reached between insurers and insured prior to the happening of one of the insolvency events set out in the Act cause problems to third party claimants under the Act

[109] For example, if proceedings against the insured are not already underway, whether the insured should be given notice of the application. Rule 10.5 (1)(b) of the Draft Civil Proceedings Rules requires notice to be served on non-parties "to whom the court's order will apply, if the application is granted".

[110] See paras 5.8-5.9 above.

[111] See *Normid Housing Association v Ralphs* [1989] 1 Lloyd's Rep 256 discussed at para 5.9, n 13 above.

[112] See para 6.9 above. Were provisions in the Insolvency Act and the Bankruptcy (Scotland) Act to be used in such cases, an assignment by an insured faced with imminent bankruptcy of his rights against his insurer might also be defeated in this way.

[113] See para 12.10 above.

[114] See para 12.9 above.

[115] Cf s 240 of the Insolvency Act 1986 which provides that transactions at an undervalue or preferences to those connected with a wound up company can be set aside if given within two years ending with the onset of insolvency. Other preferences can be set aside if given within six months of that point.

and whether, in their view, the Act should be amended to allow third parties to apply to set aside such settlements.

Were such an amendment to be made to the Act, within what period prior to the insolvency should settlements be vulnerable to setting aside?

PAYMENT OF THE INSURANCE PROCEEDS BY THE INSURER

12.48 In some jurisdictions, legislation requires the insurer to pay the insurance proceeds direct to a third party claimant.[116] We understand that this often happens in practice here or that the insurer will require a receipt from the recipient of the money. We also suspect that problems are less likely to arise here because, if he did not pay the third party, the insurer would pay the insolvency practitioner rather than the insolvent insured (who might be tempted not to pay it over to the third party). As the third party is in the position of the insured following the transfer of rights under the Act, the insurer should arguably pay him in any event.

We seek consultees' views on whether or not a provision should be included in an amended Act requiring insurers expressly to pay insurance proceeds direct to the third party.

Should a third party have a right of direct action against the insurer of an insured party who has disappeared?

12.49 In Australia, legislation has been introduced providing third parties with rights of action against insurers in cases where the insured has died or cannot, after reasonable enquiry, be found.[117] We are not aware of this causing problems in this country.[118] A third party wishing to proceed against an insured who has disappeared may be able to obtain an order for substituted service[119] or service by newspaper advertisement.[120] Were third parties to have such a right under an amended Act, they would, we suggest, have to satisfy the court that they had made all reasonable efforts to find the insured.

We seek consultees' views on whether the 1930 Act should be extended to provide third parties with a right of action against the insurers of insured parties who have disappeared.

[116] See, for example, Article L124-3 of the French Code des Assurances, set out at para 1.30 of Appendix F.

[117] Section 51 of the Insurance Contracts Act 1984. Separate legislation deals with insolvency. See Appendix F. In the context of our legislation, such a provision would only be relevant to cases involving individual insureds.

[118] The 1930 Act applies in cases where the insolvent insured has died. See para 2.21 above. The position of dissolved companies which have been struck off the register and so no longer exist, is discussed at paras 4.44-4.51 above.

[119] RSC O 65, r 5 and CCR O 7, r 8. In personal injury actions arising out of road traffic accidents, if the defendant cannot be traced, the injured third party must show that all reasonable efforts have been made to trace him and to effect personal service of the writ. If the Master is so satisfied and if the identity of the insurer is known, the Master may make an order for substituted service on the defendant at the address of his insurer. See *Gurtner v Circuit* [1968] 2 AB 587 and RSC O 65, r 4(5).

[120] Court of Session Rules, rule 16.5.

PART 13
DISCLOSURE OF POLICY INFORMATION

13.1 In Part 12,[1] we gave our provisional view that the third party should acquire rights against the insurer once two events have occurred: the incident giving rise to the liability of the insured and one of the insolvency events set out in the Act.[2] In this Part, we suggest that the duty to disclose policy information should arise at the same point, or within a specified time afterwards.[3] We consider what information should be discloseable under section 2[4] and give our provisional view that the duty to disclose should not vary according to the nature of the third party's claim.[5] We ask who should have a duty to disclose and what the extent of that duty should be.[6] We consider whether the duty should be extended to brokers and others authorised to hold policy information[7] and, if so, what the extent of their duty should be.[8] We suggest that the duty of the insured and of the insurer to disclose should arise simultaneously.[9]

When should the duty to disclose policy information arise?

13.2 It appears, despite the interpretation given to the section by the court, that Parliament intended to lay down in section 2 a duty to disclose policy information before the third party starts proceedings against the insured.[10] Pre-action disclosure of information is also in line with the "cards on the table" approach to

[1] See para 12.10 above.

[2] In Part 6, we considered the duty of disclosure under s 2 of the Act and under the general law.

[3] As the disclosing party may need an opportunity to review documentation and to consider which documents should be disclosed. See paras 13.2-13.4 below.

[4] See paras 13.5-13.14 below.

[5] See para 13.15 below.

[6] See paras 13.16-13.20 below.

[7] See paras 13.19-13.20 below.

[8] See para 13.20 below.

[9] See para 13.17 below.

[10] The Attorney General told MPs that "it is in the interests of all parties that there is pre-action disclosure of as much policy information as possible to third parties".

litigation which has been taken in recent years[11] and with recommendations in the Woolf Report. [12]

13.3 Concern has been voiced by insurers that information disclosed to a third party might be passed on to other potential claimants.[13] Documents obtained in discovery may be used only for the proper purposes of conducting that case and an implied undertaking is made to the court not to use the information received for any collateral or ulterior purpose. Any misuse of the information may be restrained by injunction or punished as a contempt.[14] Some insurance policies contain confidentiality clauses which prohibit the recipient of policy information from disclosing that information to others. Depending on the terms of such clauses and the circumstances in which they come into effect, they may be undermined by section 2(1) of the Act.[15]

13.4 We have already given our provisional view that the right to proceed against the insurer should not be conditional on his first establishing the liability of the insured and should arise once two events have occurred: the incident giving rise to the liability of the insured and the happening of one of the insolvency situations set out in the Act.[16] Were the Act to be amended in this way, third parties' rights to pre-action disclosure under the Act and under the general rules of procedure would be improved in any event as the insurer would be a party to the third party's proceedings at an earlier stage.[17] We suggest that, whether or not the Act is

[11] See comments of Peter Goldsmith QC in a speech to the British Insurance Law Association, 3 February 1995: "The tendency over the past ten years has been the move to a more and more open approach to litigation. We had witness statements, skeleton arguments and pre-trial hearings all designed to give both a better understanding in advance of the trial of the other side's case so realistic assessments can be made of the merits of settlement. In the modern age of "cards sides on the table" litigation, is it really so wrong to suggest that the one factor which may be most key to a plaintiff's view, what is the limit of cover and will the costs eat it up anyway, should be known?" As we have seen, Philips J gave judicial support to allowing third parties early access to policy information in *BBL v Eagle Star*, *The Times* 21 February, 1995. See para 4.37 above.

[12] *Access to Justice*, Chapter 10, page 107, para 4. The Woolf Report seeks to set up a system which "enables the parties to a dispute to embark on meaningful negotiation as soon as the possibility of litigation is identified, and ensures that as early as possible they have the relevant information to define their claims and make realistic offers to settle". See paras 10.9-10.11 above. See para 4.34 above for another potential effect of early disclosure of policy information.

[13] This issue was raised, for example, in *Cox v Bankside* [1995] 2 Lloyd's Rep 437.

[14] *The Distillers Co (Biochemicals) Ltd v Times Newspapers Ltd* [1975] QB 613, following *Alterskye v Scott* [1948] 1 All ER 469, 471. An action based on a document obtained in discovery in other proceedings will usually be dismissed as an abuse of process of the court; *Riddick v Thames Board Mills Ltd* [1977] QB 881; [1977] 3 All ER 677, CA though in an appropriate case a party may apply to the court for leave to use discovered documents in a separate action; *Sybron Corporation v Barclays Bank plc* [1985] Ch 299, 320H - 321A. See also *Miller v Scorey*, *The Times* 2 April 1996.

[15] See para 3.2 above.

[16] See para 12.33 above.

[17] Under s 33(2) of the Supreme Court Act 1981 and s 52(2) of the County Courts Act 1984, third parties have better rights to pre-action disclosure and to disclosure against non-parties in cases involving death or personal injury. This followed recommendations in the report of the Royal Commission on Civil Liability and Compensation for Personal Injury 1978 ("the

amended in this way, the duty to disclose policy information should arise after those two events and should not be dependent on the third party establishing the liability of the insured. We take the view, however, that it would be preferable to postpone the duty to disclose until the disclosing party has had a reasonable period in which to consider what he should disclose and to locate and obtain relevant documentation and information. Once triggered, the duty to disclose should, we suggest, be continuous. This may be particularly important with regard to information on repudiation and the value of the insurance cover.

Consultees' views are sought on our provisional conclusion that the obligation to disclose policy information should not be dependent on the establishment of the liability of the insured but that it should arise after the incident giving rise to the liability of the insured and after the event of insolvency and that disclosure should be given within 14 days of the disclosing party becoming aware that a third party has a possible claim[18] under the Act.[19]

Do consultees agree that disclosing parties should have a continuing duty to disclose[20] information?

If consultees disagree, when do they consider the duty to disclose should arise?[21]

Pearson Report") which, it appears, were limited to death and personal injury actions because of the Committee's terms of reference. The Report notes : "Our recommendations relate to personal injury cases because that is the class of case within our terms of reference. If any of our recommendations is thought to be worthy of more general application, in most cases we should be very pleased". We discussed in Part 11 above whether the scope of the Act should be restricted to cases involving death or personal injury. Section 8 of the Civil Procedure Act 1997 gives the Lord Chancellor power to extend s 33(2) SCA 1981 and s 52(2) CCA 1984 to other types of claim. In Scotland, s 1 of the Administration of Justice (Scotland) Act 1972 confers power on the courts to order the production and inspection of documents which appear to the court to be property as to which any question may relevantly arise in existing or likely proceedings. The proceedings are not limited to actions involving personal injury or death. Before the proceedings are commenced, application is by petition under rule 64 of the Court of Session Rules; afterwards it is by motion in the proceedings under rule 35.

[18] In many cases, the insured and the insurer are likely already to be aware of the third party's claim on the happening of one of the insolvency events set out in the Act. Where the third party was unaware of the identity of the insurer, he could obtain this information from the insolvency practitioner and contact the insurer himself to ensure that the insurer was aware of his claim. Section 2 of the Act currently provides for disclosure to be made "on the request of" the third party.

[19] Were our provisional recommendations to be implemented, this would be when the insurer was aware of the event giving rise to the liability of the insured to the third party and that one of the insolvency events set out in the Act had occurred.

[20] The duty to disclose is continuous under the general law (see RSC O 24) but there may be advantages to providing expressly that the duty to disclose under the Act is also continuous.

[21] They may believe, for example, that disclosure of insurance details should not take place until the third party has commenced proceedings against the insurer.

Consultees' views are sought on whether a time period other than 14 days would be appropriate with regard to some or all of the categories discussed below.[22]

INFORMATION DISCLOSEABLE UNDER SECTION 2

13.5 We have already referred to criticism of the vague wording of the definition in section 2.[23] It should be noted that section 2, by contrast with the provisions as to documents, does not specifically list the types of information which may be of use to a third party and which we suggest below should be disclosed.[24] To help us to ascertain the documentation and information to which third parties might be entitled under the Act and to consider whether all such documentation and information should be disclosed at the same time, it is helpful to list the main categories of information which could possibly be of use to a third party seeking to proceed under the 1930 Act:-

(i) the existence of the insurance policy;

(ii) the identity of the insurer;

(iii) details of whether or not the insurer has repudiated cover;

(iv) the grounds of repudiation (for example for non-disclosure or breach of warranty and details of the breach);

(v) the terms of the insurance policy;

(vi) the value of the insurance cover and details of whether or not some or all of the insurance fund has already been paid out to other claimants;

(vii) details of any settlement between the insurer and the insured.

We have reached the provisional conclusion that the definition in section 2 of the categories of information to which the duty of disclosure extends should be clarified by a list in the Act.

Consultees' views are sought on this provisional conclusion.[25]

THE CATEGORIES OF POLICY INFORMATION WHICH SHOULD BE DISCLOSED

The existence of the insurance policy and the identity of the insurer

13.6 Unless he has information about whether or not the defendant or defender is insured, the third party will not know whether or not he might have a remedy under the 1930 Act. If he does not know the identity of the insurer, he will not know from whom he can seek that remedy. In many cases, this information will

[22] See para 13.5 (i)-(vii).

[23] The wording of which is set out at Appendix A. See para 6.4 above.

[24] See para 13.13 below.

[25] We discuss at para 13.13 below the categories of policy documentation and information which might be included in any statutory list.

already have been provided to the third party. In some cases, however, an officeholder may find it difficult to establish from the insured's records whether or not insurance cover is in place.

The terms of the insurance policy

13.7 As we have seen, third parties must have early disclosure of the terms of the insurance contract if they are to meet certain notice requirements and to assess whether any purported repudiation of cover by the insurer on the grounds of non-compliance by the insured is justified. Early disclosure of this information should discourage third parties from commencing proceedings if it is clear that the insurer is not liable to indemnify the insured under the insurance contract. Pre-action disclosure of the terms of insurance contracts may already be obtainable in Scotland.[26]

Whether or not the insurer has repudiated cover

13.8 In some cases, the insurer will voluntarily inform the third party whether or not he has purported to repudiate cover as this may prevent the third party from pursuing an action against the insured which the insurer will defend. This information alone, without details of the grounds of repudiation, may be of limited use to the third party but should, in our view, also be made available: it too relates to the very existence of cover.

The grounds of repudiation (for example for non-disclosure or breach of warranty and details of the breach)

13.9 Knowledge of the grounds of any purported repudiation of cover by the insurer may be vital to the ability of the third party to challenge the insurer's defence and to pursue his claim under the Act. Disclosure of this information before the liability of the insured has been established may, however, prejudice the defence of the insured.

13.10 We need to consider whether an insurer would or should be able to apply to court for an order exempting him from having to disclose the grounds of repudiation in certain cases or requiring disclosure to be made to certain persons only. Procedural rules only allow parties to limit initial disclosure to the court[27] or to their opponents' legal advisers in exceptional circumstances.[28] In appropriate cases, however, the court may order any issue of fact or law to be tried as a preliminary

[26] Under Scots law, third parties may be able to obtain disclosure of the terms of the insurance contract as well as of the identity of the insurer under s 1(1A) of the Administration of Justice (Scotland) Act 1972. See para 4.18 above.

[27] Eg where an assertion of public interest immunity is made. See RSC O 24, r 7A(7) (CCR, O 13, r 7(1)(g) and 2A).

[28] RSC O 32. See also *Arab Monetary fund v Hashim* [1989] 1 WLR 565, 577 where the court held that there is "only a limited jurisdiction to be exercised only in exceptional circumstances, whereby the court can direct that facts disclosed by one party are not disclosed to the other party provided, of course, that they are disclosed to someone on that party's side, who can effectively deal with the matter".

issue[29] and the disclosure issue could be dealt with in this way. The court may also order split trials.[30]

Consultees' views are sought on whether the disclosing party should be able to apply to court for an order dispensing with their duty to disclose the grounds for a purported repudiation of cover by the insurer, in addition to any right which they may have to apply for a split trial or for the resolution of the cover point as a preliminary issue.[31]

The value of the insurance cover and details of whether or not some or all of the insurance fund has already been paid out to other claimants

13.11 In English and Scottish law, those defending civil proceedings have no duty to disclose their financial assets, including any insurance policies which they may have.[32] It is argued that such disclosure might encourage litigation.[33] Some commentators suggest that information relating to the value of any insurance cover held by an insolvent insured should be treated differently as the insurance relates to the particular liability of the insured to the third party and is likely to be the insolvent insured's only valuable asset.[34]

[29] RSC O 33, r 3 set out in Appendix B.

[30] RSC O 15, r 5 set out in Appendix B. See para 12.12, n 34 above. The court will consider whether joinder might cause damage to one party because evidence might be admissible in the action against the co-party which would be inadmissible in an action against him; see *Sandes v Wildsmith* [1893] 1 QB 771, 774.

[31] Insurers could be permitted, for example, to make initial disclosure to the court alone so that the court could decide whether or not disclosure was necessary. The position of insurers may be improved under the Draft Civil Proceedings Rules, rule 27.15 of which provides that the court "may direct that disclosure shall take place in stages". Rule 27.16(1) provides that any party may apply for an order "dispensing with or limiting his duty of standard disclosure".

[32] But as to Scotland, see para 4.18 above. In the United States, Rule 26(a)(1)(D) of the Federal Rules of Civil Procedure provides for the disclosure of the insurance policy, including the value of the cover, "without awaiting a discovery request". The Advisory Committee Note on the precursor to this rule (Rule 26(b)(2)) said that insurance coverage "should be distinguished from any other facts concerning defendant's financial status (1) because insurance is an asset created specifically to satisfy the claim; (2) because the insurance company ordinarily controls the litigation; (3) because information about coverage is available only from defendant or his insurer; and (4) because disclosure does not involve a significant invasion of privacy". This rule has not been adopted in all states.

[33] As we have already seen (para 4.22, n 41) disclosure of the existence of insurance cover was previously prohibited by the court, but the position has now changed.

[34] See, for example, Sir Jonathan Mance "Insolvency at Sea" [1995] LMCLQ 34, at 43. "True, a plaintiff must normally take his defendant as he finds him. But the key to the 1930 Act is to recognise the fundamental difference between an insolvent defendant and other defendants. First the insolvent defendant is and is known to be unable to pay. Secondly, despite his own insolvency, his insurers can and will often make the task of establishing liability against him extremely onerous, a problem which all the inventiveness of Lord Woolf's Enquiry into Access to Justice will be hard put entirely to eliminate ..". See also Peter Goldsmith in a speech to BILA, 3 February 1995: "In the modern age of "cards sides on the table" litigation, is it really so wrong to suggest that the one factor which may be most key to a plaintiff's view, what is the limit of cover and will the costs eat it up anyway, should be known?"

13.12 In many cases, third parties proceeding under the 1930 Act may assume that the insured has adequate insurance and proceed with their claims anyway. This may lead to all parties incurring unnecessary costs and to fruitless actions being pursued through the courts.[35] Were third parties to know at an early stage that the insurance fund was likely to be inadequate to meet their claim, they might not proceed with their actions.

13.13 In *Cox v Bankside*,[36] there was some judicial support for allowing disclosure of the value of insurance cover in cases involving the 1930 Act. The Court of Appeal held "with regret" that there was no duty to disclose details of insurance cover,[37] but Saville LJ suggested that "in the circumstances of the Lloyd's litigation, there is much to be said for the view that the sooner the parties know where they stand as regards likely recoveries at the end of the road, the sooner and cheaper will be the resolution of this litigation, which can only be for the benefit of all".[38]

We have reached the provisional conclusion that the following categories of policy documentation and information should be disclosed to third party claimants under the Act:-

(i) the existence of any insurance contract;

(ii) the identity of the insurer;

(iii) relevant policy documentation, including the cover terms;

(iv) whether the insurer has purported to repudiate cover;

(v) the grounds of any purported repudiation;

(vi) the value of the insurance cover and details of whether or not some or all of the insurance fund has already been paid out to other claimants;[39]

Do consultees agree that all these categories should be disclosed? If not, which are objectionable? Are there any other categories of documentation or information which should be disclosed?

[35] See our discussion of *Banque Bruxelles Lambert v Eagle Star Insurance* [1997] AC 191, at para 4.37 above.

[36] [1995] 2 Lloyd's Rep 437. See para 7.2 above.

[37] Because this information was not relevant to the legal issues raised by the applicants.

[38] *Ibid*, at p 465. See also the decision of Phillips J at [1995] 2 Lloyd's Rep 437. In the Lloyds litigation, the Commercial Court actually warned claimants at the outset that there might be insufficient funds to meet all claims. Lloyds underwriters were concerned that disclosure of the level of errors and omissions cover taken out by underwriting agencies would enable a Name who was a member of more than one action group and who received information as a member of one group to use that knowledge in connection with another claim.

[39] Whether as a result of a judgment of the court, an arbitration award or of settlement. We discuss at Part 15 below whether of not a scheme of rateable distribution of insurance proceeds to multiple claimants under the Act should be introduced.

Do consultees think that, in addition to any list of discloseable information set out in an amended Act,[40] it should also contain a catch all provision requiring disclosure of "other relevant documents and information"?

Details of any settlement between the insurer and the insured

13.14 We discussed above the anti-avoidance provision in section 3 of the Act preventing the insurer and the insured from settling claims under the policy after one of the insolvency situations set out in the Act.[41] We have also noted that section 3 does not affect settlements reached before that point.[42] We have set out our provisional view that third parties should not acquire rights under the Act, including the right to challenge such settlements, until the happening of one of the insolvency situations set out in the Act.[43]

We have reached the provisional conclusion that the duty to disclose should not extend to details of any settlement between the insured and the insurer before the occurrence of one of the insolvency situations.[44] Do consultees agree with this provisional conclusion?

SHOULD THE EXTENT OF THE DUTY OF DISCLOSURE VARY ACCORDING TO THE NATURE OF THE THIRD PARTY OR OF HIS CLAIM?

13.15 In Part 11, we discussed whether only certain types of claimant or claimants with a particular type of claim should be able to rely on the amended Act.[45] We gave our provisional view that the scope of the Act should not be restricted in this way.[46] All litigants have better rights to pre-action disclosure and to disclosure against non-parties in cases involving death or personal injury.[47] As we have seen, Parliament has also placed a duty on employers to exhibit certificates of insurance at their place of business.[48] In line with our provisional view that the scope of the Act should not be restricted to particular types of claim or claimant, we also take the provisional view that the duty of disclosure should not vary according to the nature of the third party's claim.

Do consultees agree that the duty to disclose under an amended Act should not vary according to the nature of the third party's claim?

[40] See para 13.5 above.

[41] See paras 5.8-5.9 above.

[42] See para 5.9 above.

[43] See para 12.10 above.

[44] Subject to the duty to disclose any decreases in the value of the insurance fund as a result of such settlements. See paras 13.11-13.13 above.

[45] See paras 11.9-11.20 above.

[46] See para 11.20 above.

[47] See s 33(2) of the Supreme Court Act 1981 and s 52(2) of the County Courts Act 1984. See also n 17 above, where we noted hopes expressed in the Pearson Report that the wider right of disclosure which they recommended would not be restricted to personal injury claims. We also discuss the position in Scotland at n 17 above.

[48] Regulation 6(2) of the Employers' Liability (Compulsory Insurance) General Regulations 1971. See para 6.20, n 26 above.

WHO SHOULD HAVE A DUTY OF DISCLOSURE AND WHAT SHOULD THE SCOPE OF THE DUTY BE?

Should the duty of the insured[49] and of the insurer to disclose policy information be simultaneous?

13.16 As we have seen, the insurer's duty to disclose policy information under section 2(2) only arises if the third party has already obtained disclosure under section 2(1) of information which "discloses reasonable ground for supposing" that rights against the insurer "have or may have been transferred" to the third party. As we have said, the insured and the officeholder may be unable or reluctant to meet their duty of disclosure or may delay doing so.[50]

13.17 It may be important for the third party to acquire information from the insurer as quickly as possible. The insurer[51] may be in a better position to provide the relevant information, particularly as he will probably be investigating the insured's rights under the policy himself and deciding whether or not to conduct the insured's defence.[52] Our provisional view is that the duties of the insured[53] and of the insurer to disclose policy information under the Act should arise at the same time. Third parties should be not be able to insist, however, that identical disclosure is made by all parties as this would lead to duplication and unnecessary costs.

Do consultees agree that the duties of the insured and of the insurer should arise simultaneously?

Should an officeholder's duty of disclosure be as onerous as that of the insurer?

13.18 Consideration needs to be given to whether the duty to disclose policy information under the Act should be as onerous for officeholders as for insurers under the Act. The affairs of a bankrupt or wound up insured may be in disarray and it may be very difficult, time consuming and costly for an officeholder to conduct a search for policy documentation. Insolvency practitioners may be reluctant to incur costs which will be deducted from the insured's general assets, to the detriment of all his creditors. Receivers appointed by those with security over particular assets held by the insured may be particularly reluctant to undertake such an exercise.

With regard to each of the categories of information set out above,[54] consultees' views are sought on what the extent of the officeholder's duty to disclose should be. For example, should his duty:-

[49] And of the officeholder and others defined in s 2(1).

[50] See para 6.9 above.

[51] Or the insurance broker. We discuss at paras 13.19-13.20 below whether the duty of disclosure should be extended to brokers and others.

[52] Requiring the insurer to disclose may also alleviate some of the problems associated with officeholders' uncertainty over their duties of disclosure. See paras 6.9-6.10 above.

[53] And of the other parties listed in s 2(1).

[54] See para 13.5 (i)-(vii).

(i) apply only to information which is reasonably ascertainable from records to which he is entitled; and/or

(ii) be limited

(a) to third parties who seek disclosure from him; or

(b) to third parties who seek such disclosure and whose claims he is aware may be covered by insurance.

Should others holding policy information have a duty of disclosure and what should the extent of that duty be?

13.19 As we have seen, the duty to disclose policy information is only expressly stated to apply to the insurer, the insured and officeholders.[55] It does not extend to insurance brokers or others authorised to hold policy information, such as managers of pools set up by a number of insurers or travel agents who have arranged insurance cover for their customers.[56] In many instances, such persons may be the best able to identify the policy governing a particular claim. In most cases, however, either the insured or the insurer will be entitled to obtain the information held by such parties and may therefore be able to disclose it.[57] Where there are potential claims against the insured, the insured or the officeholder and the insurer may already have obtained such information to enable them to investigate the claim and possible defences to it.

13.20 Consideration needs to be given to whether there would be advantages to persons other than the insured, the officeholder and the insurer having an express duty to provide information under the Act and to what information they should be required to disclose. Consultees may consider that the involvement of such persons may be unnecessary, particularly if third parties can usually obtain the information from the insured, the officeholder or the insurer.

Consultees' views are sought on the extent to which the position of third parties would be improved were a duty of disclosure under the Act to extend to all those in possession of insurance information or documentation and on whether the duty of disclosure should be extended in this way.

If such persons were to have a duty of disclosure, should it be limited? For example, should it be limited to information as to the identity of the

[55] See s 2(1) and (2).

[56] See para 6.7, n 4. Commentators who have voiced support for extending the duty to disclose to brokers include Sir Jonathan Mance, "Insolvency at Sea", and Philip Rocher and Mark Pring, Insurance Day, 7 September 1995, 6.

[57] Their entitlement to such information and documents would depend on whether those others could be said to be the agents of the insured or insurers. Brokers, for example, are usually agents of the former but may be agents of the latter. If the insured or insurer had not obtained documents to which they were entitled it is unlikely that O 24, r 1 (CCR O 14) would operate to impose a duty on them to obtain the documents (as being within their "power") for the purpose of disclosure under s 2 of the Act. In Scotland, any person in possession of documents may be required to make them available.

insurer or to information which is reasonably ascertainable from the records maintained by such persons?

Do consultees consider that the duty of disclosure should be extended only to insurance brokers?

PART 14
DEFENCES

14.1 In Part 5 we considered the ability of insurers to rely, as against third parties, on defences which they would have had against the insured under the insurance contract and at the problems which this has caused to third parties. In this Part, we consider whether the ability of insurers to rely on certain breaches against third parties should be restricted and, if so, what form any restrictions should take. We appreciate that the issue of the ability of insurers to rely on defences is a wide one, with implications far beyond the 1930 Act. The ability of insurers to rely on defences of non-disclosure and breach of warranty was discussed in a Law Commission report in 1980.[1] We concentrate here on whether the particular problems faced by third party claimants under the Act would justify restricting the ability of insurers to rely on defences against them.[2]

14.2 First, we consider briefly again the position of third party claimants under the 1930 Act. Secondly, we list possible bases for limiting the ability of insurers to rely on defences and consider when limitations might arise. Thirdly, we consider whether, were insurers to be prevented from relying on certain defences, they should have a right of recourse against the insured's assets to recover any sums which they have paid to third parties because of their inability to rely on those defences. We set out a number of tentative suggestions on which we seek consultees' views.

THE POSITION OF THIRD PARTY CLAIMANTS UNDER THE 1930 ACT

14.3 The transfer of the insured's rights against the insurer to the third party under the Act was intended to place the third party in the position of the insured. As we have seen, however, the effect of the Act has been somewhat different. Third parties may be unable to meet policy conditions which could be met by the insured because the nature of those conditions is such that they can only be met by the insured or because the insurer is able to insist on performance by the insured himself.[3] The insured's failure to satisfy such conditions then prevents the third party recovering under the Act. This has been the case with conditions requiring the insured to co-operate and provide assistance to the insurer[4] and those requiring

[1] Insurance Law, Non-disclosure and Breach of Warranty (1980) Law Com No 104. See also the recent report of the National Consumer Council, Insurance Law Reform; The Consumer Case for a Review of Insurance Law (May 1997) referred to at para 2.7, n 16 above.

[2] Were some of our provisional recommendations to be implemented, the position of a third party claimant under an amended Act would be different from that of a solvent insured seeking an indemnity from his insurer. Insurers might, for example, be able to rely on policy breaches which were not connected to the loss or which did not cause prejudice to the insurer against a solvent insured but prevented from relying on them against a third party claimant to whom an insolvent insured was liable.

[3] See Part 5 above.

[4] *Edwards v Minster Insurance Co Ltd* (unreported) 10 March 1994, see paras 5.52-5.54. As we have seen, the court rejected the argument that such conditions were merely incidental to the right to an indemnity.

the insured to pay the third party before seeking an indemnity from the insurer.[5] Our provisional view is that the law should permit third parties to satisfy certain policy conditions, such as notice requirements.

14.4 Without access to policy information, third parties may not know of the existence or scope of even those policy conditions which they might be able themselves to fulfil.[6] Implementation of our provisional recommendations on earlier rights of action and duties of disclosure would itself improve the position of third parties.

14.5 The inclusion in the Act of specific notice and anti-avoidance provisions shows that its draftsmen recognised that third party claimants would need certain additional rights to those transferred to them from the insured.

14.6 We suggest that some restrictions should be placed on the ability of insurers to rely on breaches of conditions. As we have already noted above, the likelihood of such breaches occurring may increase in the period running up to the insolvency of the insured when the insured may be technically insolvent.[7] At that point, rights cannot transfer under the Act because the insured has not yet been declared bankrupt or wound up.[8] Among the issues we discuss below is whether the ability of insurers to rely on such breaches should depend on the consequences of the breaches.

Consultees' views are sought on our provisional view that:

(i) restrictions should be placed on the ability of insurers to rely on certain defences against third parties because of the particular problems faced by third party claimants under the 1930 Act which are not faced by the insured;[9] and

(ii) insurers should not be permitted to insist that policy conditions are met by the insured personally where the third party can meet them.[10]

5 *The Fanti* [1991] 2 AC 1. See para 5.59-5.62 above.

6 Third parties may find their claims defeated because of the inaction of the insured's insolvency practitioner or administrative receiver.

7 In that he is unable to meet all his liabilities.

8 See the discussion of this distinction in *The Fanti* at para 5.61 above. We discussed in Part 12, and provisionally rejected the idea that third parties should acquire rights under the Act prior to the happening of one of the insolvency events set out in the Act.

9 It has been suggested of Australian reforms restricting the ability of insurers to rely on defences that "there is no evidence that it has had any significant financial implication in terms of putting up the cost of insurance for consumers". National Consumer Council Report: Insurance Law Reform: The Consumer Case for a Review of Insurance Law (May 1997) p 48.

10 The most obvious types of condition to which this would apply are notice requirements. See para 14.3 above. We do not take the view that third parties should have a duty as well as a right to meet policy conditions where they are in a position to do so. It would be odd to impose a duty on third parties under the 1930 Act when no such duty exists under the general law. Also imposing such a duty might cause confusion between the insured, the officeholder and the third party as to who owed the duty and as to when the duty arose.

WHAT BASES COULD BE USED TO LIMIT THE ABILITY OF INSURERS TO RELY ON DEFENCES?

14.7 As we have seen, there are already a number of statutory and non-statutory restrictions on the ability of insurers to rely on defences.[11] The Road Traffic Act 1988 and the Employers' Liability (Compulsory Insurance) General Regulations 1971 prohibit certain types of policy condition.[12] Other restrictions have been voluntarily undertaken by insurers themselves, through compliance with industry Statements of Practice.[13] Most but not all insurers abide by these restrictions and there are concerns that, as the single market develops, insurance may increasingly be provided by insurers outside the United Kingdom who are not bound by them.[14]

14.8 We consider below whether these or other types of restriction introduced in this country and in other jurisdictions should be used as possible bases for limiting the ability of insurers to rely on defences[15] against third party claimants under the 1930 Act. We consider whether insurers should be prevented from relying on defences where the relevant risk is covered by compulsory insurance[16] or where the third party's claim is of a particular type.[17] We discuss whether there should be a ban on insurers relying on certain defences after a certain point in time[18] or whether the consequences of a breach of duty or policy term should determine the ability of the insurer to rely on the breach.[19]

14.9 We set out below a number of defences commonly relied on by insurers[20] and suggest that particular considerations may determine whether such general restrictions should apply to them. We suggest, for example, that insurers should not be prevented from relying against third party claimants on defences of non-disclosure or misrepresentation as, in most cases, such defences are likely to relate to the insured's general right to cover rather than to his right to an indemnity in respect of his liability to the third party. We seek consultees' views on whether a

[11] See Part 5.

[12] See paras 5.10-5.12 above.

[13] See para 5.13. It is not clear whether third parties can rely on this statement. Most insurers also submit to the dispute handling scheme operated by the Insurance Ombudsman Bureau. This scheme leads to the speedy and cheap resolution of many disputes and, according to the National Consumer Council "has arguably been the industry's most effective form of self-regulation as far as consumers are concerned". See Insurance Law Reform; the Consumer Case for a Review of Insurance Law, NCC Report (May 1997) p 10. Currently, however, the Bureau's jurisdiction does not extend to complaints from third parties, although the Insurance Ombudsman has recommended that it should do so. See Insurance Day, 26/3/97.

[14] See para 2.7 above.

[15] The defences commonly relied on by insurers and to which such limitations might apply are set out at paras 14.29-14.41.

[16] See paras 14.10-14.12.

[17] See paras 14.13-14.14.

[18] See paras 14.15-14.18.

[19] See paras 14.19-14.25.

[20] See paras 14.29-14.41.

number of specific restrictions should apply to limit the ability of insurers to rely on such defences.

We seek consultees' views on whether any of the following or other restrictions should be used individually or cumulatively to limit the ability of insurers to rely on defences against third party claimants under an amended Act.

Restrictions which apply when the insurance cover is compulsory

14.10 In Part 11, we considered arguments for restricting the scope of the Act to risks covered by compulsory insurance. We suggested that such a restriction would have the advantage of providing additional rights only to third parties who had suffered as a result of activities which Parliament had decided should be covered by compulsory insurance.[21] Our provisional view was, however, that the Act should continue to apply to all liability insurance policies.

14.11 Limiting insurers' rights to rely on defences against third parties to cases where insurance is compulsory could cause confusion as some statutory schemes of compulsory insurance already prevent insurers from relying, as against third parties, on certain policy conditions.[22] To avoid such confusion, a list of compulsory insurance schemes,[23] to which the restrictive provisions in the amended Act applied, could be included in a schedule to the amended Act.[24]

14.12 Were insurers' rights to rely on defences to be restricted to cases where the risk insured was covered by compulsory insurance, consideration would also need to be given to the type of restriction which should apply. One option would be to put a blanket ban on insurers relying on all defences against third parties in such cases. Alternatively, the restriction on the ability of insurers to rely on defences in such cases could be combined with one or more of the restrictions set out below.

[21] See paras 11.12-11.14 above. Belgian law imposes greater restrictions on the ability of insurers to rely on defences against third parties where insurance is compulsory. See para 1.33 of Appendix F.

[22] Section 148(5) of the Road Traffic Act 1988 prohibits insurers from relying on breaches of condition by the insured after the date of the event giving rise to liability in respect of death, personal injury or property damage suffered by third parties up to £250,000. As we have seen, the Act also provides a specific procedure for third party claims. See para 1.12 above. Regulation 2 of the Employers' Liability (Compulsory Insurance) General Regulations 1971 prohibits conditions which state that employers can repudiate cover for breaches of notice of loss provisions, reasonable care clauses, obligations to comply with health and safety legislation and conditions relating to the keeping of records which occur after the employer has incurred liability to the employee. See para 5.11 above. Depending on the scope of any restrictions imposed by an amended 1930 Act, third party rights under such schemes might be supplemented. Were restrictions under an amended 1930 Act to be more limited in scope than those under existing schemes, we would not advocate limiting third party rights under such schemes.

[23] The list might include the Nuclear Installations Act 1965, the Riding Establishments Act 1964, the Dangerous Wild Animals Act 1976, the Solicitors Act 1974, the Credit Unions Act 1979 and the Estate Agents Act 1979. See para 11.14, n 25 above. As we have already noted, such a list is included in the Policyholders Protection Act 1975. See para 11.14, n 29 above.

[24] The schedule could be updated by statutory instrument as necessary.

Do consultees consider that restrictions should be placed on the ability of insurers to rely on defences against third party claimants under an amended Act only when insurance is compulsory? If so, what restrictions do they think should apply and what should those restrictions be?

Restrictions which apply when the third party's claim is of a particular type

14.13 In Part 11, we also sought consultees' views on whether the Act should only apply when a third party's claim was of a particular type. We discussed, for example, whether the Act should only apply when the third party's claim related to death or personal injury,[25] was in tort or delict rather than contract[26] or was a consumer claim.[27] Restrictions have already been placed on the enforcement of contractual rights against consumers by the Unfair Terms in Consumer Contracts Regulations 1994.[28]

14.14 We gave our provisional view that the applicability of the Act should not depend on the nature of the third party's claim. We now seek consultees' views on whether the same approach should be taken to restrictions on the ability of insurers to rely on defences against third parties.

Do consultees consider that restrictions should be placed on the ability of insurers to rely on defences where the third party's claim is of a particular type? If so, to what types of claim should the restrictions apply and what should those restrictions be?

Restrictions which apply after a certain point in time.

14.15 As we have seen, provisions in the Road Traffic Act 1988 and the Employers' Liability (Compulsory Insurance) General Regulations 1971 prevent insurers from relying on certain breaches of condition which occur after the date of the incident giving rise to the liability of the insured.[29] Employees bringing actions under the 1930 Act are already able to rely on these provisions.[30]

[25] See paras 11.15-11.16.

[26] See paras 11.19-11.20.

[27] See paras 11.17-11.18.

[28] SI 1994 No 3159, implementing European Council Directive 93/13/EC. The regulations allow the court to assess the fairness of an individual term in an insurance contract which does not define the insurer's obligations or determine the amount of the premium or the sum payable on loss.

[29] In some jurisdictions which provide third parties with a right of direct action against insurers, there is a general prohibition on insurers relying on such breaches. See, for example, article R124-1 of the French Insurance Code (see para 1.30 of Appendix F). Under Belgian law, insurers can rely on defences occurring prior to the incident giving rise to the liability of the insured if the insurance is non-compulsory but cannot rely on breaches, whenever they occurred, if the insurance is compulsory. See para 1.33 of Appendix F.

[30] See para 5.11 above. Third party claimants under the Road Traffic Act 1988 have a separate right of action against the insurers of insolvent insureds under that Act insofar as any

14.16 We have already set out our preliminary view that third parties should acquire rights under the Act once two events have occurred, the incident giving rise to the liability of the insured and one of the insolvency events set out in the Act.[31] We need now to consider whether, if this approach is taken, it is justifiable to restrict the contractual rights of insurers in relation to third party claims before third parties have acquired rights to proceed against them.

14.17 As we have already discussed, many policy conditions are as likely, or more likely, to be breached before the happening of one of the insolvency situations listed in the Act. Restricting the ability of insurers to rely on those breaches which occur after that point might be of limited benefit to third parties who, in most cases, will not be in a position themselves to ensure that policy conditions are met.

14.18 Another consideration is that restricting the ability of insurers to rely on defences after a certain point in time provides no incentive for the insured, officeholder or third parties to comply with policy conditions.[32] This may be the position even if such conditions could still be met and if the consequences of any breach are grave for the insurer.

Do consultees consider that the ability of insurers to rely on defences should be restricted by reference to the timing of the breaches on which those defences are based? If so, what should be the point in time after which breaches could not give rise to insurers' defences?[33]

Restrictions which depend on the consequences of the breach of duty or of policy terms

14.19 The issue of whether or not insurers should be permitted to rely on breaches which have not caused them prejudice is controversial and has been the subject of much debate.[34] Recommendations for general reform of the law in this area have not been implemented although the legal position is often tempered by insurance practice.[35] In this paper, we consider this issue only insofar as it relates to claims by third parties under the 1930 Act.

judgment which they obtain against the insured relates to compulsory risks. With regard to other risks, third parties can rely on the 1930 Act, see para 2.8 above.

31 See para 12.10. As we have already discussed, the Act's link with insolvency distinguishes it from many of the foreign schemes which we have examined.

32 We discuss at para 14.31 below whether or not insurers should be prevented from relying on notification defences under claims made policies.

33 Insurers could be prevented, for example, from relying on breaches which occurred after the incident giving rise to the liability of the insured or after the happening of one of the insolvency events set out in the Act.

34 See, for example, the reports of the Law Commission and the National Consumer Council, referred to at para 1.16 above. See also paras 5.17-5.31 above. We have already discussed the ability of insurers to insist on personal performance of policy conditions by the insured rather than the third party and gave our provisional conclusion at para 14.6 above that insurers should not be able to do this where the nature of conditions is such that they can be met by a third party claimant.

35 See, for example, para 5.62 above.

Safeguarding the interests of the insurer

14.20 We recognise that many policy conditions may be vital to the protection of the insurer. For example, those relating to notice, to the provision of information and assistance and those requiring the insured not to admit liability may be crucial to the ability of the insurer to investigate claims and to conduct the insured's defence. Those requiring the insured to abide by relevant health and safety regulations or to maintain minimum security arrangements may be key to limiting the risk to which the insurer agreed to expose himself on providing insurance cover.

The consequences of breach

14.21 A number of criteria have been used in other contexts in this country and in other jurisdictions to determine whether or not insurers should be entitled to rely on breaches of policy conditions.

14.22 An insurer may not be able to rely, for example, on a breach, unless it is causally related to the claimant's loss. The ABI Statement of General Insurance Practice provides that insurers should not rely on breaches of warranty or condition where "the circumstances of the loss are unconnected with the breach".[36]

14.23 The Insurance Ombudsman has sought to apply what is known as the principle of proportionality to determine whether a breach was sufficiently causative of the loss to justify the insurer making a total rather than a partial denial of cover.[37] In 1996, the Ombudsman commented as follows on the need to strike a balance between the interests of insurer and of insured:[38]

> 'Splitting it down the middle' works well in some insurance disputes, but I have to ensure that it does not become a cop-out from making a difficult decision in others ... . Something less than all will be quite unfair if the policyholder is entitled to his claim in full, or if the insurer has reasonable grounds for declining to make any payment whatsoever. Adopting a proportionate solution must involve no less an exercise of judgment than deciding one way or the other.

14.24 Assessing the degree of prejudice suffered by the insurer as a result of a breach may be difficult. Tests may be difficult to define and to apply to the facts of a

[36] See para 5.13 above. See also s 11 of the New Zealand Insurance Law Reform Act 1977 which prevents insurers from relying on breaches to exclude or limit liability "if the insured proves on the balance of probability that the loss in respect of which the insured seeks to be indemnified was not caused or contributed to by the happening of such events or the existence of such circumstances". The causal connection between breach and loss may be relevant, for example, to conditions relating to the duty to preserve insured assets, to abide by minimum standards or to hold certain licences or qualifications. See para 14.37 below.

[37] He has applied the principle to non-disclosure and misrepresentation (see Annual Report 1989, para 2.16-7), to the interplay of pre-existing medical conditions and accidental injuries in the case of personal accident policies (see Annual Report 1994, para 2.10), and of latent defects and storm damage in claims under household buildings policies, where the storm was required to be the "sole cause" of the loss, and to the entitlement of an employee returning only to "light duties" to policy benefits (Annual Report 1997, p 20).

[38] L Slade, Insurance Ombudsman 1994-6, The Insurance Ombudsman Bureau, Digest of Annual Reports and Bulletins, 1996, p 19.

particular case.[39] As we saw in our review of cases involving breaches of notice requirements, the English court has adopted a strict approach to such breaches, allowing insurers to rely on them even if they have suffered little or no prejudice. In some states in the USA, the insurer seeking to rely on certain policy breaches must prove significant prejudice.[40]

14.25 In Australia, the Insurance Contracts Act[41] prevents insurers from relying on a breach which is not capable of causing or contributing to the loss (of the insured) but they can reduce their liability proportionately to the prejudice which they were caused by that breach.[42] This approach avoids the "all or nothing" approach to prejudice which entitles the insurer to repudiate cover if it can show a certain degree of prejudice.[43] This approach appears to us to be fairer, although it might involve each side in expense as each seeks to prove its loss and to challenge the other's. It may be difficult in some cases to put a financial value on the prejudice caused to the insurer. The proportionality and causal connection tests contained in the Australian legislation have caused a degree of uncertainty and have been "the subject of much judicial consideration."[44] We have reached the tentative conclusion that if restrictions are to be placed on the ability of insurers to rely on defences, those restrictions should depend on the consequences of breaches of duty and/or

[39] See for example, the extensive caselaw on the applicability of the "prejudice" requirement in the context of dismissing cases for want of prosecution. The latest case in which a full statement of the principles is to be found is *Shtun v Zalejska* [1996] 1 WLR 1270. Of the specific types of policy conditions discussed below, prejudice to the insurer may only be relevant to those relating to notice, arbitration and to the provision of co-operation and assistance to the insurer.

[40] In *Home Indemnity Co v Finley*, 261 F Supp 318, 321 (Ark, 1966), the court held: "The burden of proving lack of co-operation of the insured is placed upon the insurer. Since the defence of lack of co-operation penalises the plaintiff for the action of the insured over whom he has no control, and since the defence frustrates the policy of this State that innocent victims of motor vehicles be recompensed for the injuries inflicted upon them, the courts have consistently held that the burden of proving the lack of co-operation is a heavy one indeed. Thus, the insurer must demonstrate that it acted diligently in seeking to bring about the insured's co-operation; and the attitude of the insured, after his co-operation was sought, was one of "wilful and avowed obstruction". In *Morales v National Grange Mutual Insurance Co*, 423 A 2d 325, 329 (NJ 1980) the court considered whether "substantial rights pertaining to a defence of a claim have been irretrievably lost" and "the likelihood of success of the insurer in defending against the accident victim's claim".

[41] Section 54, discussed at paras 1.7-1.8 of Appendix F. See also s 11 of the New Zealand Law Reform Act 1977, discussed at para 1.15 of Appendix F and at para 14.22, n 36 above.

[42] Note that section 54 differentiates, not between acts which do cause loss and those which do not, but between those which are capable of doing so and other acts.

[43] Comparisons can be made with a counterclaim in a damages action on the grounds of contributory negligence. On the question of where the onus lies in proving prejudice, it has been said of the Australian legislation that the burden "rests primarily on the insured but not to establish a negative proposition of the absence of prejudice. It is enough in itself without proof if that is a natural inference from the circumstances and the onus then shifts to the insurer to establish it by evidence rather than by conjecture through argument". See Derrington and Ashton, *The Law of Liability Insurance*, p 363, referring to *Findlay v Madill* (1980) 111 DLR (3d) 180.

[44] P Mann and C Lewis, *Annotated Insurance Contracts Act* (2nd ed 1997) p 133. See also Minter Ellison, *The Insurance Contracts Act 1984* (2nd ed 1996) p 70, where it is suggested that the distinction between acts which cause or contribute to loss "is conceptually difficult and may one day give rise to interesting questions of causation".

of policy terms and that insurers should not be able to rely on breaches which are neither connected to the third party's loss nor prejudicial to them.[45]

Do consultees consider that, if restrictions are to be placed on insurers' ability to rely on defences, those restrictions should depend on the consequences of the breach of duty and/or of policy terms? If so, do they agree with our tenative view that insurers should not be able to rely, as against third parties, on breaches unless they are both causative of the third party's loss and prejudicial to the insurer?

14.26 We have reached the provisional conclusion that if such restrictions were to be imposed, insurers should only be able to make deductions from the indemnity paid to third parties under the insurance policy proportionate to the extent that the breach was causative of the loss or to any prejudice to their interests.[46] We recognise that, in some cases, the deductions might reduce the amount recoverable to nil.[47]

Do consultees agree that, if such restrictions were to be imposed, insurers should only be entitled to reduce the indemnity proportionally to the extent that the breach was causative of the loss or to any prejudice to their interests?

14.27 Consideration needs to be given to whether the third party or the insurer should have the burden of proving the connection with the third party's loss and with any prejudice suffered by the insurer.[48] In our view, the third party should have the burden of proving the former and the insurer the latter.

Do consultees agree that, if such restrictions were to be imposed, the burden of proof for establishing that there was no connection between the breach and the loss should be on the third party[49] but that the burden of

[45] As we have seen, the approach taken by s 54 of the Australian Insurance Contracts Act is to differentiate between acts which can and cannot cause or contribute to the loss. See n 42 above. We have not adopted this approach, partly because of problems which the distinction might cause and partly because our approach echoes criteria already employed in the ABI Statement of Insurance Practice.

[46] The advantage of this approach would be that no test would have to be set down as to the degree of prejudice which the insurer would need to have suffered for his ability to rely on defences to arise: effectively, the insurer would have a duty to indemnify, subject to his right to deduct some or all of the indemnity, depending on the prejudice he had suffered as a result of the breach. This is similar to the approach adopted by the Insurance Ombudsman and in the Australian legislation.

[47] See para 14.23 above where we discuss the application by the Insurance Ombudsman of the principle of proportionality. See also paras 1.7-1.8 of Appendix F, where we discuss s 54 of the Australian Insurance Contracts Act 1982: in *Ferrcom Pty Ltd v Commercial Union Assurance Co of Australia Ltd* (1989) 5 ANZ Insurance Cas 60-907, it was held that, if the breach made the risk uninsurable, the claim would be reduced to nothing.

[48] See para 14.25 above.

[49] The third party could be required to show, for example, on the balance of probability, that the loss in respect of which he seeks an indemnity was not caused or contributed to by the breach. See s 11 of the New Zealand Insurance Law Reform Act 1977, referred to at n 36 above.

proof for establishing the prejudice suffered by the insurer should be on the insurer?[50]

Restrictions on insurers relying on certain types of defence or on breaches of certain policy terms

14.28 The restrictions set out above could be applied generally to all types of policy defence. Following on from our analysis in Part 5 of defences commonly relied on by insurers, we now consider whether particular defences should be subject to specific restrictions.

We seek consultees' views on whether the restrictions set out above or other restrictions should be applied to prevent insurers from relying on each of the following types of defence.

We also seek consultees' views on whether the specific restrictions set out below should apply to them and on whether other specific restrictions should apply to any other types of policy condition to which we have not referred.

Non-disclosure and misrepresentation

14.29 In most cases, defences based on non-disclosure and misrepresentation are likely to relate to the insured's general right to cover rather than to his right to an indemnity in respect of his liability to the third party. There have been a number of calls for a general review of the law in this area[51] and we do not think it appropriate to consider a narrow reform affecting only the 1930 Act.

Do consultees agree that it would be inappropriate to enact new law in the context of the 1930 Act alone restricting the ability of insurers to rely on non-disclosure and misrepresentation?

Notice requirements

14.30 It is our provisional view that insurers should not be permitted to defend a claim by a third party solely on the ground that a notice requirement has not been met by the insured where the third party can meet it.[52] Where neither the insured nor the third party has complied with such a requirement then insurers should not be able to rely on that breach unless it has prejudiced them and caused them loss.[53] Some degree of prejudice may be caused to insurers by any delay in their ability to investigate the case against the insured. The ABI Statement of General Practice provides that insurers should not rely on notice provisions, providing that notice is given "as soon as reasonably possible".[54]

[50] Cf the position under s 54 of the Australian Insurance Contracts Act. See para 14.25, n 45.

[51] See para 14.1 above.

[52] See para 14.3 above.

[53] See para 14.25 above.

[54] See para 5.31 above.

14.31 If restrictions are placed on the ability of insurers to rely on breaches of notice requirements, consideration needs to be given to whether those restrictions should extend to insurers under claims made policies. A failure to give notice within the prescribed time may mean that notification is not made within the policy's claim period. It could be argued, however, that to make insurers liable to third parties under claims made policies in respect of claims made outside the claims period would undermine the basis of the insurance cover, not merely their ability to rely on specific policy conditions.[55]

We seek consultees' views on whether insurers should be prevented from relying on breaches of notice requirements in claims made policies where late notification would bring the claim outside the claims period.[56]

Arbitration clauses[57]

14.32 Particular procedural considerations apply to arbitration clauses. As we have seen, third parties, as well as the insured whose rights they acquire under the Act, are bound by arbitration clauses in the insurance contract.[58] This is so even if they cannot afford the expense of arbitration proceedings, for which they will not be entitled to legal aid.[59] As we have seen, there is judicial support for amending the Act to prevent insurers from enforcing arbitration clauses in such cases.[60]

14.33 Some commercial insurers see arbitration clauses as vital to the cover which they provide.[61] One of the main aims of the Arbitration Act 1996, which applies to England and Wales, was to ensure that, where parties had chosen to include an arbitration clause in the contract between them, they should be bound by that agreement. This is also an established principle of Scottish law.[62]

[55] This argument, used to challenge reliance by an insured on s 54 of the Australian Insurance Contracts Act 1984, was rejected by the New South Wales Court of Appeal in *East End Real Estate Pty Ltd v C E Heath Casualty and General Insurance Ltd* (1992) 25 NSWLR 400. Consideration would also need to be given to whether such a right would only apply if there was no new insurer providing cover in respect of the claims period in which the third party' s claim was made. Otherwise, two insurers might be potentially liable for the same claim.

[56] Depending on the nature of restrictions placed on insurers under an amended Act, the claim could, for example, be deemed to have been made within the claims period, but insurers be permitted to rely on the delay in claiming they had suffered prejudice as a result of the breach. See paras 14.25-14.26 above.

[57] We discuss in Part 17 whether third parties can or should be able to substitute themselves in arbitration proceedings started by the insured against the insurer to avoid limitation problems.

[58] Although such clauses may be merely "an incident of the right to an indemnity". See Saville J in *Edwards v Minster Insurance Co Ltd* (unreported) 10 March 1994. See para 5.52-5.54 above.

[59] See para 5.41 above.

[60] See para 5.44 above.

[61] For example, the rules of Protection and Indemnity Clubs invariably make submission to arbitration a condition precedent to the right of members to bring legal action against a Club and usually insist that such a submission is made.

[62] *Sanderson and Son v Armour and Co Ltd* 1922 SC(HL) 177.

14.34 We need to consider whether the enforcement of arbitration clauses by insurers against third parties is a problem in practice. We have already noted that, following proposals by the ABI in the 1950s, most insurers do not enforce arbitration clauses against consumer claimants. It is possible that such clauses may also be challenged under the Unfair Terms in Consumer Contracts Regulations.[63]

14.35 Following amendment to the 1996 Act, it appears that the court's discretion to grant a stay of legal proceedings will be removed, unless the arbitration agreement is null and void, inoperative or incapable of being performed.[64] It appears, therefore, that allowing the court a discretion to refuse to grant a stay of legal proceedings brought by third party claimants under the Act where such a clause exists[65] is no longer available. Instead, any reform of the 1930 Act would have to make arbitration clauses null and void against third party claimants under the Act. Consultees may consider that such a reform would be contrary to the general philosophy of the Arbitration Act and would not be justified, given that, in many cases, arbitration clauses may not be enforced against third party claimants.[66]

We seek consultees' views on the extent to which insurers' reliance on arbitration clauses causes problems to third party claimants under the Act.

Consultees' views are also sought on whether arbitration clauses in insurance contracts should be unenforceable against third party claimants or certain types of claimant under the Act.

Duty to co-operate and provide assistance[67]

14.36 As such conditions and similar conditions such as those requiring the insured not to admit liability to claimants or to provide them with any assistance may be vital to the insurer's ability to conduct the insured's defence, it may be easy in most

[63] See para 5.35 above.

[64] Section 9 of the 1996 Act. See para 5.49 above.

[65] As was discussed, for example, by the court in *Smith v Pearl Assurance Co Ltd* [1939] 1 All ER 95 and in *Fakes v Taylor Woodrow Construction Ltd* [1973] 1 QB 436. See paras 5.42-5.48 above.

[66] The National Consumer Council has recommended that clauses providing for mandatory arbitration for disputes about liability or the amount of a claim should be made void (National Consumer Council Report, Insurance Law Reform, recommendation 9, p 7 and p 53) pointing out that the Consumer Arbitration Agreements Act 1988 (which does not apply to insurance contracts) generally prohibits arbitration clauses in consumer contracts. The ABI's response is that "ABI member insurers agreed many years ago to remove mandatory arbitration clauses from personal lines insurance contracts. In the UK, arbitration is rarely, probably never, imposed upon the individual personal lines insurance policyholder. Instead, the insurance industry's own ADR initiative, the Insurance Ombudsman Bureau, has proved extremely successful and comprehensive". See para 7.2 of Insurance Law Reform: the Response of the ABI to the NCC Report, July 1997. Arbitration clauses are avoided by s 43 of the Australian Insurance Contracts Act 1984.

[67] We discuss the operation of such clauses at paras 5.51-5.54 above.

cases for the insurer to show that he has suffered prejudice as a result of a breach. In other cases, there may be no link between the breach and the loss suffered.[68]

Conditions relating to the duty of the insured to preserve the assets/business insured (for example to maintain security).[69]

14.37 Again, the breach may or may not be connected to the loss and the insurer may or may not be able to show that the breach caused him prejudice.

Conditions relating to the ability of the insured to pay[70]

14.38 The conditions in insurance contracts relating to the insured's duty to pay are fundamental to the insurer's agreement to provide insurance cover. Third parties may be dismayed to find the amount of any sum they recover under the 1930 Act reduced because of a condition in the insurance contract setting out an "excess" to be paid by the insured in respect of each claim. However, this is a consequence of their acquiring the rights of the insured under the Act.[71]

14.39 Whereas it is reasonable for the third party's claim to be subject to payment conditions which relate to that particular claim, it may not reasonable for the claim also to be subject to conditions which affect the general relationship between the insurer and the insured. For example, a condition allowing the insurer to deduct unpaid premiums from sums recovered would relate to all potential claims, not to the specific claim brought by the third party. In *Murray v Legal and General Assurance Society Ltd*,[72] it was suggested, however, that insurers might be able to rely on terms allowing them to deduct unpaid premiums from individual claims if such terms were expressed to be conditions precedent.[73]As we have already suggested, the payment of premiums is fundamental to the insurer's agreement to provide cover.

We seek consultees' views on whether insurers should be permitted to deduct unpaid premiums from amounts recovered by a third party under the Act.[74]

14.40 As we have seen, the validity of pay first clauses,[75] requiring the insured to have paid the third party's claim before being entitled to an indemnity from the

[68] In a US case, *Home Indemnity Co v Finley*, 261 F Supp 318, 321 (Ark, 1966), the court held that an insurer seeking to rely on a breach of conditions relating to the duty to assist might have to show that he "acted diligently in seeking to bring about the insured's co-operation".

[69] Policy conditions may also require the insured to hold a particular licence or to have a particular qualification.

[70] Such conditions are discussed at paras 5.56-5.63 above.

[71] See however in relation to employer's liability insurance para 5.11, n 17 above.

[72] [1970] 2 QB 495.

[73] Although the court held that this was not so in that case.

[74] We suggest at para 14.42 that the insurer should have a right of indemnity against the insured to recover any sums which he has paid to a third party because of restrictions imposed by the 1930 Act.

[75] Used principally in the rules of P&I Clubs. See para 5.58 above.

insurance, was upheld by the House of Lords in *The Fanti*.[76] Such clauses will, therefore, bar recovery by third parties under the Act. The House of Lords stressed the commercial reasons for the use of such clauses and appeared to take comfort from the practice of most Clubs not to rely on such clauses against third parties bringing claims for death or personal injury.[77]

14.41 It has been questioned whether there continues to be a commercial justification for the use of such clauses and whether voluntary practices are adequate protection for third parties.[78] Because of the particular nature of the cover provided by Clubs, we have not, however, formed a provisional conclusion on the use of such clauses.

We seek consultees' views on whether insurers should be permitted to rely, as against third party claimants under the Act, on pay to be paid clauses.

AN INSURER'S RIGHT TO AN INDEMNITY FROM THE INSURED

14.42 If the insurer is prevented from relying, as against third parties, on certain defences which he could have invoked against the insured, he should have a right of recourse against the insured's assets to recover any sums which he has paid to the third party because of his inability to rely on those defences. We suspect that, in most cases, insurers are unlikely to wish to proceed against an insolvent insured as they are unlikely to recover much from him. However, where they wish to do so, it appears to us that insurers should be entitled to an indemnity from the insured to compensate the insurer for the loss of a benefit to which the insurer was entitled under the insurance contract.[79] The insurer would have a provable claim in the insured's insolvency.

Do consultees agree that any right to an indemnity which insurers might have against the insured in cases where they have been prevented by the Act from relying, against third parties, on defences which they could have invoked against the insured is unlikely to be of much practical assistance to insurers in most cases?

[76] [1991] 2 AC 1.

[77] See para 5.62 above. The House of Lords rejected the argument that such clauses breached the Act's anti-avoidance provisions. See para 5.61 above.

[78] See para 5.58 above. One of the main reasons for the introduction of the Louisiana direct action statute was the inclusion of "no action" clauses allowing insurers to indemnify the insured only after it had paid the injured party. "No action" clauses are prohibited in many states in the US.

[79] Cf section 1(4) of the Act which preserves residual rights of recourse for third parties and for the insured. Under the Belgian law of 25/6/92, an insurer is able to recover from the insured sums he has paid to the third party which he could have refused to pay to the insured under the insurance contract. The insurer has a similar right under French law. See paras 1.31,
n 58 and 1.34 of Appendix F.

Do consultees consider that such a right should be included in an amended Act in any event?[80]

[80] It is possible that, in some instances, insurers will be contractually entitled to recover such sums from the insured under the insurance contract.

PART 15
THE DISTRIBUTION OF A LIMITED INSURANCE FUND TO MULTIPLE CLAIMANTS

15.1 In Part 7 we considered the implications of the Court of Appeal's decision in *Cox v Bankside*[1] that, where there are multiple claimants against a limited insurance fund, the fund should be distributed to those who establish their claims first rather than rateably to all claimants. Some commentators who have claimed that this "first past the post" system leads to the unequal treatment of third party claimants have suggested that it should be replaced by a statutory scheme of rateable distribution. Others have suggested that the introduction of such a scheme is not justifiable as problems such as those which arose in *Cox v Bankside* arise very rarely. The problem of the distribution of a limited insurance fund to multiple claimants is not limited to cases involving the 1930 Act but we consider, in this Part, how such a scheme might operate.

Consultees are asked to inform us whether or not they have had experience of problems caused by the "first past the post" principle in the context of claims under the 1930 Act (other than in the Lloyd's litigation).

DISCLOSURE OF PRIOR SETTLEMENTS AND JUDGMENTS AND OF THE LEVEL OF REMAINING INSURANCE COVER

15.2 In most cases involving the 1930 Act, the insured's insurance cover will be adequate to meet all claims. If the cover is inadequate, this may be obvious from an early stage or only after one or more judgments have been obtained by third parties. As the law now stands, third parties can only guess if the remaining cover is adequate to cover their claims as the insurer has no duty to inform them of this.[2] We have already given our provisional view that insurers should have a continuing duty to disclose the value of outstanding cover to third parties.[3] This would improve the position of claimants under the existing law and protect their rights under any new statutory scheme.[4]

POSSIBLE SCHEMES UNDER CURRENT LAW

15.3 Before considering how a statutory scheme of rateable distribution, and variations on such a scheme, might operate, we consider briefly whether a scheme could be

[1] [1995] 2 Lloyd's Rep 437.

[2] See our discussion of the interlocutory application for disclosure in *Cox v Bankside* [1995] 2 Lloyd's Rep 437 at paras 6.15-6.16 above.

[3] See para 13.13 above.

[4] We discuss, at paras 15.6-15.18 below, how such a scheme might operate.

introduced based on the existing powers of the court to give simultaneous judgment in a number of cases or to consolidate actions.[5]

The court's power to give simultaneous judgment

15.4 We have already mentioned that the court is reluctant to exercise any existing power which it may have to give simultaneous judgments. A scheme based on an express court power to do so in cases under the 1930 Act might not be welcomed by the court and would not be workable in cases where the number of potential claimants was unknown.

A court imposed representative action or consolidation of actions

15.5 Another option might be for third parties to be required to proceed by way of a representative action or to consolidate their actions.[6] This would be inappropriate,[7] however, where the third parties' claims arose out of different events, involved different allegations and were subject to different defences.[8] In England and Wales, third parties might choose to bring representative proceedings in any event in cases where group actions were appropriate (for example where the third parties were all victims of a disaster).[9]

Do consultees consider that the court's existing powers are adequate to impose a scheme of rateable distribution on claimants under the Act? If not, do they consider that the court should be provided with additional procedural powers? What additional powers do they consider the court should have?[10]

HOW MIGHT A STATUTORY SCHEME OF RATEABLE DISTRIBUTION OPERATE?

15.6 We consider that the only feasible statutory scheme would be one based on the administration of sums payable under the insurance policy by the court, a court appointed receiver or, possibly, by the insured's insolvency practitioner. We consider how such a scheme would be triggered, who could administer it, how it would be administered and what problems it might cause.

[5] See also paras 7.5-7.9 above where we suggested that, following the Court of Appeal's decision in *Cox v Bankside* [1995] 2 Lloyd's Rep 437, 459 any scheme would have to be introduced legislatively as the court may be reluctant to use existing powers which it might have. Having summarised the issues which might need to be dealt with by a non-statutory scheme, the Master of the Rolls concluded that the scheme "would have to do all this without the authority of any statute or subordinate legislation". See para 7.9 above. See also Sir Jonathan Mance "Insolvency at Sea" [1995] LMCLQ 34.

[6] RSC O 15, r 6 and O 4 set out in Appendix B. See paras 7.18-7.20 above.

[7] And impossible under the rules of court. See RSC O 15, r 6 (CCR O 5, r 4).

[8] Their claims might also be covered by different insurance policies.

[9] Following the Woolf reforms such claims are likely to be managed by MPS schemes. See para 7.20, n 26 above. In Scotland, there are no special procedures for group actions. The Scottish Law Commission has made recommendations in its Report on Multi-Party Actions, Scot Law Com No 154 which are under consideration by the Government.

[10] For example, should they have additional powers to synchronise judgments or to consolidate actions?

How would the scheme be triggered?

15.7 The circumstances in which the insurance fund might be fed into the scheme might vary greatly. In some cases, it will be clear that third party claims exceed the available insurance cover and that the insurer is liable to pay under the policy. It might be appropriate for the insurer in such cases to be allowed to pay the entire insurance fund over to be administered under the statutory scheme.[11] This would limit the insurer's exposure to legal costs and be of benefit to claimants as such costs are usually deductible from the sums recovered.

15.8 Insurers and prior claimants would want to ensure that any payments made (following settlement or judgment) prior to the scheme being triggered were not open to challenge by subsequent claimants. In our view, the interests of insurers and prior claimants should be protected in this way and settlement encouraged but only if the insurer has a duty to disclose the fact that such settlements have been reached (or judgments obtained) to other third parties of whose claims he is aware[12] and if those third parties had an opportunity to apply for any payments made or to be made by the insurer to be caught by the statutory scheme.[13] One option might be that the insurer should not pay such sums over until a certain period after disclosure of this information had been given to other claimants, during which period they would have an opportunity to apply to court to trigger the statutory scheme.

15.9 Third parties would need to be able to trigger the scheme by making an application to court. Their application might be for an order requiring any sums due to a third party who had already obtained judgment or who was about to do so to be paid into a fund to be administered under the scheme or for a stay of execution pending the resolution of other claims.[14] Provision would need to be made for subsequent amounts recovered to be paid into the same fund.[15] The court would have to be satisfied that there was some basis for the third party's claim before making an order, the effect of which would be to deprive the third party who had obtained judgment of the immediate benefit of that judgment.

[11] Although this might cause problems if arguments arose between claimants as to the ratio of their shares and as to what the value of any judgment against the insurer was likely to have been. We discuss at para 15.16 below the problems which might be caused by the need to ascertain and value third party claims under a statutory scheme.

[12] We set out our provisional view at paras 13.5 and 13.13 above that disclosing parties should have a continuing duty to disclose decreases in the value of the insurance fund. Unidentified third parties would obviously miss this opportunity as they would not be given this information.

[13] We do not believe, however, that third parties should be able to "claw back" sums paid out before the happening of one of the insolvency situations set out in the Act. See our discussion in Part 12 of when rights should transfer under the Act.

[14] As we have already suggested, if it was clear before any sums were paid out that the insurance fund would be inadequate to pay all claims and that the insurer was liable, the insurer might agree to pay over the fund at that stage. See para 15.7 above.

[15] As well as for the treatment of sums which had been paid to third parties before the scheme was triggered. See para 15.15 below.

Who could administer the scheme?

15.10 Those who could administer a scheme of rateable distribution are the court, a court appointee or, possibly, the insured's insolvency practitioner.[16] The insurance fund could be paid into court and payments made following applications for directions and interim payments.[17] If the identity of claimants were known, it might be appropriate for the court to administer such schemes. Otherwise, the court could have the power to order that the scheme be administered by the insured's insolvency practitioner or, if he was not prepared to do so, by a receiver appointed by the court. In any statutory scheme, the court would probably be required to give directions as disputes would be likely to arise between third party claimants, for example, as to the value of their claims and their entitlement to interim payments.[18] The balance of any unpaid claims would be unsecured claims in the insolvency proceedings.

15.11 Where an insolvency practitioner has already been appointed, there would be obvious advantages were the existing officer to administer the day to day management of any scheme of rateable distribution under the Act. The insolvency practitioner would be in a position to establish the existence and the value of third party claims against the insured and have the skills and experience necessary to organise a rateable distribution of the insurance fund. As we have already discussed, however, insolvency practitioners may have conflicting interests which might prevent them from undertaking such a role.[19]

15.12 An insolvency practitioner could only be expected to undertake the administration of such a scheme if payment of his fees and costs (which might be substantial) could be guaranteed from the scheme. Whereas he is able to establish the value of the insured's assets in the main insolvency, he will not know how much, or indeed if any, sums payable under the insured's insurance policies will be recovered by third parties under the Act.

[16] In theory, the insurer could manage the scheme himself, but is unlikely to want to do this, nor to have the necessary skills. Nor will he have any particular interest in ensuring that there is a fair distribution. The costs of managing the scheme may be high and would be deducted before any proceeds were paid out. In Germany, however, the insurer has a duty under para 156(3) of the VVG (the Insurance Contract Act 1908) to organise a pro rata distribution to claimants in such cases.

[17] Or the court could appoint a receiver or judicial factor to recover sums. See s 61 of the Financial Services Act 1986, which provides that the court, on the application of the Secretary of State, may grant injunctions or interdicts and require those contravening certain provisions of that Act to pay sums into court. Section 61(6) provides that "Any amount paid into court by or recovered from a person in pursuance of an order ... shall be paid out to such person or persons appearing to the court to have entered into transaction with that person as a result of which the profits ... have accrued to him or the loss or adverse effect ... has been suffered".

[18] In Canada, s 96(3) of the Insurance Act provides that in all actions where several persons are interested in insurance proceeds, the court may apportion the proceeds among the persons entitled to it and give all necessary directions and relief. See para 1.38, Appendix F.

[19] Particularly if their fees and costs were not paid from the insurance fund but fell to be met by the insured's other creditors. See para 6.9 above. Also, this option would not be appropriate where the officeholder bound by the Act was, for example, a receiver.

How would the scheme be administered?

15.13 As under the Insolvency Act 1986, there would need to be a statutory order of priority for the payment of monies to be distributed under the scheme. For example, the costs of administering the scheme would have to be deducted first. Were the scheme to be triggered following a successful action by one or more third parties, provision might also need to be made for the costs of those third parties to be met before the fund was distributed.

15.14 A statutory scheme modelled on the insolvency regime would treat all outstanding claims equally, so that they crystallised on the happening of one of the insolvency situations set out in the Act. Another option would be to provide for distribution to be made by reference to the order of the dates of the events giving rise to liability.[20] Provision might also need to be made for interim payments to be made to claimants. The balance of any unpaid claims would be an unsecured claim in the insolvency proceedings.

15.15 As we have already discussed,[21] another issue which would need to be dealt with by the scheme would be whether sums paid out by insurers to third parties before the scheme was triggered should be clawed back for distribution to all claimants under the scheme. We take the view that such payments should not be clawed back. However, in the case of payments made after the happening of one of the insolvency situations, third parties should have an opportunity to trigger the operation of the scheme.[22]

The problems which a scheme of rateable distribution might cause

15.16 A number of problems might arise were a statutory scheme of rateable distribution to be introduced. First, the existence of potential claims would have to be established and provision made for the class of claimants to be closed.[23] It may be difficult or impossible to ascertain possible long-tail claims. The value of each claimant's claim (and of his "share" in the fund) may be difficult to determine, particularly if the insured (and the insurer) had raised defences based, for example,

[20] In Australia, where there are two or more claims, the order of precedence is the order of the dates of the events giving rise to liability, but where several claims arose on the same date, they rank pari passu: Section 25(3) Insurance Contracts Act. See also s 6(3) of the New South Wales Law Reform (Miscellaneous Provisions) Act 1946, s 25(3) of the Australian Capital Territory legislation and s 9(3) of the New Zealand Law Reform Act 1935. Some commentators have suggested that such provisions have "the potential to operate unfairly by denying claimants in leading actions, who pursue those actions diligently and take a significant financial risk, the prospect of a full reward for their efforts". See Drummond and Mann, "Abolish section 6" Insurance Law Journal, April 1997, vol 8 no 2.

[21] See para 15.8.

[22] See para 15.9 above.

[23] The way in which potential third party claimants should be notified is likely to vary from case to case. Often, the insured will be aware of the identity of most potential claimants so they should not be too difficult to locate. In some cases, it might be appropriate for notices to appear in newspapers or specialist publications. It might be necessary for the class of claimants to close after a certain period of time, but this period is likely to vary from case to case and may depend on the number of potential claimants. The Lord Chancellor's Department has canvassed the issue of cut-off dates in a consultation paper, *Access to Justice, Multi-Party Situations: Proposed New Procedures*, paras 35-38.

on contributory negligence by the third party. Claimants may dispute values allotted to their claims and they, or the insolvency practitioner, may seek to have issues resolved by the court. Any proper resolution of the value of claims might involve a mini-trial of the issues which would have been raised had the third party proceeded with his case against the insurer.

15.17 Although the insured's insolvency practitioner will ascertain potential claims in the main insolvency, there are likely to be different class closing rules and dates for the third party scheme. A scheme involving the ascertaining and valuation of potential claims is likely to cause delay, both to distribution under the 1930 Act and under the main insolvency, as the insolvency practitioner will not be able to make full distribution until he knows if there are any outstanding claims under the 1930 Act which can be advanced against the insured.

OUR PROVISIONAL VIEWS

15.18 We have not reached any provisional conclusions on whether the first past the post system should be replaced by a statutory scheme of rateable distribution. We appreciate that the current system leads to the unequal treatment of third parties but are concerned that a statutory scheme of distribution might lead to greater uncertainty and complexity.[24]

(i) Do consultees consider that a new statutory scheme of rateable distribution should be introduced

(ii) If so, we should be grateful for their views on the following scheme and on any other scheme which they think should be introduced.

We suggest that any new statutory scheme should work in the following way:-

> **(a) the scheme would be triggered following an application to the court by a third party[25] or by the insurer;[26]**
>
> **(b) the court should decide how the fund should be administered. Depending on the circumstances of the case,[27] the**

[24] The problems of schemes of rateable distribution have been discussed in other contexts. See, with regard to awards of punitive damages to multiple claimants**,** Law Commission report: Aggravated, Exemplary and Restitutionary Damages Law Com No 247 and *Riches v News Group Newspapers* [1986] QB 256. With regard to the sale of goods in bulk, see Sale of Goods Forming Part of a Bulk Law Com No 215; Scot Law Com No 145, 1993, p 26, where the Law Commission and the Scottish Law Commission considered whether a statutory adjustment scheme should be introduced, requiring a buyer who received excess goods out of a bulk to pay other buyers a proportionate amount of the value of the excess. One of the reasons for not recommending such a scheme was that it would be difficult to operate and that the "increase in the complexity of the law might not, in practice, be balanced by a corresponding increase in justice".

[25] Or third parties.

[26] This could be before or after some payments had been made from the insurance fund.

[27] Eg if all potential claimants had been identified and if the insolvency situation governed by the Act is a bankruptcy or winding up rather than a receivership.

court might order sums payable under the insurance contract[28] to be paid into court, to a court appointee or, in appropriate cases,[29] to the insured's insolvency practitioner;

(c) the scheme would provide for the costs of the court, the court appointee or the insolvency practitioner to be deducted before any distribution was made to third party claimants. In appropriate cases, it would also provide for the costs of the third party triggering the scheme to be deducted prior to distribution. The scheme would provide for interim payments to be made and, if possible, for the value of outstanding claims to be assessed and appropriate "shares" in the fund determined, without further recourse to litigation.

[28] Ie those payable in respect of a particular judgment and those payable in any future cases. The insurer may choose to pay the entire sum over to be administered under the scheme.

[29] See para 15.11 above.

PART 16
PRIVATE INTERNATIONAL LAW

16.1 In Part 8, we suggested that it is uncertain when the Act will apply to cases with a foreign element. We consider in this Part whether the Act should be amended to clarify the position and whether the jurisdiction of UK courts to hear claims under the Act should be widened.

SHOULD THE ACT'S PROVISIONS ADDRESS PRIVATE INTERNATIONAL LAW ISSUES?[1]

16.2 We suggest that cases raising questions as to the applicability of the Act may arise more frequently as cross border insurance increases.[2] We also suggest that amending the Act so that its provisions addressed private international law issues would avoid disputes over the applicability of the Act and whether different rules should apply to different rights transferred under the Act.[3]

Do consultees agree with our provisional conclusion that the private international law aspects of the Act should be clarified or do they think that such matters should be left to the court?

WHAT CRITERIA SHOULD DETERMINE THE APPLICABILITY OF THE ACT?

16.3 We consider a number of criteria which could be used to determine the applicability of the Act to cases with a foreign element. Whatever criteria are used, the ability of a third party to rely on the Act will depend on both its applicability and on whether or not the court in which he is proceeding has jurisdiction over the insurer.[4] We consider whether the fact that a UK court has jurisdiction over the insurer should itself be the criterion for the applicability of the Act or whether its applicability should depend on other factors.

The insured has been declared bankrupt or wound up in this country

16.4 The current focus of the 1930 Act is insolvency and we have given our provisional view that it should continue to be so.[5] If this is the case, it would be consistent with

[1] Although statutes do not usually state their territorial basis of application, some do. See s 72 Bills of Exchange Act 1882, s 27 Unfair Contract Terms Act 1977 and s 153(5) of the Employment Protection (Consolidation) Act 1978. These provisions were referred to by Staughton LJ in *The Irish Rowan* [1991] 2 QB 206. See paras 8.4-8.5 above.

[2] And were the EU Convention on Insolvency Proceedings ever to come into force. Cf the position in 1990 when the Law Commissions rejected the need for statutory clarification of what principles should govern direct action statutes on the basis that the issue "is of hardly any practical importance, there being no reported case in England or Scotland". See para 3.51 of Law Com No 193 and Scot Law Com No 129 on Private International Law Choice of Law in Tort and Delict.

[3] As we have seen, Staughton LJ in *The Irish Rowan* suggested that different criteria might apply to the rights transferred under ss 1 and 2. See para 8.8 above.

[4] We concentrate on the ability of a third party to bring proceedings against an insurer in a UK court.

[5] See para 12.10 above.

the scheme of the Act to allow third parties to rely on it if the insured has been declared bankrupt or wound up within the jurisdiction.[6] As we have seen, the power of the court in England and Wales to grant winding up and bankruptcy orders against foreign insureds is wide.[7]

16.5 Were the applicability of the Act to depend on whether the insured had been declared bankrupt or wound up in the UK, the court might be more likely to decide that actions under it fell outside the Brussels Convention which does not apply to "bankruptcy, proceedings relating to the winding-up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings."[8] If so, third parties seeking to rely on the Act would have to show that the insurer could be served with a writ and made a defendant to proceedings before the English court under RSC Order 11, rule 1.[9] In Scotland, a court cannot acquire jurisdiction by service of a writ abroad.[10]

The insurance proceeds are payable in this country

16.6 The fact that insurance proceeds are payable in England may be an important factor in the court's decision to grant a bankruptcy or winding up petition against a foreign company which has no other assets in the jurisdiction. Staughton LJ suggested in *The Irish Rowan* that this fact might itself be sufficient for the Act to apply in a particular case. It is doubtful whether Scottish courts have a similar jurisdiction.[11]

[6] Sir Jonathan Mance has suggested that allowing the proper law of the insurance contract to govern this issue, the approach taken by Dicey and Morris *The Conflict of Laws*, is "inappropriate in the context of a statute designed to remove a palpable injustice resulting from the rules of pari passu distribution of assets in English bankruptcy and winding up. Dicey & Morris' views make sense where the only question is whether a third party can claim direct against an insurer, in the absence of any issue of insolvency. Under the laws of many of the United States, third parties can of course do this. The focus of the 1930 Act's operation is insolvency not contract". See Sir Jonathan Mance "Insolvency at Sea" [1995] LMCLQ 35, at 52.

[7] Its power to grant such orders might be narrowed were the European Insolvency Convention ever to come into force. The Convention, which provides for the recognition by Convention states of insolvency proceedings in other Convention states, was approved by the Council of Ministers in 1995 but was not ratified by the UK during the period when it was open for signature. We are not aware of any current plans to revive it, although this cannot be ruled out. The scheme of the draft Convention is discussed briefly in Appendix A.

[8] Article 1(2). See para 8.23 above.

[9] See paras 16.14-16.18 below.

[10] *Lord Advocate v Tursi* 1997 SCLR 264.

[11] See para 8.16 above.

The courts have jurisdiction in respect of the tort or delict or breach of contract committed by the insured

16.7 This approach has also been supported, on the basis that the third party's right of action under the Act is merely an extension of his main cause of action against the insured.[12]

The law applicable to the insurance contract is English or Scottish law

16.8 This approach has been supported by a number of commentators, including Dicey and Morris.[13] Staughton LJ in *The Irish Rowan*,[14] suggested that there was "a substantial argument against the proper law of the contract being the connecting factor" as section 1(3) of the Act was designed to override the contract of the parties and the intention of Parliament could be frustrated "if it were open to the parties to a contract of insurance to exclude the operation of section 1 by choosing a foreign proper law ...". In our view, it is unlikely that the applicability of the 1930 Act to any future disputes with third parties will lead parties not to make English or Scottish law the law of the insurance contract as other factors are more likely to dictate their choice of law.[15]

16.9 Whatever criteria are used to determine the applicability of the Act, it is necessary to consider whether the provisions of the Act should override the rights and obligations of the insurer, the insured and the third party under the law applicable to the insurance contract, if its provisions were different from those of the Act.

16.10 We suggest that it would be inappropriate for the provisions of the 1930 Act to interfere with the provisions of the law applicable to the insurance contract. We see

[12] The Law Commissions' report on Private International Law Choice of Law in Tort and Delict, published in 1990, Law Com No 193, Scot Law Com No 129, p 26 considered the applicability of the 1930 Act and concluded: "The direct action is not in any real sense contractual, since the claimant is not suing a party with whom he is in privity of contract. It is true that neither has a wrong been perpetrated by the insurer on the claimant. However, the action against the wrongdoer's insurer may be more akin to a claim in tort than contract, since what would normally be the claimant's primary remedy would be a tortious action against the wrongdoer. If the claimant's action against the actual wrongdoer would be tortious, an action against the insurer may be better seen as an extension of this tortious action. Although the direct action cannot exist in the absence of the contract of insurance, neither would the direct action exist in the absence of any wrongdoing. While to apply a law other than the law of the insurance contract would expose the insurer to a liability greater than he contemplated, nevertheless, depending on where the insurer carries on his activities, his expectations might reasonably be expected to include not only the potential liability of the insured under the law of that jurisdiction to which cover extends, but also any potential direct liability". The Law Commissions' proposals on the applicable law which should govern the determination of cases relating to tort or delict with a foreign element were broadly implemented by the Private International Law (Miscellaneous Provisions) Act 1995 but, in line with a Law Commissions' recommendation, the implementing legislation did not contain provision for direct actions.

[13] See Dicey and Morris *The Conflict of Laws*. This approach has been taken in a number of Australian cases. See, for example, *Plozza v South Australian Insurance Company Ltd* [1963] SASR 122.

[14] [1991] 2 QB 206. See paras 8.4-8.5 above.

[15] Third party rights against insurers may be wider under the law of other jurisdictions, in any event.

some justification, however, in the argument that once the insurer is liable to provide an indemnity, it should be irrelevant to him to whom the indemnity is payable. So that if the only difference between the Act's provisions and those of the law applicable to the insurance contract is that the Act gives the third party the right to sue the insurer then the Act should prevail.

16.11 Some of our provisional recommendations might cause problems, however. For example, we have suggested that third parties should be allowed to meet certain policy conditions which had not been met by the insured and that insurers should be able to seek an indemnity from the insured if they are required to pay sums to a third party which they would not have been required to pay to the insured under the insurance contract.[16] These rights may not be available in the law applicable to the insurance contract.

16.12 Whether or not third parties proceeding before a UK court sought to argue[17] that the 1930 Act or the law governing the insurance contract was the applicable law would depend on which law gave them greater rights.[18] The 1930 Act and the governing law might each under its own provisions be applicable.

16.13 Consultees may consider that the rights and obligations of the insurer, the insured and the third party under the law governing the insurance contract should not be overridden by the 1930 Act. If so, this might favour making the fact that the insurance contract is governed by English or Scottish law the criterion determining the applicability of the 1930 Act.

The insurer is subject to the jurisdiction of a UK court[19]

16.14 We discussed in Part 8 the circumstances in which a UK court will have jurisdiction over claims against insurers, whether under the Brussels Convention or otherwise. We have already suggested that claims under the 1930 Act may be treated as falling outside the Brussels Convention, in which case third parties would need to seek leave to serve the insurer out of the jurisdiction under RSC Order 11, rule 1.[20]

16.15 As we have already discussed, problems might arise were the UK court to have jurisdiction but one or other of the parties to claim that the law of another

[16] See paras 14.6 and 14.42 above.

[17] And insurers to challenge.

[18] At para 16.15 below, we note that the UK courts apply foreign applicable law in appropriate cases.

[19] Allowing only third parties domiciled in the UK to rely on the Act, which was one option suggested to us, is likely to be discriminatory under Articles 6 and 59-66 of the EC Treaty. In *Philip Alexander Securities and Futures Ltd v Bamberger The Times* 22 July 1996, the Court of Appeal held that the exclusion from the Consumer Arbitration Agreements Act 1988 of non-domestic arbitration agreements constituted a restriction on the freedom to provide services to nationals of other member states of the EC who were parties to such agreements, so was contrary to article 59 and amounted to unlawful discrimination, contrary to article 6 of the EC Treaty.

[20] See para 16.5 above. Scottish courts cannot acquire jurisdiction by service of writs outside Scotland.

jurisdiction was the applicable law governing the claim and that its provisions conflicted with those of the amended Act. UK courts apply foreign applicable law in appropriate cases and would have to decide whether the provisions of the 1930 Act or of the foreign law were applicable.[21]

16.16 Were the amenability of the insurer to the jurisdiction of a UK court to be the criterion for the applicability of the Act, the existing rights of third parties might be prejudiced in cases where the applicable law governing the insurance contract is English or Scottish law and where the third party seeks to rely on the Act before the courts of another jurisdiction.

Consultees' views are sought on whether one or more of the following criteria or any other criteria should be used to determine the applicability of the 1930 Act:-

(i) the insured has been declared bankrupt or wound up in this country;

(ii) the insurance proceeds are payable in this country;

(iii) the law governing the insurance contract is English or Scottish law;

(iv) the courts have jurisdiction in respect of the tort or delict or breach of contract committed by the insured;

(v) the insured is subject to the jurisdiction of a UK court.[22]

Consultees' views are also sought on whether the provisions of an amended Act should always override conflicting provisions in the law applicable to the insurance contract. If not, when, if at all, should the applicable law be overridden?

SHOULD THE JURISDICTION OF UK COURTS TO HEAR CLAIMS UNDER THE 1930 ACT BE WIDENED?

16.17 In Part 8, we discussed the circumstances in which a UK court would have jurisdiction, under the Brussels Convention or otherwise, to hear claims under the Act.[23] Some of our reform options would enable a third party to proceed directly

[21] See para 16.12 above. In some US courts, the third party's claim is governed by the lex fori (the law of the place where the action is brought). See *McArthur v Maryland Casualty Co* 184 Miss. 665 186 So 305 (1939) where the Supreme Court of Mississippi refused to enforce the Louisiana direct action statute on the basis that it was a Louisiana procedural device which would not apply in Mississippi.

[22] Some foreign law measures have recognised the difficulties in selecting from criteria which, according to the facts of a particular case, may or may not be appropriate and have provided that a number of jurisdictional criteria may apply. For example, article 137 of the Swiss Private International Law states: "The victim may bring his action directly against the wrongdoer's insurer if this is permitted by the law governing the wrongful act or by the law governing the insurance contract". Article 9 of the Hague Traffic Accidents Convention has similar provisions, although it lists potentially applicable laws in order of priority, the law governing the contract of insurance being last in the list.

[23] See paras 8.21-8.26 above.

against the insurer or to join the insurer as a defendant to proceedings against the insured.[24] Under the Brussels Convention,[25] the ability of a third party to proceed against the insurer in the UK might be improved were he to have such new rights because Article 10 of the Convention would give the UK court jurisdiction over the insurer if it had jurisdiction over the insured.[26]

16.18 The provisions of RSC Order 11, rule 1(1) could be amended to provide expressly that third party claimants under the Act could bring proceedings against foreign insurers under an amended Act.[27] There is no equivalent in Scotland to RSC Order 11 and we consider it would be anomalous to create such a ground of jurisdiction in Scotland merely for the purposes of the 1930 Act.[28]

We seek consultees' views on whether or not the provisions of RSC Order 11, rule 1(1) are broad enough to found jurisdiction in England and Wales for claims under the current 1930 Act and under an amended Act. If not, do consultees consider that express provision should be made so that third parties can proceed against insurers outside the jurisdiction, for the purposes of proceeding against them under the 1930 Act?[29]

[24] See Part 12.

[25] If it applies. See paras 8.23 and 16.5 above.

[26] See para 8.24 above.

[27] See, for example, RSC O 11, r 1(e), which makes specific provision for the Nuclear Installations Act.

[28] The provisions of RSC O 11, r 1(1) are already broad in scope and, were third parties to be able to proceed against both insurer and insured in the same proceedings, it may be that it will be easier to found jurisdiction, for example under r 1(1)(c) on the basis that the third party's claim is against a person duly served within or out of the jurisdiction and a person out of the jurisdiction is a necessary or proper party thereto. In *DVA v Voest Alpine* [1997] 2 Lloyd's Rep 279, 286, the Court of Appeal held that a transferee or assignee of contractual rights under a contract governed by English law could rely on Order 11, rule (d)(iii). RSC O 11(1) is set out in Appendix B.

[29] Any amendment could not, of course, derogate from the Brussels Convention.

PART 17
LIMITATION AND PRESCRIPTION

17.1 In this Part, we seek consultees' views on whether English and Scottish rules on limitation and prescription should provide for a third party's right of action under an amended Act to be governed by a fresh limitation period or for a new prescriptive period to govern the insurer's obligation. We also seek consultees' views on whether a third party should be able to substitute himself in English arbitration or court proceedings started by the insured against the insurer.[1] Finally, we consider whether amendments should be made to the limitation provisions contained in section 651 of the Companies Act 1985 governing applications to restore dissolved companies to the Register of Companies.[2]

17.2 We look first at English law.[3] The Law Commission is currently conducting a comprehensive review of the law on limitation periods in England and Wales and a consultation paper will be published shortly. We have not, therefore, dealt with wider limitation issues, which will be covered by that paper.[4]

SHOULD A FRESH LIMITATION PERIOD GOVERN THE ACTIONS OF THIRD PARTIES UNDER THE ACT UNDER ENGLISH LAW?

17.3 One view is that an insurer's duty to the insured is contractual and that the limitation period governing actions against him should not vary according to whether or not the insured is solvent. The limitation period governing all claims under the insurance contract should be that applicable to the insured's right of action as it is unfair for insurers to face potentially very lengthy extensions to the limitation period.[5] In many cases, third parties will know of the existence of their claim and may be negotiating it with the insured or the insurer before the insured has been declared bankrupt or wound up.

17.4 Another view is that the relationships between insurer, insured and third parties are fundamentally altered by the Act and that it is unreasonable that a third party's

[1] As we have seen, this is already possible under Scottish law. See para 9.22 above.

[2] See paras 17.17-17.18 below.

[3] We suggested in Part 9 that it is unclear from English case law whether or not the limitation period governing a third party's right of action under the Act is that which would have governed the insured's right of action against the insurer. Also, it is not certain that the third party can be substituted in proceedings started by the insured against the insurer. See para 9.17 above.

[4] For example, we have not considered whether time should run from accrual of the cause of action or from when the cause of action against the insurer is discoverable. Nor have we considered what the length of any limitation period governing a third party's right of action under an amended Act should be or whether there should be any provision for the period to be extended at the court's discretion.

[5] The insurer's assessment of risk might be particularly difficult where a policy is "occurrence" based. See our discussion at para 2.19 above of the distinction between occurrence and claims made cover.

right of action against the insurer should be governed by the same limitation period applicable to that of the insured, which may start to run before the third party's right of action has accrued. In most cases, the third party will be able to take steps to ensure that proceedings against the insured are brought within the existing limitation period, by starting bankruptcy or winding up proceedings against the insured, but this may not always be the case.[6] Although the third party's rights against the insurer are those of the insured assigned to him under section 1 of the Act,[7] the Act gives him a separate right of action which should arguably be governed by a fresh limitation period.

17.5 A third party claimant under the current Act cannot proceed against the insurer until he has established the liability of the insured and the insured has been declared bankrupt or wound up. We have provisionally recommended that rights should transfer to the third party once two events have occurred: the incident giving rise to the liability of the insured and one of the insolvency events set out in the Act and that after those events the third party should be able to sue the insurer for a declaration.[8] We have also suggested amendments to the 1930 Act which would allow third parties to proceed against the insurer, alone or jointly with the insured.[9]

17.6 We have also provisionally recommended that a third party's right of action should not be subject to a leave requirement.[10] Were a contrary view to be taken, consideration would need to be given to whether the limitation period governing the third party's right of action should not begin to run until leave had been granted.[11]

6 See para 9.17 above.

7 Although his rights may be improved by other provisions in the Act. See Parts 5 and 14 above.

8 See para 12.10 above.

9 See para 12.23 above. It could be argued that the limitation period governing a third party's right of direct action against an insurer should be that which would have applied to his right of action against the insured (which would have run from the date of the occurrence of the event by which the insured incurred liability).

10 See para 12.40 above.

11 Factors which might be relevant are whether the third party could decide when to apply for leave or whether he had to apply within a certain period of time. He could, for example, be required to apply for leave within a certain period following the transfer of his right of action and learning the identity of the insurer. Leave requirements imposed on third parties have caused limitation problems in New Zealand, the Australian Capital Territory and New South Wales. In *New South Wales Medical Defence Union v Crawford* (1993) 31 NSWLR 469, the New South Wales Court of Appeal held that the time for the third party's action against the insurer did not begin to run until leave had been granted. Kirby P said that "leave is a necessary part of the cause of action which is thereby conferred by statute upon a person wishing to bring proceedings against an insurer to enforce the charge. Until such leave is given, the cause of action is not complete. The claimant may not prosecute it in the courts. Time does not run against the claimant". Cf *UEB Packaging v QBE Insurance (International) Ltd* [1996] 2 NZLR 467, where the New Zealand court held that the third party's right of action against the insurer under section 9 of the New Zealand Act expired at the same time as did his claim against the insured. See para 1.10 of Appendix F.

We seek consultees' views on whether a third party's right of action under the Act should be treated as a new cause of action under English law[12] and governed by a fresh limitation period, or whether it should be governed by the limitation period applicable to the insured's right of action against the insurer.[13]

Were the third party's right of action to be governed by a fresh limitation period and to be subject to a leave requirement, do consultees think that the limitation period should only start to run when leave has been granted?

SHOULD THIRD PARTIES BE ABLE TO SUBSTITUTE THEMSELVES IN COURT OR ARBITRATION PROCEEDINGS BEGUN BY THE INSURED?[14]

17.7 As we have seen, there is judicial and other support for allowing third parties to substitute themselves in proceedings started by the insured against the insurer within the limitation period governing his right of action against the insurer.[15] We agree with this view. Were a new limitation period to govern a third party's right of action under the Act, there would be less need for substitution; the main purpose of substitution would be to avoid the wasted costs and delay of fresh proceedings.

17.8 Were third parties to be entitled to be substituted in such proceedings, consideration would need to be given to some of the practical problems which Phillips J, in *The Felicie*, suggested might result.[16]

Costs

17.9 Were the third party to be substituted for the insured, should the third party assume responsibility for those costs or should they fall to be met out of the general assets of the insured? Should the third party be liable for costs already

[12] The position of third parties under Scottish law is discussed at paras 17.14-17.16 below.

[13] If our provisional recommendation is supported, the third party's right of action would arise on the happening of one of the insolvency events set out in the Act. See para 17.5 above. The Law Commission's consultation paper on limitation will discuss the issue of whether a plaintiff should know the identity of a defendant before the limitation period governing his right of action starts to run. We discussed in Part 13 the information which should be disclosed to third party claimants under the Act, including the identity of the insurer, and when that information should be disclosed.

[14] As we have already seen, third parties can already substitute themselves in this way under Scottish law. See para 9.22 above.

[15] See paras 9.4-9.17 above. See also Sir Jonathan Mance, "Insolvency at Sea" [1995] LMCLQ 34, at 51:"A possible implication of *Lefevre v White* [1990] 1 Lloyd's Rep 569 is that a third party's claim under the 1930 Act may become time-barred without his ever acquiring the right to pursue it under the 1930 Act. If that is the implication, the 1930 Act would certainly need amending. Even if Phillips J's apparent contrary view about limitation in *The Felicie* is correct, still the Act needs amending to ensure that a third party transferee of rights under the Act has the power to step into the shoes of the insured and pursue any existing arbitration. There is no reason why the principles in *The Jordan Nicolov* and *Baytur* should not be incorporated into the context of the 1930 Act".

[16] See para 9.12 above.

incurred relating to his own claim and, if so, how can such costs be apportioned? There might be problems from other creditors were the trustee in bankruptcy or liquidator to be expected to pay such sums out of the insured's general assets. An insolvent insured's legal advisers might wish to come to some arrangement with the third party for payment of outstanding fees before doing further work.

17.10 In *The Jordan Nicolov*, Hobhouse J suggested that such problems should not arise on a legal assignment as this "does not relieve the assignor of his liabilities" but recognised that there might be different considerations where the 1930 Act was concerned. One view is that it is not unreasonable for assets of the insolvent insured to be used to pay costs incurred up to that point because it is his liability and right to an indemnity which are in issue.

Other matters in issue in the proceedings between the insured and the insurer

17.11 Phillips J suggested that problems might arise if the dispute between the insured and the insurer went beyond the question of whether or not the insured's liability to the third party should be indemnified. Such issues (for example, the liability of the insured towards other third parties) could be severed and pursued by other third parties or by the insured's trustee in bankruptcy or liquidator, as appropriate.[17]

Notice and the mechanics of substitution

17.12 As we have seen, in *Baytur SA v Finagro Holding SA*,[18] the Court of Appeal held that assignees of rights of action can be substituted in pending proceedings but that they must first apply to court for an order under RSC Order 15, rule 7(2)[19] or, in the case of arbitration proceedings, give notice to the other parties and submit to the jurisdiction of the arbitrator. There seems no reason why a similar system of application and notification could not be used in relation to third party rights under the 1930 Act.

17.13 It will usually be in the interests of all parties and the court or arbitration that existing proceedings are maintained so that the cost and delay necessitated by commencing fresh proceedings are avoided. We suggest, therefore, that a third party should be able to apply to substitute himself in court and arbitration proceedings[20] commenced by the insured against the insurer.

[17] See Hobhouse J in *The Jordan Nicolov* [1990] 2 Lloyd's Rep 11, at 19 "If the relevant claimants, or plaintiffs, are not appropriately or conveniently combined in the same proceedings, then they should be severed into separate proceedings".

[18] [1992] 1 Lloyd's Rep 569. See para 9.16 above.

[19] Set out in Appendix B, together with relevant provisions from Part 18 of the Draft Civil Proceedings Rules. It is not clear whether or not CCR O 15 attracts the provisions of RSC O 15, r 7. Popplewell J in *Lefevre v White* [1990] 1 Lloyd's Rep 569 held that RSC O 15, r 7(2) did not apply to a third party under the 1930 Act. See para 9.6 above.

[20] By giving notice to the other parties to the arbitration and to the arbitrator.

Consultees' views are sought on our provisional conclusion that a third party should be able to apply to substitute himself in court and arbitration proceedings already commenced by the insured against the insurer prior to the insolvency of the insured

Consultees' views are also sought on where responsibility for the costs of the insured and the insurer incurred prior to substitution should lie. We provisionally favour the first of the following options:-

(i) requiring the insured to pay his own costs up to substitution and requiring a successful insurer to recover his costs prior to substitution from the insured's estate rather than from the third party; or

(ii) requiring the third party to indemnify the insured and the insurer for costs incurred prior to substitution in the event of the action against the insurer failing.

SCOTTISH LAW

17.14 As we have seen,[21] the obligation of the insurer to indemnify the insured under the policy is enforceable once the third party has established the liability of the insured and the five year prescriptive period of this obligation starts to run from that date at the earliest. On insolvency, the third party becomes, by virtue of the 1930 Act, a statutory assignee of the insured's rights as against the insurer.[22] This assignation does not interrupt the running of prescription. As we have also seen, the third party can, under Scottish law, be substituted in proceedings started by the insured against the insurer.[23]

17.15 In our discussion of the English rules on limitation, we discussed some of the arguments for and against allowing a fresh limitation period to govern a third party's right of action against an insurer under an amended Act. The position is rather different under the Scottish law on prescription. The prescription technique focuses attention on the obligation of the person required to pay or to do something, in this case the insurer, rather than on whether the person whose rights are affected has sufficient time to bring proceedings. It may be seen as unreasonable to suggest that the period of prescription should be extended merely because there has been a statutory transfer of the creditor's rights. There could be cases where the third party, having established the liability by decree but having failed to enforce his decree for over 4 years, finds that the insured has been sequestrated and that no relevant claim has been made against the insurer or relevant acknowledgement obtained. The third party then has only a short time in which to make a claim against the insurer. However, this kind of situation is not unusual under the law of prescription and it might be anomalous to give the third party another 5 years if the insured's insolvency occurs just before the expiry of the

[21] See para 9.19 above.

[22] *Greenless v Port of Manchester Insurance Company Limited* 1933 SC 383.

[23] See para 9.22 above.

5 year period but no rights at all (as there would be none to be transferred) if the insolvency event occurred just after the expiry of the 5 year period.

17.16 The Scottish Law Commission does not consider that any change is required to the existing law on prescription in Scotland in order to deal with this situation but, as the issue of a new or extended limitation period in English law has been raised, the Scottish Law Commission invites the views of consultees. A similar question might arise if, contrary to our provisional view,[24] the third party were to require leave to raise proceedings against the insurer.

We seek consultees' views on whether the law of prescription in Scotland should be changed to provide for the start of a new prescriptive period where one of the insolvency events set out in the Act (or the granting of leave, if leave were to be required) occurs during the running of the period of prescription of the insurer's obligation to the insured.

SECTION 651 COMPANIES ACT 1985[25]

17.17 As we have seen, section 651 provides that an application to restore a dissolved company to the register must be made within two years of the date of dissolution, except in actions involving death or personal injury.[26] We have given our provisional view that third parties should not be required to restore dissolved companies to the register before proceeding against insurers under the Act.[27] Should the Act not be amended in this way, we suggest that this distinction should be removed.[28] Third parties would then be able to apply for an order restoring a dissolved company to the register at any time, whatever the nature of their claim against the company. No order would be made, however, if it appeared to the court that the limitation period governing the third party's right of action against the company had expired, although in some death and personal injury actions the court could order that the period between the dissolution of the company and the making of the order restoring it should not count as part of that period.[29]

[24] See para 12.40 above.

[25] This issue is relevant to English and Scottish law.

[26] See paras 4.38-4.39 above.

[27] See para 12.23 above.

[28] We queried at paras 11.15-11.16 above whether distinctions between claims involving death or personal injury were justifiable.

[29] See s 651(6) and (7). See *Re Workvale Ltd* [1992] 1 WLR 416, 424, 425. In that case it was held that it was "well arguable" that the applicant under s 651 would be entitled to an order under s 33 of the Limitation Act 1980 (permitting a personal injury plaintiff to bring proceedings out of time) and that in the circumstances an order under s 651(5) that the time between dissolution and the making of the order was to be discounted was correctly made. The three year limitation period had not expired at the date of dissolution of the company. Also see *Re Mixhurst Ltd* [1994] 2 BCLC 19, 29 in which it was held that, by contrast with the position under s 653(3), orders under s 651 which override the limitation period are only available in the circumstances governed by s 651(5) (death and personal injury claims). See also paras 4.40-4.43 above.

We seek consultees' views on our provisional conclusion that, if third parties are still to be required to restore dissolved companies to the register for the purposes of proceeding under the Act, the two year limitation period for claims not involving death or personal injury should be abolished.

17.18 Section 141(4) Companies Act 1989 provides that applications cannot be made to restore companies dissolved more than twenty years before the commencement of that section.[30] It has been suggested that this period may be too short, particularly in cases involving long tail personal injury claims.[31]

We seek consultees' views on whether third parties should be able to restore to the register companies dissolved more than twenty years before the coming into force of section 141 Companies Act 1989. If consultees do not consider that all third parties should have this right, do they consider that it should be open to those claiming for death or personal injury?[32]

[30] Section 141 of the 1989 Act came into force in England and Wales on 16 November 1989. Article 75 of the 1990 Northern Ireland order came into force on 11 March 1991. These provisions were retrospective so as to permit claimants whose causes of action accrued before their coming into force to rely on them; Law Reform Advisory Committee for Northern Ireland, Discussion Paper No 2; Actions arising out of Insidious Diseases 1992, para 6.6.

[31] In their Discussion Paper No. 2, Actions Arising out of Insidious Diseases, 1992, at para 6.8.1, the Law Reform Advisory Committee for Northern Ireland suggested that "the period of 20 years may be too short in many cases to assist the victims of insidious diseases ... . All lawyers engaged in litigation arising out of insidious diseases will be well aware of many cases where such diseases have become manifest much later than 20 years after exposure".

[32] Under the current provision it is not possible to obtain a declaration that a dissolution prior to 16 November 1969 is void. If the 20 year restriction were to be repealed then the new law would operate retrospectively to allow restoration to the register of companies dissolved at any time. There may be an argument that such a reform, in so far as it would permit claims against insurers for funds which currently could not be claimed from them, is in breach of Article 1 of the First Protocol to the European Convention on Human Rights as depriving them of "possessions".

PART 18
SUMMARY OF OUR PROVISIONAL PROPOSALS AND CONSULTATION QUESTIONS

18.1 We have formed provisional views on a number of issues in this paper. We have suggested that a third party should acquire rights under an amended Act before he has established the liability of the insured. His rights would arise once two events had occurred: the incident giving rise to the liability of the insured and one of the insolvency events set out in the Act.[1] After those events the third party would also have the right to sue the insurer for a declaration.[2]

18.2 We have suggested that the Act should continue to apply to all liability insurance policies,[3] that third parties should have earlier and increased access to policy information and that the ability of insurers to rely on defences against third parties should be restricted.[4] We have sought consultees' views on whether a statutory scheme of rateable distribution to multiple third party claimants should replace the current "first past the post" system.[5] We have given our provisional view that the private international law aspects of the Act should be clarified[6] and have sought consultees' views on the criteria which might be used to determine the applicability of the Act.[7] We have sought consultees' views on whether a new limitation period should govern the third party's right of action against the insurer[8] and have suggested that third parties should be able to substitute themselves in proceedings started by the insured within the limitation period.[9]

18.3 We set out below a summary of the particular issues on which we seek consultees' comments. We invite comments on any of the matters raised in this paper and any other suggestions which consultees may have. Consultees should not feel obliged to answer all the questions: we appreciate that their views or experience may be relevant to some only.

1 See para 12.10 above.

2 See para 12.33 above.

3 See para 11.20 above.

4 See para 14.6 above.

5 See para 15.18 above.

6 See para 16.2 above.

7 See para 16.16 above.

8 See para 17.6 above.

9 As they can in Scotland. See paras 9.22 and 17.13 above.

THE SCOPE OF THE ACT

1. Do consultees agree with our provisional conclusion that the Act should not be extended to reinsurance policies?[10] If they do not, to what types of reinsurance policy should the Act apply?

2. Consultees' views are sought on our provisional conclusion that the Act should continue to apply to all liability insurance policies, regardless of the nature of the third party claimant or of his claim?[11]

3. If consultees disagree, they are asked to specify how the applicability of the Act should be restricted.[12]

THIRD PARTY RIGHTS UNDER AN AMENDED ACT[13]

When should the third party's right of action arise?

4. Do consultees agree that a third party's rights under an amended Act should arise once two events have occurred: the incident giving rise to the liability of the insured and one of the insolvency events set out in the Act?[14]

5. If consultees consider that the third party's rights should arise before or after this point, when do they think they should arise? For example, should they arise:-

(i) after close of pleadings in the proceedings brought by the third party against an insured who has been declared bankrupt or wound up;

(ii) on the happening of the event giving rise to the liability of the insured, regardless of the solvency or otherwise of the insured; or

(iii) when an insured who has incurred liability to the third party is in financial difficulties prior to the happening of one of the insolvency events set out in the Act? Consultees who favour this option are requested to suggest a trigger for the third party's rights.[15]

6. Do consultees agree that, in its application to Scotland, the amended Act should use the phrase "person's estates being sequestrated" instead of "becoming bankrupt"?[16]

[10] See para 11.8 above.

[11] See para 11.20 above.

[12] See para 11.20 above.

[13] See Question 15 below for our provisional recommendation as to the nature of the third party's rights under an amended Act.

[14] See para 12.10 above.

[15] See para 12.10 above.

[16] See para 12.10 above.

The implications of the liability of insurer and insured being resolved in the same proceedings

7. Consultees' views are sought on our provisional conclusion that insurers conducting the defence of their insured under the Act should be able to do so without prejudice to their right to repudiate their liability to the insured under the insurance contract.[17]

Should the third party proceed against both insurer and insured?[18]

8. We have reached the provisional conclusion that the insured[19] and the insurer should be parties to the third party's action unless the insured is a dissolved company which has been struck off the Register of Companies,[20] in which case the third party should have a right to proceed against the insurer alone.[21] Do consultees agree?

9. Consultees' views are sought on the adequacy of existing procedures under sections 651 and 653 of the Companies Act 1985.[22]

10. Consultees' views are sought on whether and, if so, how the existing procedures should be simplified if, contrary to our provisional view, third parties continue to be required to restore a dissolved company to the register.[23]

11. Alternatively, do consultees consider that a third party should have a right to proceed[24] against the insurer alone:

(i) in all cases;

(ii) in other limited cases (for example, where insurance is compulsory).[25]

12. Do consultees agree with our provisional conclusion that, if a third party had a right to proceed against the insurer alone, he should, if he chose, be able to

[17] See para 12.13 above.

[18] See para 12.23 above.

[19] (Represented by the officeholder)

[20] Or unless the liability of the insured has already been established, when there would be no need to join the insured under an amended Act or under the current Act.

[21] See para 12.23 above. For the nature of the third party's "action" see our provisional recommendation set out in Question 15 below. In Question 16, we ask whether the third party's right of action should be subject to a leave requirement.

[22] See para 12.23 above.

[23] See para 12.23 above.

[24] See Question 15 below for our provisional view as to the nature of the third party's rights against the insurer.

[25] See para 12.23 above.

proceed against the insured as well[26] and, if he had already started proceedings against the insured, to join the insurer into those proceedings?[27]

13. If the insured was not a party to the proceedings brought by the third party, do consultees believe that the insurer should be able to join the insured into the proceedings and that the insured should be able to intervene in those proceedings?[28]

14. If so, do consultees consider that the existing rules on joinder and substitution[29] are adequate or do they think that specific provision should be made in the amended Act.

Third party rights under an amended Act

15. We have reached the provisional view that once two events have occurred: the event giving rise to the liability of the insured and one of the insolvency events set out in the Act, the third party should acquire the insured's rights under the insurance policy. The third party should in addition have a right to seek a declaration or declarator[30] that, on the liability of the insured being established, the insurer will be liable to indemnify the third party.[31]

Do consultees agree with this provisional view? If not, what rights do they think third parties should acquire under an amended Act.

Should the third party's right of action against the insurer be subject to a leave requirement?

16. We seek consultees' views on our provisional conclusion that a third party's right to proceed against insurers under the Act should not be subject to a leave requirement nor to a requirement that he notify the insurer of his intention to proceed against it.[32]

17. If, contrary to our provisional conclusion, consultees consider that a third party's right of action under the Act should be subject to a leave requirement, their views are sought on:-

(i) when the leave application should be made;

(ii) what the leave criteria should be; and

[26] See para 12.23 above.

[27] See para 12.23 above.

[28] See para 12.23 above.

[29] See paras 12.22-12.23 and Appendix B.

[30] As we have already discussed, third parties can already seek a declarator under Scottish law, but it is uncertain whether they can do so under English law. See para 12.33, n 84 above.

[31] See para 12.7 above.

[32] See para 12.40 above.

(iii) whether the leave application should be made ex parte or inter partes and whether any other specific procedural requirements should apply.[33]

Settlements between the insurer and the insured[34]

18. We seek consultees' views on whether settlements reached between insurers and insured prior to the happening of one of the insolvency events set out in the Act cause problems to third party claimants under the Act and whether, in their view, the Act should be amended to allow third parties to apply to set aside such settlements.

19. Were such an amendment to be made to the Act, within what period prior to the insolvency should settlements be vulnerable to setting aside?

Payment of the insurance proceeds by the insurer[35]

20. We seek consultees' views on whether or not a provision should be included in an amended Act requiring insurers expressly to pay insurance proceeds direct to the third party.

A third party right of direct action against the insurer of a disappeared insured[36]

21. We seek consultees' views on whether the 1930 Act should be extended to provide third parties with a right of action against the insurers of insured parties who have disappeared.[37]

THE DUTY TO DISCLOSE POLICY INFORMATION

When should the duty to disclose policy information arise?

22. Consultees' views are sought on our provisional conclusion that the obligation to disclose policy information should not be dependent on the establishment of the liability of the insured but that it should arise after the incident giving rise to the liability of the insured and after the event of insolvency and that disclosure should be given within 14 days of the disclosing party becoming aware that a third party has a possible claim under the Act.[38]

[33] See para 12.44 above.

[34] See para 12.45 above.

[35] See para 12.48 above.

[36] See para 12.49 above.

[37] If the court was satisfied that the third party had made all reasonable efforts to find him.

[38] Were our provisional recommendation to be implemented, this would be when the insurer was aware of the event giving rise to the liability of the insured to the third party and one of the insolvency events set out in the Act had occurred. See para 13.4 above. Consultees may wish to give their views on whether a time period other than 14 days would be appropriate with regard to some or all of the categories of information listed in Question 28 below.

23. Do consultees agree that disclosing parties should have a continuing duty to disclose information?[39]

24. If consultees disagree, when do they consider the duty to disclose should arise?

25. Consultees' views are sought on whether a time period other than 14 days would be appropriate with regard to some or all of the categories discussed below.[40]

Information discloseable under section 2

26. We have reached the provisional conclusion that the definition in section 2 of the categories of information to which the duty of disclosure extends should be clarified by a list in the Act.[41] Consultees' views are sought on this provisional conclusion.

27. Consultees' views are sought on whether the disclosing party should be able to apply to court for an order dispensing with their duty to disclose the grounds for a purported repudiation of cover by the insurer, in addition to any right which they may have to apply for a split trial or for the resolution of the cover point as a preliminary issue.

28. We have reached the provisional conclusion that the following categories of policy documentation and information should be disclosed[42] to third party claimants under the Act.

(i) the existence of any insurance contract;

(ii) the identity of the insurer;

(iii) relevant policy documentation, including the cover terms;

(iv) whether the insurer has purported to repudiate cover;

(v) the grounds of any purported repudiation;

(vi) the value of the insurance cover and details of whether or not some or all of the insurance fund has already been paid out to other claimants;

(vii) details of any settlement between the insurer and the insured.

29. Do consultees agree that all these categories should be disclosed? If not, which are objectionable? Are there any other categories of documentation or information which should be disclosed?

[39] See para 13.4 above.

[40] See Question 28 below.

[41] See para 13.5 above.

[42] See para 13.13 above.

30. Do consultees think that, in addition to any list of discloseable information set out in an amended Act,[43] it should also contain a catch all provision requiring disclosure of "other relevant documents and information"?

31. We have reached the provisional conclusion that the duty to disclose should not extend to details of any settlement between the insured and the insurer before the occurrence of one of the insolvency situations.[44] Do consultees agree with this provisional conclusion?

Should the extent of the duty of disclosure vary according to the nature of the third party or of his claim?[45]

32. Do consultees' agree that the duty to disclose under an amended Act should not vary according to the nature of the third party's claim.

Who should have a duty of disclosure and what should the scope of the duty be?[46]

33. Do consultees agree that the duties of the insured[47] and of the insurer to disclose policy information under the Act should arise simultaneously?

34. With regard to each of the categories of information set out above,[48] consultees' views are sought on what the extent of the officeholder's duty to disclose should be. For example, should his duty:-

(i) apply only to information which is reasonably ascertainable from records to which he is entitled; and/or

(ii) be limited

(a) to third parties who seek disclosure from him; or

(b) to third parties who seek such disclosure and whose claims he is aware may be covered by insurance.

35. Consultees' views are sought on the extent to which the position of third parties would be improved were a duty of disclosure under the Act to extend to all those in possession of insurance information or documentation and on whether the duty of disclosure should be extended in this way.

36. If such persons were to have a duty of disclosure, do consultees consider that the duty should be limited? For example, should it be limited to information as to

[43] See Question 28 above.

[44] Subject to the duty to disclose any decreases in the value of the insurance fund as a result of such settlements. See Questions 23 and 28.

[45] See para 13.15 above.

[46] See paras 13.16-13.20 above.

[47] And of the other parties listed in s 2(1). See para 13.19 above.

[48] See Question 28 above.

the identity of the insurer or to information which is reasonably ascertainable from the records maintained by such persons?

37. Do consultees consider that the duty of disclosure should be extended only to insurance brokers?

THE ABILITY OF INSURERS TO RELY ON DEFENCES

The position of third party claimants under the 1930 Act[49]

38. Consultees' views are sought on our provisional view that:

(i) restrictions should be placed on the ability of insurers to rely on certain defences against third parties because of the particular problems faced by third party claimants under the 1930 Act which are not faced by the insured; and

(ii) insurers should not be permitted to insist that policy conditions are met by the insured personally where the third party can meet them.

What bases could be used to limit the ability of insurers to rely on defences?

39. We seek consultees' views on whether any of the following or other restrictions should be used individually or cumulatively to limit the ability of insurers to rely on defences against third party claimants under an amended Act.[50]

40. Do consultees consider that restrictions should be placed on the ability of insurers to rely on defences against third party claimants under an amended Act only when insurance is compulsory?[51] If so, what restrictions do they think should apply and what should those restrictions be?

41. Do consultees consider that restrictions should be placed on the ability of insurers to rely on defences where the third party's claim is of a particular type?[52] If so, to what types of claim should the restrictions apply and what should those restrictions be?

42. Do consultees consider that the ability of insurers to rely on defences should be restricted by reference to the timing of the breaches on which those defences

[49] See para 14.3 above.

[50] See para 14.9 above. By "restrictions" we mean preventing insurers from relying on defences where the insurance is of a particular category and/or where the claim or claimant is of a particular type and/or by reference to the timing of the breach and/or by reference to the consequences of the breach. See Questions 40-43 below. In Question 45 we canvass a different kind of restriction which would flow from applying the "consequences" restriction, namely that payment out under the insurance policy could be proportionate to the consequences of the breach. If consultees consider that other types of restriction would be appropriate they are asked to specify them.

[51] See para 14.12 above.

[52] See paras 14.13-14.14 above.

are based? If so, what should be the point in time after which breaches could not give rise to insurers' defences?[53]

43. Do consultees consider that, if restrictions are to be placed on insurers' ability to rely on defences, those restrictions should depend on the consequences of the breach of duty and/or of policy terms?

44. If so, do they agree with our tentative view that insurers should not be able to rely, as against third parties, on breaches unless they are both causative of the third party's loss and prejudicial to the insurer?[54]

45. Do consultees agree that, if such restrictions were to be imposed, insurers should only be entitled to reduce the indemnity proportionally to the extent that the breach was causative of the loss or to any prejudice to their interests?[55]

46. Do consultees agree that, if such restrictions were to be imposed, the burden of proof for establishing that there was no connection between the breach and the loss should be on the third party but that the burden of proof for establishing the prejudice suffered by the insurer should be on the insurer?[56]

47. We seek consultees' views on whether the restrictions set out above or other restrictions should be applied to prevent insurers from relying on each of the following types of defence. We also seek consultees' views on whether the specific restrictions set out below should apply to them and on whether other specific restrictions should apply to any other types of policy condition to which we have not referred.

(i) Non-disclosure and misrepresentation;[57]

(ii) Notice requirements;[58]

(iii) Arbitration clauses;[59]

(iv) Conditions relating to the duty to co-operate and provide assistance;[60]

[53] Insurers could be prevented, for example, from relying on breaches which occurred after the incident giving rise to the liability of the insured or after the happening of one of the insolvency events set out in the Act. See paras 14.15-14.18 above.

[54] See para 14.25 above.

[55] See para 14.26 above.

[56] See para 14.27 above.

[57] See para 14.29 above.

[58] See paras 14.30-14.31 above.

[59] In Question 66, we seek consultees' views on whether third parties should be able to substitute themselves in arbitration proceedings started by the insured against the insurer to avoid limitation problems.

[60] See para 14.36 above.

(v) Conditions relating to the duty of the insured to preserve the assets/business insured (for example to maintain security) or to hold a particular licence or have a particular qualification;[61]

(vi) Conditions relating to the ability of the insured to pay.[62]

48. Do consultees agree that it would be inappropriate to enact new law in the context of the 1930 Act alone restricting the ability of insurers to rely on non-disclosure and misrepresentation?[63]

49. We seek consultees' views on whether insurers should be prevented from relying on breaches of notice requirements in claims made policies where late notification would bring the claim outside the claims period.[64]

50. We seek consultees' views on the extent to which insurers' reliance on arbitration clauses causes problems to third party claimants under the Act.[65]

51. Consultees' views are also sought on whether arbitration clauses in insurance contracts should be unenforceable against third party claimants or certain types of claimant under the Act.[66]

52. Do consultees consider that insurers should be permitted to deduct unpaid premiums from amounts recovered by a third party under the Act?[67]

53. We seek consultees' views on whether insurers should be permitted to rely, as against third party claimants under the Act, on pay to be paid clauses.[68]

54. Do consultees consider that other specific restrictions should apply to other types of policy condition to which we have not specifically referred?

The right of the insurer to an indemnity against the insured

55. Do consultees agree that any right to an indemnity which insurers might have against the insured in cases where they have been prevented by the Act from relying on defences which they could have invoked against the insured is unlikely to be of much practical assistance to insurers in most cases?[69]

[61] See para 14.37 above.

[62] Such conditions are discussed at para 14.38 above.

[63] See para 14.29 above.

[64] See para 14.31 above.

[65] See para 14.35 above.

[66] See para 14.35 above.

[67] See para 14.39 above.

[68] See para 14.41 above.

[69] See para 14.42 above.

56. Do consultees consider that such a right should be included in an amended Act in any event?[70]

THE DISTRIBUTION OF A LIMITED INSURANCE FUND TO MULTIPLE CLAIMANTS

57. Consultees are asked to inform us whether or not they have had experience of problems caused by the "first past the post" principle in the context of claims under the 1930 Act (other than in the Lloyd's litigation).[71]

58. Do consultees consider that the court's existing powers are adequate to impose a scheme of rateable distribution on claimants under the Act? If not, do they consider that the court should be provided with additional procedural powers? What additional powers do they consider the court should have?[72]

59. Alternatively, do consultees consider that a new statutory scheme of rateable distribution should be introduced? If so, we should be grateful for their views on the following suggested scheme[73] and on any other scheme which they think should be introduced.

We suggest that any new statutory scheme should work in the following way:-

(a) the scheme would be triggered following an application to the court by a third party or by the insurer;

(b) the court should decide how the fund should be administered. Depending on the circumstances of the case, the court might order sums payable under the insurance contract to be paid into court, to a court appointee or, in appropriate cases, to the insured's insolvency practitioner;

(c) the scheme would provide for the costs of the court, the court appointee or the insolvency practitioner to be deducted before any distribution was made to third party claimants. In appropriate cases, it would also provide for the costs of the third party triggering the scheme to be deducted prior to distribution. The scheme would provide for interim payments to be made and, if possible, for the value of outstanding claims to be assessed and appropriate "shares" in the fund determined, without further recourse to litigation.

[70] See para 14.42 above.

[71] See para 15.1 above.

[72] For example more extensive powers to synchronise judgments. See para 15.5 above.

[73] See para 15.18 above.

PRIVATE INTERNATIONAL LAW

60. Do consultees agree with our provisional conclusion that the private international law aspects of the Act should be clarified or do they think that such matters should be left to the court?[74]

61. Consultees' views are sought on whether one or more of the following criteria or any other criteria should be used to determine the applicability of the 1930 Act:-

(i) the insured has been declared bankrupt or wound up in this country;[75]

(ii) the insurance proceeds are payable in this country;[76]

(iii) the law governing the insurance contract is English or Scottish law;[77]

(iv) the courts have jurisdiction in respect of the tort or delict or breach of contract committed by the insured;[78]

(v) the insurer is subject to the jurisdiction of a UK court.[79]

62. Consultees' views are also sought on whether the provisions of an amended Act should always override conflicting provisions in the law applicable to the insurance contract. If not, when, if at all, should the applicable law be overridden?[80]

63. We seek consultees' views on whether or not the provisions of RSC Order 11, rule 1(1) are broad enough to found jurisdiction for claims under the current 1930 Act and under an amended Act?[81] If not, do consultees consider that express provision should be made so that third parties can proceed against insurers outside the jurisdiction, for the purposes of proceeding against them under the 1930 Act?[82]

LIMITATION AND PRESCRIPTION

English law

64. We seek consultees' views on whether a third party's right of action under the Act should be treated as a new cause of action under English law, and

[74] See para 16.2 above.

[75] See paras 16.4-16.5 above.

[76] See para 16.6 above.

[77] See para 16.8-16.13 above.

[78] See para 16.7 above.

[79] See paras 16.14-16.16 above.

[80] See para 16.16 above.

[81] Ie in cases not governed by the Brussels Convention. See para 16.14 above. There is no equivalent to RSC Order 11, rule 1(1) in Scottish law. See para 16.18 above.

[82] Any amendment could not, of course, derogate from the Brussels Convention. See para 16.18, n 29 above.

governed by a fresh limitation period, or whether it should be governed by the limitation period applicable to the insured's right of action against the insurer?

65. Were the third party's right of action to be governed by a fresh limitation period and to be subject to a leave requirement, do consultees think that the limitation period should only start to run when leave has been granted?

66. Consultees' views are sought on our provisional view that a third party should be able to apply to substitute himself in court and arbitration proceedings already commenced by the insured against the insurer prior to the insolvency of the insured.[83]

67. Consultees' views are also sought on where responsibility for the costs of the insured and the insurer incurred prior to substitution should lie. We provisionally favour the first of the following options:-

(i) requiring the insured to pay his own costs up to substitution and requiring a successful insurer to recover his costs prior to substitution from the insured's estate rather than from the third party; or

(ii) requiring the third party to indemnify the insured and the insurer for costs incurred prior to substitution in the event of the action against the insurer failing.[84]

Scottish law

68. We seek consultees' views on whether the law of prescription in Scotland should be changed to provide for the start of a new prescriptive period where one of the insolvency events set out in the Act (or the granting of leave, if leave were to be required) occurs during the running of the period of prescription of the insurer's obligation to the insured.[85]

The limitation period governing the restoration of companies to the register

69. We seek consultees' views on our provisional conclusion that, if third parties are still to be required to restore dissolved companies to the register for the purposes of proceeding under the Act, the two year limitation period for claims not involving death or personal injury should be abolished.[86]

70. We also seek consultees' views on whether third parties should be able to restore to the register companies dissolved more than twenty years before the coming into force of section 141 Companies Act 1989. If consultees do not

[83] See para 17.13 above.

[84] See para 17.13 above.

[85] See para 17.16 above.

[86] See para 17.17 above.

consider that all third parties should have this right, do they consider that it should be open to those claiming for death or personal injury?[87]

[87] See para 17.18 above.

APPENDIX A
LEGISLATION

THIRD PARTIES (RIGHTS AGAINST INSURERS) ACT 1930

1 Rights of third parties against insurers on bankruptcy, etc, of the insured

(1) Where under any contract of insurance a person (hereinafter referred to as the insured) is insured against liabilities to third parties which he may incur, then-

(a) in the event of the insured becoming bankrupt or making a composition or arrangement with his creditors; or

(b) in the case of the insured being a company, in the event of a winding-up order or an administration order being made, or a resolution for a voluntary winding-up being passed, with respect to the company, or of a receiver or manager of the company's business or undertaking being duly appointed, or of possession being taken, by or on behalf of the holders of any debentures secured by a floating charge, of any property comprised in or subject to the charge or of a voluntary arrangement proposed for the purposes of Part 1 of the Insolvency Act 1986 being approved under that Part;

if, either before or after that event, any such liability as aforesaid is incurred by the insured, his rights against the insurer under the contract in respect of the liability shall, notwithstanding anything in any Act or rule of law to the contrary, be transferred to and vest in the third party to whom the liability was so incurred.

(2) Where the estate of any person falls to be administered in accordance with an order under section 421 of the Insolvency Act 1986, then, if any debt provable in bankruptcy (in Scotland, any claim accepted in the sequestration) is owing by the deceased in respect of a liability against which he was insured under a contract of insurance as being a liability to a third party, the deceased debtor's rights against the insurer under the contract in respect of that liability shall, notwithstanding anything in any such order, be transferred to and vest in the person to whom the debt is owing.

(3) In so far as any contract of insurance made after the commencement of this Act in respect of any liability of the insured to third parties purports, whether directly or indirectly, to avoid the contract or to alter the rights of the parties thereunder upon the happening to the insured of any of the events specified in paragraph (a) or paragraph (b) of subsection (1) of this section or upon the estate of any person falling to be administered in accordance with an order under section 421 of the Insolvency Act 1986, the contract shall be of no effect.

(4) Upon a transfer under subsection (1) or subsection (2) of this section, the insurer shall, subject to the provisions of section 3 of this Act, be under the same liability to the third party as he would have been under to the insured, but-

(a) if the liability of the insurer to the insured exceeds the liability of the insured to the third party, nothing in this Act shall affect the rights of the insured against the insurer in respect of the excess; and

(b) if the liability of the insurer to the insured is less than the liability of the insured to the third party, nothing in this Act shall affect the rights of the third party against the insured in respect of the balance.

(5) For the purposes of this Act, the expression "liabilities to third parties", in relation to a person insured under any contract of insurance, shall not include any liability of that person in the capacity of insurer under some other contract of insurance.

(6) This Act shall not apply-

(a) where a company is wound up voluntarily merely for the purposes of reconstruction or of amalgamation with another company; or

(b) to any case to which subsection (1) and (2) of section seven of the Workmen's Compensation Act 1925 applies.

2 Duty to give necessary information to third parties

(1) In the event of any person becoming bankrupt or making a composition or arrangement with his creditors, or in the event of the estate of any person falling to be administered in accordance with an order under section 421 of the Insolvency Act 1986, or in the event of a winding-up order or an administration order being made, or a resolution for a voluntary winding-up being passed, with respect to any company or of a receiver or manager of the company's business or undertaking being duly appointed or of possession being taken by or on behalf of the holders of any debentures secured by a floating charge of any property comprised in or subject to the charge it shall be the duty of the bankrupt, debtor, personal representative of the deceased debtor or company, and, as the case may be, of the trustee in bankruptcy, trustee, liquidator, administrator, receiver, or manager, or person in possession of the property to give at the request of any person claiming that the bankrupt, debtor, deceased debtor or company is under a liability to him such information as may reasonably be required by him for the purpose of ascertaining whether any rights have been transferred to and vested in him by this Act and for the purpose of enforcing such rights, if any, and any contract of insurance, in so far as it purports, whether directly or indirectly, to avoid the contract or to alter the rights of the parties thereunder upon the giving of any such information in the events aforesaid or otherwise to prohibit or prevent the giving thereof in the said events shall be of no effect.

(1A) The reference in subsection (1) of this section to a trustee includes a reference to a supervisor of a voluntary arrangement proposed for the purposes of, and approved under Part I or Part VIII of the Insolvency Act 1986.

(2) If the information given to any person in pursuance of subsection (1) of this section discloses reasonable ground for supposing that there have or may have

been transferred to him under this Act rights against any particular insurer, that insurer shall be subject to the same duty as is imposed by the said subsection on the persons therein mentioned.

(3) The duty to give information imposed by this section shall include a duty to allow all contracts of insurance, receipts for premiums, and other relevant documents in the possession or power of the person on whom the duty is so imposed to be inspected and copies thereof to be taken.

3 Settlement between insurers and insured persons

Where the insured has become bankrupt or where in the case of the insured being a company, a winding-up order or an administration order has been made or a resolution for a voluntary winding-up has been passed, with respect to the company, no agreement made between the insurer and the insured after liability has been incurred to a third party and after the commencement of the bankruptcy or winding-up or the day of the making of the administration order, as the case may be, nor any waiver, assignment, or other disposition made by, or payment made to the insured after the commencement or day aforesaid shall be effective to defeat or affect the rights transferred to the third party under this Act, but those rights shall be the same as if no such agreement, waiver, assignment, disposition or payment had been made.

COMPANIES ACT 1985

651 Power of court to declare dissolution of company void

(1) Where a company has been dissolved, the court may, on an application made for the purpose by the liquidator of the company or by any other person appearing to the court to be interested, make an order, on such terms as the court thinks fit, declaring the dissolution to have been void.

(2) Thereupon such proceedings may be taken as might have been taken if the company had not been dissolved.

(3) It is the duty of the person on whose application the order was made, within 7 days after its making (or such further time as the court may allow), to deliver to the registrar of companies for registration an office copy of the order.

If the person fails to do so, he is liable to a fine and, for continued contravention, to a daily default fine.

(4) Subject to the following provisions, an application under this section may not be made after the end of the period of two years from the date of the dissolution of the company.

(5) An application for the purpose of bringing proceedings against the company–

> (a) for damages in respect of personal injuries (including any sum claimed by virtue of section 1(2)(c) of the Law Reform (Miscellaneous Provisions) Act 1934 (funeral expenses)), or
>
> (b) for damages under the Fatal Accidents Act 1976 or the Damages (Scotland) Act 1976,

may be made at any time; but no order shall be made on such an application if it appears to the court that the proceedings would fail by virtue of any enactment as to the time within which proceedings must be brought.

(6) Nothing in subsection (5) affects the power of the court on making an order under this section to direct that the period between the dissolution of the company and the making of the order shall not count for the purposes of any such enactment.

(7) In subsection (5)(a) "personal injuries" includes any disease and any impairment of a person's physical or mental condition.

...

653 Objection to striking off by person aggrieved

(1) The following applies if a company or any member or creditor of it feels aggrieved by the company having been struck off the register.

(2) The court, on an application by the company or the member or creditor made before the expiration of 20 years from publication in the Gazette of notice under section 652, may, if satisfied that the company was at the time of the striking off carrying on business or in operation, or otherwise that it is just that the company be restored to the register, order the company's name to be restored.

(3) On an office copy of the order being delivered to the registrar of companies for registration the company is deemed to have continued in existence as if its name had not been struck off; and the court may by the order give such directions and make such provisions as seem just for placing the company and all other persons in the same position (as nearly as may be) as if the company's name had not been struck off.

...

COMPANIES ACT 1989

141 Application to declare dissolution of company void

(1) Section 651 of the Companies Act 1985 (power of the court to declare dissolution of company void) is amended as follows.

(2), (3)...[1]

(4) An application may be made under section 651(5) of the Companies Act 1985 as inserted by subsection (3) above (proceedings for damages for personal injury, &c) in relation to a company dissolved before the commencement of this section notwithstanding that the time within which the dissolution might formerly have been declared void under that section had expired before commencement.

But no such application shall be made in relation to a company dissolved more than twenty years before the commencement of this section.

(5) Except as provided by subsection (4), the amendments made by this section do not apply in relation to a company which was dissolved more than two years before the commencement of this section.

[1] Section 141(2) and (3) amended s 651(4) and (5) of the Companies Act 1985. See Appendix A above.

Schedule 1: Convention on Jurisdiction and Enforcement of Judgments in Civil and Commercial Matters

Title I. Scope

ARTICLE 1

This Convention shall apply in civil and commercial matters whatever the nature of the court or tribunal. It shall not extend, in particular, to revenue, customs or administrative matters.

The Convention shall not apply to:

(1) the status or legal capacity of natural persons, rights in property arising out of a matrimonial relationship, wills and succession;

(2) bankruptcy, proceedings relating to the winding-up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings;

(3) social security;

(4) arbitration.

Section 3: Jurisdiction in matters relating to insurance

ARTICLE 7

In matters relating to insurance, jurisdiction shall be determined by this Section, without prejudice to the provisions of Articles 4 and 5(5).

ARTICLE 8

An insurer domiciled in a Contracting State may be sued:

(1) in the courts of the State where he is domiciled, or

(2) in another Contracting State, in the courts for the place where the policy-holder is domiciled, or

(3) if he is a co-insurer, in the courts of a Contracting State in which proceedings are brought against the leading insurer.

An insurer who is not domiciled in a Contracting State but has a branch, agency or other establishment in one of the Contracting States shall, in disputes arising out of the operations of the branch, agency or establishment, be deemed to be domiciled in that State.

ARTICLE 9

In respect of liability insurance or insurance of immovable property, the insurer may in addition be sued in the courts for the place where the harmful event occurred. The same applies if movable and immovable property are covered by the same insurance policy and both are adversely affected by the same contingency.

ARTICLE 10

In respect of liability insurance, the insurer may also, if the law of the court permits it, be joined in proceedings which the injured party has brought against the insured.

The provisions of Articles 7, 8 and 9 shall apply to actions brought by the insured party directly against the insurer, where such direct actions are permitted.

If the law governing such direct actions provides that the policy-holder or the insured may be joined as a party to the action, the same court shall have jurisdiction over them.

ARTICLE 11

Without prejudice to the provisions of the third paragraph of Article 10, an insurer may bring proceedings only in the courts of the Contracting State in which the defendant is domiciled, irrespective of whether he is the policy-holder, the insured or a beneficiary.

The provisions of this Section shall not affect the right to bring a counterclaim in the court in which, in accordance with this Section, the original claim is pending.

ARTICLE 12

The provisions of this Section may be departed from only by an agreement on jurisdiction:

(1) which is entered into after the dispute has arisen, or

(2) which allows the policy-holder, the insured or a beneficiary to bring proceedings in courts other than those indicated in this Section, or

(3) which is concluded between a policy-holder and an insurer, both of whom are at the time of conclusion of the contract domiciled or habitually resident in the same Contracting State, and which has the effect of conferring jurisdiction on the courts of that State even if the harmful event were to occur abroad, provided that such an agreement is not contrary to the law of that State, or

(4) which is concluded with a policy-holder who is not domiciled in a Contracting State, except in so far as the insurance is compulsory or relates to immovable property in a Contracting State, or

(5) which relates to a contract of insurance in so far as it covers one or more of the risks set out in Article 12A.

ARTICLE 12A

The following are the risks referred to in Article 12(5):

(1) Any loss of or damage to

(a) sea-going ships, installations situated offshore or on the high seas, or aircraft, arising from perils which relate to their use for commercial purposes,

(b) goods in transit other than passengers' baggage where the transit consists of or includes carriage by such ships or aircraft,

(2) Any liability, other than for bodily injury to passengers or loss of or damage to their baggage,

(a) arising out of the use or operation of ships, installations or aircraft as referred to in (1)(a) above in so far as the law of the Contracting State in which such aircraft are registered does not prohibit agreements on jurisdiction regarding insurance of such risks,

(b) for loss or damage caused by goods in transit as described in (1)(b) above;

(3) Any financial loss connected with the use or operation of ships, installations or aircraft as referred to in (1)(a) above, in particular loss of freight or charter-hire;

(4) Any risk or interest connected with any of those referred to in (1) to (3) above.

THE DRAFT EU CONVENTION ON INSOLVENCY PROCEEDINGS[2]

1.1 The EU Convention provides for the recognition by Convention states of insolvency proceedings in other Convention states. It was approved by the Council of Ministers in 1995 but was not signed by the United Kingdom during the period fixed for signature.[3] We are not aware of any current plans to revive the Convention, although it is possible that it may be revived in future.

1.2 The Convention provides that main proceedings should be brought in one Contracting State but that secondary proceedings can be brought in others to allow local creditors to protect their interests.[4] The main bankruptcy proceedings are to be brought in the Contracting State where the centre of the debtor's main interests is located. As regards companies, this is the place of the company's registered office.[5] As regards individuals, this appears to be their professional domicile or habitual place of residence.[6]

1.3 Article 3 provides that secondary proceedings may be brought if the debtor "possesses an establishment" within the Contracting State. Article 2(h) defines "establishment" as "any place of operations where the debtor carries out a non-transitory economic activity with human means and goods".[7] It seems, therefore, that secondary proceedings could only be started in the English court if the insured has an "establishment" in this country: where the insured had no "goods" here (and where his only asset was a claim under an insurance policy), secondary proceedings could probably not be brought.[8]

[2] The draft Convention was the subject of consultation by the Insolvency Service in February 1996.

[3] Ie by 23 May 1996.

[4] Article 3. Article 5 provides that the opening of insolvency proceedings shall not affect the rights in rem of creditors in respect of assets in another Contracting State "at the time of the opening of proceedings". It is unlikely that third party rights under the 1930 Act would be covered by this definition.

[5] Art 3, para 1.

[6] See para 44 of the explanatory note to the Convention.

[7] Paragraph 39 of the Explanatory Report notes: "it should be mentioned that Art 3(2) was one of the most debated concepts throughout the negotiations. Several Contracting States wished to have the possibility of basing territorial proceedings on the presence of assets (assigned to an economic activity) without the debtor having to be established there. However, for the sake of a global consensus on the Convention, those States agreed to abandon the presence of assets as a basis for international competence provided that the concept of establishment is interpreted in a broad manner, but consistently with the text of the Convention". Paragraph 40 notes: "The emphasis on an economic activity having to be carried out using human means shows the need for a minimum level of organisation. A purely occasional place of operations cannot be classified as an "establishment". A certain stability is required. The negative formula ("non-transitory") aims to avoid minimum time requirements. The decisive factor is how the activity appears externally, and not the intention of the debtor".

[8] See the Response of the Joint Sub-Committee on Insolvency Law of the Law Society's Consumer and Commercial Law and Company Law Committees to the Insolvency Service's Consultative Document of February 1996, April 1996. The Law Society's

1.4 The Convention provides for the co-ordination of main and secondary proceedings. For example, liquidators in all proceedings have a duty to collaborate and to exchange information and can lodge claims in other insolvency proceedings. The liquidator in the main proceedings can request a stay on the liquidation of the assets in the secondary proceedings.

1.5 The Convention only applies to insolvency proceedings which satisfy the requirements of article 1. These are listed in an annex to the Convention and do not include receiverships (which are caught by the 1930 Act).

Insurance Law Sub-Committee of the Consumer and Commercial Law Committees has suggested, however, that the word "goods" in the English version of the Convention is a mistranslation of the term "biens" in the French text, which might include non-corporeal property, including claims under an insurance policy. Article 55 of the Convention provides that each text is equally authentic, but the Sub-Committee suggests that the European Court of Justice might interpret Articles 2 and 3 in accordance with the French meaning. This could have the effect of allowing secondary proceedings to be brought in the UK when there is a claim against a UK underwriter.

APPENDIX B
PROCEDURAL RULES

RULES OF THE SUPREME COURT

Consolidation, etc., of causes or matters

RSC Order 4, rule 9

9.-(1) Where two or more causes or matters are pending in the same Division and it appears to the Court -

(a) that some common question of law or fact arises in both or all of them, or

(b) that the rights to relief claimed therein are in respect of or arise out of the same transaction or series of transactions, or

(c) that for some other reason it is desirable to make an order under this paragraph

the Court may order those causes or matters to be consolidated on such terms as it thinks just or may order them to be tried at the same time or one immediately after another or may order any of them to be stayed until after the determination of any other of them.

(2) Where the Court makes an order under paragraph (1) that two or more causes or matters are to be tried at the same time but no order is made for those causes or matters to be consolidated, then, a party to one of those cause or matters may be treated as if he were a party to any other of those causes or matters for the purpose of making an order for costs against him or in his favour.

Principal cases in which service of writ out of jurisdiction is permissible

RSC Order 11, rule 1

1.-(1) Provided that the writ does not contain any claim mentioned in Order 75, r.2(1)[1] and it is not a writ to which paragraph (2) of this rule applies, service of a writ out of the jurisdiction is permissible with the leave of the Court if in the action begun by the writ-

(a) relief is sought against a person domiciled within the jurisdiction;

(c) the claim is brought against a person duly served within or out of the jurisdiction and a person out of the jurisdiction is a necessary or proper party thereto;

[1] Which relates to proceedings under the Merchant Shipping Act 1995.

(d) the claim is brought to enforce, rescind, dissolve, annul or otherwise affect a contract, or to recover damages or obtain other relief in respect of the breach of a contract, being (in either case) a contract which-

(i) was made within the jurisdiction, or

(ii) was made by or through an agent trading or residing within the jurisdiction on behalf of a principal trading or residing out of the jurisdiction, or

(iii) is by its terms, or by implication, governed by English law,[2] or

(iv) contains a term to the effect that the High Court shall have jurisdiction to hear and determine any action in respect of the contract;

(e) the claim is brought in respect of a breach committed within the jurisdiction of a contract made within or out of the jurisdiction, and irrespective of the fact, if such be the case, that the breach was preceded or accompanied by a breach committed out of the jurisdiction that rendered impossible the performance of so much of the contract as ought to have been performed within the jurisdiction;

(f) the claim is founded on a tort and the damage was sustained, or resulted from an act committed, within the jurisdiction;

(o) the claim is brought under the Nuclear Installations Act 1965[3] or in respect of contributions under the Social Security Act 1975;

…

Joinder of parties[4]

RSC Order 15, rule 4

4.-(1) Subject to rule 5(1)[5] two or more persons may be joined together in one action as plaintiffs or as defendants with the leave of the Court or where

[2] In *DVA v Voest Alpine* [1997] 2 Lloyd's Rep 279, 286, the Court of Appeal held that leave to serve a defendant out of the jurisdiction could be granted to the transferee or assignee of contractual rights under a contract governed by English law under Order 11, rule (d)(iii).

[3] See para 2.4 above.

[4] We discussed in paras 4.20-4.26 above whether a third party or insured could join an insurer into proceedings between the third party and the insured and whether the insurer could apply to be joined to such proceedings.

[5] Which allows the court to order separate trials. See below.

(a) if separate actions were brought by or against each of them, as the case may be, some common question of law or fact would arise in all the actions, and

(b) all rights to relief claimed in the action (whether they are joint, several or alternative) are in respect of or arise out of the same transaction or series of transactions.

Misjoinder and nonjoinder of parties

RSC Order 15, rule 6

6.-(2) Subject to the provisions of this rule, at any stage of the proceedings in any cause or matter the Court may on such terms as it thinks just and either of its own motion or on application[6]

…

(b) order any or the following persons to be added as a party, namely -

(i) any person who ought to have been joined as a party or whose presence before the Court is necessary to ensure that all matters in dispute in the cause or matter may be effectually and completely determined and adjudicated upon, or

(ii) any person between whom and any party to the cause or matter there may exist a question or issue arising out of or relating to or connected with any relief or remedy claimed in the cause or matter[7] which in the opinion of the Court it would be just and convenient to determine as between him and that party as well as between the parties to the cause or matter.[8]

[6] The court has power to add or substitute a defendant on the application of the defendant and of a person not already a party, even if this is against the wishes of the plaintiff. *Amon v Raphael Tuck & Sons* [1956] 1 QB 357.

[7] One of the main objects of this rule is to prevent multiplicity of proceedings. See RSC O 15, r 6(8). Intervention will be permitted where the proprietary or pecuniary interests of the intervener are directly affected or where he may be liable to satisfy any judgment: RSC O 15, r 6(9). The Motor Insurers' Bureau can be joined in an action arising out of a road traffic accident as any judgment can be enforceable against them: see *Gurtner v Circuit* [1968] 2 QB 587. See also *Wood v Perfection Travel* [1996] LRLR 233, discussed at para 4.25-4.26 above.

[8] The court may refuse to make an order adding or substituting a defendant where this would have the effect of adding a new cause of action. RSC O 15, r 6(6). See *Raleigh v Goschen* [1898] 1 Ch 81. Cf *Ashley v Taylor* (1878) 10 Ch D 768. The court may add a party if the presence of the party before it is necessary to ensure that all matters in dispute are effectively dealt with, even if there is no cause of action against that party. RSC 15, r 6(6). See *TSB Private Bank International SA v Chabra* [1992] 1 WLR 231. The court has no jurisdiction to order joinder where the cause or matter is not liable to be defeated by the non-joinder, where the proposed defendants were not persons who ought to have been sued in the first instance and where they were not persons whose presence as defendants was necessary to enable the court effectually to adjudicate on all the questions involved. RSC 15, r 6(6). See *Amon v Raphael Tuck & Sons* [1956] 1 QB 357, at 369 and *Miguel Sanchez and Compania SL v The Result* [1958] p 174, at 184; See also our discussion of *Carpenter v*

Change of parties by reason of death, etc.

RSC Order 15, rule 7

7.-(2)Where at any stage of the proceedings in any cause or matter the interest or liability of any party is assigned or transmitted to or devolves upon some other person, the Court may, if it thinks it necessary in order to ensure that all matters in dispute in the cause or matter may be effectually and completely determined and adjudicated upon, order[9] that other person to be made a party to the cause or matter and the proceedings to be carried on as if he had been substituted for the first mentioned party.[10]

An application for an order under this paragraph may be made *ex parte*.

Declaratory judgment

RSC Order 15, rule 16

16. No action or other proceeding shall be open to objection on the ground that a merely declaratory judgment or order is sought thereby, and the Court may make binding declarations of right whether or not any consequential relief is or could be claimed.[11]

Third party notice

RSC Order 16, rule 1

1.(1) Where in any action a defendant who has given notice of intention to defend-

(a) claims against a person not already a party to the action any contribution or indemnity; or

(b) claims against such a person any relief or remedy relating to or connected with the original subject-matter of the action and

Ebblewhite [1939] 1 KB 347*; Meadows Indemnity Co Ltd v Insurance Corp of Ireland* [1989] 2 Lloyd's Rep 298; *Wood v Perfection Travel* [1996] LRLR 233; *Brice v Wackerbarth* [1974] 2 Lloyd's Rep 274 and *Spelling Goldberg Productions v BPC Publishing Ltd* [1981] RPC 280 at paras 4.21-4.26 above.

9 The application procedure is set out at O 17, r 7(21) which starts by noting that it must be shown that the order is necessary then continues: "The application is made ex parte to the Master or Registrar supported by an affidavit showing (1) the nature of the action and the stage at which it has arrived; (2) the change that has occurred; (3) the interest or liability of the party by or against whom it is proposed to carry on the proceedings; (4) the fact, if necessary, that the cause of action survives or continues; and (5) what order is asked".

10 The effect of substitution is described in O 15, r 8(7): "Once the substituted person becomes a party in the action, the following consequences ensue, namely: (1) the substituted party is placed in the exact position of the party whom he has replaced ...; and (2) everything done in the course of the proceedings before the order was made under r 6 or r 7, is fully effective and operative in relation to the substituted party as they had been in relation to the party whom he has replaced ...".

11 We discuss at paras 4.21-4.26 above whether a third party claimant under the 1930 Act could seek a declaration from the insurer under RSC O 15.

substantially the same as some relief or remedy claimed by the plaintiff; or

(c) requires that any question or issue relating to or connected with the original subject-matter of the action should be determined not only as between the plaintiff and the defendant but also as between either or both of them and a person not already a party to the action;

then ... the defendant may issue ... a third party notice ....[12]

…

(3) Where a third party notice is served on a person against whom it is issued, he shall as from the time of service be a party to the action...with all the same rights in respect of his defence against any claim made against him in the notice and otherwise as if he had been duly sued in the ordinary way by the defendant by whom the notice is issued.

Time, etc. of trial of questions or issues

RSC Order 33, rule 3[13]

3. The Court may order any question or issue arising in a cause or matter, whether of fact or law or partly of fact and partly of law, and whether raised by the pleadings or otherwise, to be tried before, at or after the trial of the cause or matter, and may give directions as to the matter in which the question or issue shall be stated.[14]

[12] In *Brice v Wackerbarth* [1974] 2 Lloyd's Rep 274, the Court of Appeal allowed an insured defendant to join his insurer to proceedings against it to seek a declaration that the insurer was liable to indemnify it. See para 4.24 above.

[13] See also RSC O 18, r 11(2). Under the Draft Civil Proceedings Rules 1.3 (e), the court's duty to further the overriding objective of dealing with cases justly (rule 1.1) includes the duty to decide the order in which issues are to be resolved. Its powers of case management also include the power to decide the order in which issues are to be tried and to direct a separate trial of any issue, (rule 5.1 (1) (f), (g)).

[14] In *Ashmore v Corporation of Lloyd's* [1992] 1 WLR 446. See also the approach of the court in *Caspian Basin Specialised Emergency Salvage Administration and Another v Bouygus Offshore South Africa and Others*, *The Times* 3 July 1997, where Rix J held that a declaration of limitation of liability under the Merchant Shipping Act 1995 could be sought before liability had been established as the determination of the former could "sensibly and profitably precede the determination of liability" in order to enable the parties "to know if the matter was worth litigating". See also draft rules 1.3 and 5.1 of the Draft Civil Proceedings Rules, set out below.

Order 5

Causes of Action and Parties

JOINDER OF CAUSES OF ACTION (O 5, R 1)

1. Subject to rule 3, a plaintiff may in one action claim relief against the same defendant in respect of more than one cause of action-

(a) if the plaintiff claims, and the defendant is alleged to be liable, in the same capacity in respect of all the causes of action, or

(b) if the plaintiff claims or the defendant is alleged to be liable in the capacity of executor or administrator of an estate in respect of one or more of the causes of action and in his personal capacity but with reference to the same estate in respect of all the others, or

(c) with the leave of the court.

JOINDER OF PARTIES (O 5, R 2)

2. Subject to rule 3, two or more persons may be joined together in one action as plaintiffs or as defendants-

(a) where all rights to relief claimed in the action (whether they are joint, several or in the alternative) are in respect of or arise out of the same transaction or series of transactions and if separate actions were brought by or against each of those persons, some common question of law or fact would arise, or

(b) in any other case, with the leave of the court.

POWER TO ORDER SEPARATE TRIALS (O 5, R 3)

3. If it appears to the court that the joinder of two or more causes of action or of two or more plaintiffs or defendants, in the same action may embarrass or delay the trial or is otherwise inconvenient, the court may order separate trials or make such other order as may be expedient.

MISJOINDER OR NONJOINDER OF PARTIES (O 5, R 4)

4. No action or matter shall be defeated by reason of the misjoinder or nonjoinder of any parties and the court may in any action or matter determine the issues or questions in dispute so far as they affect the rights and interests of the persons who are parties to the action or matter.

Order 12

Third Party and Similar Proceedings

THIRD PARTY NOTICE (O 12, R 1)

1.- (1) Where in any action a defendant-

(a) claims against a person not already a party to the action any contribution or indemnity, or

(b) claims against such a person any relief or remedy relating to or connected with the original subject-matter of the action and substantially the same as some remedy or relief claimed by the plaintiff, or

(c) requires any question or issue relating to or connected with the original subject-matter of the action to be determined not only as between the plaintiff and the defendant but also as between either or both of them and a person not already a party to the action,

then, subject to paragraph (2), the defendant may issue a notice (in this Order referred to as a third-party notice) containing a statement of the nature and grounds of the claim made by the defendant or, as the case may be, of the question or issue required to be determined.

Order 13

Applications and Orders in the Course of Proceedings

DIRECTIONS (O 13, R 2)

2.-(1) In any action or matter the court may at any time, on application or of its own motion, give such directions as it thinks proper with regard to any matter arising in the course of the proceedings.

(2) In the exercise of the power conferred by paragraph (1) the court may, in particular-

(c) order one or more questions or issues to be tried before the others.

APPLICATION OF RSC RELATING TO OTHER INTERLOCUTORY MATTER (O 13, R 7)

7. (1) Subject to the following paragraphs of this rule, the provisions of the RSC with regard to-

(g) the exercise of the powers conferred by sections 33 to 35 of the Supreme Court Act 1981;

shall apply in relation to proceedings or, as the case may be, subsequent proceedings in a county court as they apply in relation to proceedings or subsequent proceedings in the High Court.

ORDER FOR CONSOLIDATION ETC. (O 13, R 9)

9.(1) Where two or more actions or matters are pending in the same county court and it appears to the court-

(a) that some common question of law or fact arises in both or all of them, or

(b) that the rights to relief claimed are in respect of or arise out of the same transaction or series of transactions, or

(c) that for some other reason it is desirable to make an order under this rule,

the court may order that the actions or matters be consolidated or may order them to be tried at the same time or one immediately after another or may order any of them to be stayed until the determination of any other of them.

(2) An order under paragraph (1) may be made by the court of its own motion or on the application of any party on notice to all other parties to the actions or matters affected.

Order 15

Amendment

AMENDMENT BY ORDER (O 15, R 1)

1.-(1) Without prejudice to Order 5, rules 8 and 11, and rule 2 of this Order, but subject to the following paragraphs of this rule, the court may, in any action or matter, by order allow or direct-

(a) any originating process, pleading or any other document in the proceedings to be amended, or

(b) any person to be added, struck out or substituted as a party to the proceedings, if the amendment, whether falling within sub-paragraph (a) or (b), is such that the High Court would have power to allow in a like case.

ACCESS TO JUSTICE, DRAFT CIVIL PROCEEDINGS RULES, JULY 1996[15]

Court's duty to manage cases[16]

1.3 The court must further the overriding objective by actively managing cases, and in particular-

(e) by deciding the order in which issues are to be resolved;

The Court's general powers of management[17]

5.1

(1) The court may-

(f) decide the order in which issues are to be tried;

(g) direct a separate trial of any issue;

...

Persons to whom notice of an application must be given [18]

10.5

(1) If notice of an application must be given, the applicant must serve notice on-

(b) any other person to whom the court's order will apply, if the application is granted.

...

Change of parties - general[19]

18.1

(2) The court may add a new party to the proceedings if-

(a) it can resolve the matter in dispute in the proceedings more effectively by adding a new party;

[15] Access to Justice: Draft Civil Proceedings Rules. The Right Honourable the Lord Woolf, Master of the Rolls. HMSO, July 1996.

[16] Para 12.36, n 91.

[17] Para 12.36, n 91.

[18] Para 12.44, n 109.

[19] Para 12.36, n 91.

(b) the new party has a claim connected to the matters in dispute in the proceedings and the court can resolve it effectively by adding it to the proceedings.

(3) The court may substitute a new party for an existing one if-

(a) the existing party's interest or liability has passed to the new party; and

(b) the court can resolve the matters in dispute in the proceedings more effectively by substituting the new party for the existing party.

Special provisions about adding or substituting parties after the end of a relevant limitation period

18.4

(1) This rule allows a change of parties after the end of a period of limitation under-

(a) the Limitation Act 1980; or

(b) the Foreign Limitation Periods Act 1984.

(2) The court may add or substitute a party if-

(a) the relevant limitation period was current when proceedings were started; and

(b) there has been a relevant passing of interest or liability; and

(c) the addition or substitution is necessary.

(3) There is a relevant passing of interest or liability-

(a) for the purpose of substituting a party, if the whole of an existing party's interest or liability has passed to the person proposed to be substituted; and

(b) for the purpose of adding a party, if part of an existing party's interest or liability has passed to the person proposed to be added.

(5) In addition, in a claim for personal injuries the court may add or substitute a party where it directs that-

(a) section 11 (special time limit for claims for personal injuries); or

(b) section 12 (special time limit for claims under fatal accidents legislation)

of the Limitation Act 1980 shall not apply to the claim by or against the new party.

(Rule 19.2 deals with other changes after the end of a relevant limitation period.)

Chapter 22

Closing records

22.3.-(1) The court shall, on the day on which the period allowed for adjustment in a cause expires, pronounce an interlocutor closing the record.

(2) The pursuer shall, within four weeks after the date of the interlocutor closing the record-

(a) send not less than six copies of the closed record to every other party; and

(b) lodge three copies of the closed record in process.

(3) If the pursuer fails to comply with either of the requirements of paragraph (2), the court may, on the motion of the other party, grant decree of dismissal.

(4) A closed record shall consist of the pleadings of the parties and the interlocutors pronounced in the cause.

(5) The pursuer shall, on lodging the copies of the closed record as required by paragraph (2), enrol a motion craving the court-

(a) where parties have agreed on further procedure, of consent-

(i) to appoint the cause to the Procedure Roll for consideration of all the preliminary pleas of parties or such of the pleas as may be specified;

(ii) to allow to parties a preliminary proof on specified matters or in respect of specified pleas;

(iii) to allow to parties a proof before answer of their respective averments under reservation of such preliminary pleas as may be specified;

(iv) to allow a proof

(v) to allow issues for jury trial; or

(vi) to make some other specified order; or

(b) where parties have been unable to agree on further procedure to appoint the cause to the By Order (Adjustment) Roll.

(6) In a cause which is one of more than one cause arising out of the same cause of action, the court may, on or after pronouncing an interlocutor ordering further procedure under paragraph (5)-

(a) on the motion of a party to that cause, and

(b) after hearing parties to all those causes,

appoint that cause or any other of those causes to be the leading cause and to sist the other causes pending the determination of the leading cause.

(7) In this rule, "pursuer" includes petitioner, noter or minuter, as the case may be.

Chapter 24

Amendment of Pleadings

Powers of court

24.1.-(1) In any cause the court may, at any time before final judgment, allow an amendment mentioned in paragraph (2).

(2) Paragraph (1) applies to the following amendments-

(a) an amendment of a principal writ which may be necessary for the purpose of determining the real question in controversy between the parties, notwithstanding that in consequence of such amendment-

(i) the sum sued for in a summons is increased or restricted; or

(ii) a different remedy from that originally concluded for or craved is sought;

(b) an amendment which may be necessary-

(i) to correct or supplement the designation of a party to the cause;

(ii) to enable a party who has sued or has been sued in his own right to sue or be sued in a representative capacity;

(iii) to enable a party who has sued or has been sued in a representative capacity to sue or be sued in his own right or in a different representative capacity;

(iv) to add the name of an additional pursuer, a petitioner or person whose concurrence is necessary;

(v) where the cause has been commenced or presented in the name of the wrong person, or it is doubtful whether it has been commenced or presented in the name of the right person, to allow any other person to be sisted in substitution for, or in addition to, the original person; or

(vi) to direct conclusions against a third party brought into an action under Chapter 26 (third party procedure);

(c) an amendment of a condescendence, defences, answers, pleas-in-law or other pleadings which may be necessary for determining the real question in controversy between the parties; and

(d) where it appears that all parties having an interest have not been called or that the cause has been directed against the wrong person, an amendment inserting in the instance of the principal writ an additional or substitute party and directing existing or additional conclusions or craves, averments and pleas-in-law against that party.[20]

Chapter 26

Third Party Procedure

Applications for third party notice

26.1.-(1) Where, in an action, a defender claims that-

(a) he has in respect of the subject-matter of the action a right of contribution, relief or indemnity against any person who is not a party to the action,[21] or

(b) a person whom the pursuer is not bound to call as a defender should be made a party to the action along with the defender in respect that such person is-

(i) solely liable, or jointly or jointly and severally liable with the defender, to the pursuer in respect of the subject-matter of the action, or

(ii) liable to the defender in respect of a claim arising from or in connection with the liability, if any, of the defender to the pursuer, he may apply by motion for an order for service of a third party notice on that other person in Form 26.1-A for the purpose of convening that other person as a third party to the action.

(2) Where-

(a) a pursuer against whom a counterclaim has been made, or

(b) a third party convened in the action,

seeks, in relation to the claim against him, to make against a person who is not a party, a claim mentioned in paragraph (1) as a claim which could be made by a defender against a third party, he shall apply by motion for an order for service of a third party notice in Form 26.1-B (notice by pursuer) or Form 26.1-C (notice by

[20] Insurers can themselves apply to become (or be sisted as) parties to the proceedings in respect of any interest they have. *Thomson v Bose* (unreported) 17 December 1993.

[21] The insured can join in his insurer as a third party to proceedings against him. *Barton v William Low and Co Ltd* 1968 SLT (Notes) 27.

third party), as the case may be, in the same manner as a defender under that paragraph; and rules 26.2 and 26.7 shall, with the necessary modifications, apply to such a claim as they apply in relation to such a claim by a defender.

Chapter 36

Proofs

Hearing parts of proof separately

36.1.-(1) In any cause the court may-

(a) at its own instance, or

(b) on the motion of any party,

order that proof on liability or any other specified issue be heard separately from proof on any other issue and determine the order in which the proofs shall be heard.

(2) The court shall pronounce such interlocutor as it thinks fit at the conclusion of the first proof of any cause ordered to be heard in separate parts under paragraph (1).

APPENDIX C
STATISTICS

CLAIMS BROUGHT UNDER THE 1930 ACT: ABI STATISTICS

1.1. In December 1996 the ABI sought information from a number of its members on their experience of the 1930 Act. The ABI's findings were that insurers had very few cases involving the 1930 Act. They suggested that there had been no more than one hundred and probably nearer to sixty or seventy cases involving the 1930 Act. Generally, the insurer dealt directly with the third party, without reference to the 1930 Act and without obliging the third party to obtain a judgment unless liability or the status of the cover was in dispute.

1.2. Many of the cases involving the 1930 Act were claims involving public liability and employers liability. The ABI represented the incidence of 1930 Act cases in the context of the different classes of general business as follows:

[A Pie Chart goes here]

LAW COMMISSION SURVEY OF APPLICATIONS TO RESTORE DISSOLVED COMPANIES TO THE REGISTER

1.3. In December 1996 and January 1997 we analysed over 1,000 applications under sections 651 and 653 of the Companies Act 1985.[1]

THE NATURE OF THE THIRD PARTY'S UNDERLYING CLAIM

1.4. The nature of the third party's underlying claim against the insured and information on whether he intended to proceed under the 1930 Act was usually clear from the application. Those applications[2] which were clearly made with the intention of proceeding under the 1930 Act could be broken down into the following categories:

[A Pie Chart goes here]

[1] 169 of the applications involved situations in which the 1930 Act was applicable. (It was specifically pleaded, however, in only 60 of those applications).

[2] 169 applications.

1.5. The fact that these claims involved actions against companies rather than individuals explains the larger number of applications involving employer's liability and the small number of claims involving professional liability.

THE APPLICATION PROCEDURE

1.6. In many of the applications which we examined, applicants filed long affidavits setting out the particulars of their underlying claims against the company, as well as affidavits of service detailing the parties who had received notification of their applications. In the cases we surveyed, every application to restore was granted.[1]

[1] We discuss at paras 4.38-4.51 above the costs and other implications for third parties claimants under the Act of having to restore dissolved companies to the register.

APPENDIX D
INSOLVENCY CLAUSE RECOMMENDED BY THE ABI/LIRMA AND ILU

Where an Insolvency Event occurs in relation to the Reinsured the following terms apply (and, in the event of any inconsistency between these terms and any other terms of this Agreement, these terms shall prevail):

1. Notwithstanding any requirement in this Agreement that the Reinsured shall actually make payment in discharge of its liability to its policyholder before becoming entitled to payment from the Reinsurer:

(a) the Reinsurer shall be liable to pay the Reinsured even though the Reinsured is unable actually to pay, or discharge its liability to, its policyholder; but

(b) nothing in this clause shall operate to accelerate the date for payment by the Reinsurer of any sum which may be payable to the Reinsured, which sum shall only become payable as and when the Reinsured would have discharged, by actual payment, its liability for its current net loss but for it being the subject of any Insolvency Event.

2. The existence, quantum, valuation and date for payment of any sum which the Reinsurer is liable to pay the Reinsured under this Agreement shall be those and only those for which the Reinsurer would be liable to the Reinsured if the liability of the Reinsured to its policyholders had been determined without reference to any term in any composition or scheme of arrangement or any similar such arrangement, entered into between the Reinsured and all or any part of its policyholders, unless and until the Reinsurer serves written notice to the contrary on the Reinsured in relation to any composition or scheme of arrangement.

3. The Reinsurer shall be entitled (but not obliged) to set-off, against any sum which it may be liable to pay the reinsured, any sum for which the Reinsured is liable to pay the Reinsurer.

An Insolvency Event shall occur if:

A (i) (in relation to (1),(2) and (3) above) a winding-up petition is presented in respect of the Reinsured or a provisional liquidator is appointed over it or the if the Reinsured goes into administration, administrative receivership or receivership or if the Reinsured has a scheme of arrangement or voluntary arrangement proposed in relation to all or any part of its affairs; or

(ii) (in relation to (1) above) if the reinsured goes into compulsory or voluntary liquidation;

or, in each case, if the Reinsured becomes subject to any other similar insolvency process (whether under the laws of England and Wales or elsewhere) and

B the reinsured is unable to pay its debts as and when they fall due within the meaning of section 123 of the Insolvency Act 1986 (or any statutory amendment or re-enactment of that section).

APPENDIX E
THE CITY OF LONDON LAW SOCIETY INSURANCE SUB-COMMITTEE

The Proposed Third Parties (Rights Against Insurers) Act 1997

An Outline of Provisions

1. The Third Parties (Rights Against Insurers) Act 1930 shall apply only to policies of insurance having inception dates up to and including 31 December 1997, and shall have no effect whatsoever in respect of policies with inception dates thereafter.

2. This Act shall apply to policies of compulsory liability insurance having inception dates on or after 1 January 1998.

3. Liability insurance is compulsory for the purposes of this Act if it is required by virtue of any Statute, Statutory Instrument, Regulation or Bylaw.

4. This Act shall apply, where liability insurance is compulsory, to mutual insurance associations and indemnity funds analogous to contracts of insurance, including (without limitation) the Solicitors Indemnity Fund.

5. Where a third party claimant has an actual or contingent claim against any company or individual insured under any contract of insurance to which this Act applies, upon the occurrence of the later of:

(a) The completion of the exchange of statements of case in any Court action or arbitration in which the claim has not already been struck out; and

(b) The passing, on grounds of insolvency, of a winding-up resolution or the making of a winding-up or Bankruptcy order or the appointment of a Provisional Liquidator,

there shall be transferred to any such claimant all the rights of the relevant company or individual under that contract of insurance in relation to the particular claim.

6. The rights transferred by 5 above shall include, without limitation:

(a) the right to commence proceedings (including arbitration) against any relevant insurer or to continue in his own name (assuming the risk of costs incurred thenceforth) any such proceedings already begun; and

(b) the right to be given all such information as may be necessary to establish whether or not he the claimant stands to benefit from any relevant insurance.

7. Any person including, without limitation, any insured, insurer, broker, underwriting agent, liquidator, administrator, provisional liquidator or trustee in bankruptcy, having within his possession, custody or power any of the information

referred to in 6(b) above shall, upon written request by the third party claimant, produce such information to him or his representative promptly.

8. Upon the transfer of rights pursuant to 5 above:

(a) the third party claimant shall be substituted for the insured in any proceedings (including arbitration) already commenced between the insured and the insurer, thereby assuming the risk of costs incurred thenceforth, which proceeding shall be heard together with the principal claim if practicable; or

(b) if there are no proceedings in progress, the third party claimant shall promptly require the insurer to state, also promptly, whether there are any coverage issues and, if so, shall join the insurer into the action (including arbitration) against the insured and any coverage issues shall be heard to together with the principal claim.

9. Any provision in any contract of compulsory insurance which:

(a) directly or indirectly vitiates it to any degree whatever in the event of insolvency; or

(b) requires the insured to perform any act or comply with any condition or be in any particular state, which requirement it cannot satisfy by reason of its insolvency; or

(c) prohibits the disclosure of any information about it,

shall be void and of no effect whatever as against any third party claimant.

10. Any agreement between the insured and the insurer, whether made before or after insolvency, which purports to reduce or remove the insurance available to a third party shall be void and of no effect whatsoever.

11. The bankruptcy or death of any individual, and the liquidation or administration or dissolution of any company, insured under any contract of insurance to which this Act applies shall not result in any claim to which the provisions of 5 or 8(a) above apply, or might otherwise apply, being stayed or struck out.

APPENDIX F
SUMMARY OF SCHEMES OF THIRD PARTY RIGHTS AGAINST INSURERS IN OTHER JURISDICTIONS

1.1 In this appendix, we look briefly at some of the schemes of third party rights which have been introduced in other jurisdictions. We do not examine broader issues, such as the ability of insurers to rely on policy defences generally nor duties of disclosure.[1]

AUSTRALIAN COMMONWEALTH LEGISLATION

1.2 Under Australian Commonwealth legislation, which applies in all states and territories, third parties do not have a right of direct action against insurers where the insured is insolvent, but have rights over the insurance monies in preference to those of other creditors. Third parties have a right of direct action against insurers in cases where the insured has died or disappeared.[2]

The rights of third parties on the bankruptcy or insolvency of the insured

1.3 Section 117 of the Bankruptcy Act 1966[3] provides that

> 117.-(1) Where-
>
> (a) a bankrupt is or was insured under a contract of insurance against liabilities to third parties; and
>
> (b) a liability against which he is or was so insured has been incurred (whether before or after he became a bankrupt)
>
> the right of the bankrupt to indemnity under the policy vests in the trustee and any amount received by the trustee from the insurer under the policy in respect of the liability shall, if the liability has not already been satisfied, be paid in full forthwith to the third party to whom it has been incurred.
>
> (2) The last preceding sub-section does not limit the rights of the third party in respect of any balance due to him after the payment referred to in that sub-section has been made.

[1] Where necessary, we have referred to such broader issues in the main text of this paper. We do, however, discuss briefly here the operation of s 54 of the Australian Insurance Contracts Act 1984 and of s 11 of the New Zealand Law Reform Act 1977 because of the relevance of these provisions to our considerations of restrictions on the insurer's ability to rely on policy defences. See paras 14.22, n 36 and 14.25 above.

[2] In the Australian Capital Territory and New South Wales, state legislation provides third parties with a right to enforce a charge over the insurance fund directly against the insurer, regardless of the solvency or otherwise of the insured. The legislation of both states was modelled on s 9 of the New Zealand Law Reform Act 1936 and is discussed at paras 1.9-1.15 below.

[3] Similar provisions are applied to companies which have been wound up by s 562 of the Corporations Law.

(3) This section applies notwithstanding any agreement to the contrary, whether entered into before or after the commencement of this Act.

The rights of third parties on the death or disappearance of the insured

1.4 Section 51 of the Insurance Contracts Act 1984 provides that

> 51.-(1) Where:
>
> (a) the insured under a contract of liability insurance is liable in damages to a person (in this section called the **"third party"**);
>
> (b) the insured has died or cannot, after reasonable enquiry, be found; and
>
> (c) the contract provides insurance cover in respect of the liability;
>
> the third party may recover from the insurer an amount equal to the insurer's liability under the contract in respect of the insured's liability in damages.
>
> (2) A payment under subsection (1) is a discharge, to the extent of the payment, in respect of:
>
> (a) the insurer's liability under the contract; and
>
> (b) the liability of the insured or of his legal personal representative to the third party.
>
> (3) This section does not affect any right that the third party has in respect of the insured's liability, being a right under some other law of the Commonwealth or under a law of a State or Territory.

1.5 It is not clear whether or not a third party must actually have established the liability of the insured before he can proceed under section 51.[4] It appears, however, that the third party may be able to bring proceedings against the insured and the insurer in one action.[5]

[4] See Derrington and Ashton, *The Law of Liability Insurance* (1990) pp 714-715: K Sutton, *Insurance Law in Australia* (2nd ed 1991) p 82 suggests that before a third party can rely on s 51, " ... the assured must either have been found liable or have admitted liability for such loss or damage to the third party". See also the Australian and New Zealand Insurance Reporter, para 27-505. *Insurance Law in Australia* (2nd ed) p 83, suggests that "It is a sine qua non for the operation of the section that the assured is liable in damages to the third party and ... this requirement would have to be established by the injured third party, at least to the extent of a prima facie case, when claiming against the insurer". See also Minter Ellison Morris Fletcher, *The Insurance Contracts Act 1984, The Insurance (Agents and Brokers) Act 1984 and their Regulations - a Handbook* (1992) p 54 where it is suggested that it is "unlikely" that section 51 "will require an actual judgment before the third party can recover".

[5] See Derrington and Ashton, *The Law of Liability Insurance* (1990) p 715: "having obtained judgment against the former, the claimant is then immediately entitled to judgment against the latter, all other things being proved".

The ability of insurers to rely on policy defences against third parties

1.6 It appears also that the insurer can rely on any defence against the third party which he could have relied on as against the insured[6] but that third parties may be able to rely on section 54 of the Insurance Contracts Act in respect of certain conditions and may themselves be able to fulfil certain conditions in the insurance contract.[7]

1.7 Section 54 of the Insurance Contracts Act 1984[8] provides as follows:

> 54.-(1) Subject to this section, where the effect of a contract of insurance would, but for this section, be that the insurer may refuse to pay a claim, either in whole or in part, by reason of some act of the insured or of some other person, being an act that occurred after the contract was entered into but not being an act in respect of which subsection(2) applies, the insurer may not refuse to pay the claim by reason only of that act but his liability in respect of the claim is reduced by the amount that fairly represents the extent to which the insurer's interests were prejudiced as a result of that act.
>
> (2) Subject to the succeeding provisions of this section, where the act could reasonably be regarded as being capable of causing or contributing to a loss in respect of which insurance cover is provided by the contract, the insurer may refuse to pay the claim.
>
> (3) Where the insured proves that no part of the loss that gave rise to the claim was caused by the act, the insurer may not refuse to pay the claim by reason only of the act.
>
> (4) Where the insured proves that some part of the loss that gave rise to the claim was not caused by the act, the insurer may not refuse to pay the claim, so far as it concerns that part of the loss, by reason only of the act.
>
> (5) Where -
>
> (a) the act was necessary to protect the safety of a person or to preserve property; or
>
> (b) it was not reasonably possible for the insured or other person to do the act,

[6] *Ibid*, 719-721: "The insurer is no doubt entitled to rely on any defences that the assured might have had against the third party's claim, and he is also entitled to rely on any defences he might have had against the assured had the latter claimed an indemnity in respect of the third party's claim".

[7] See Derrington and Ashton, *The Law of Liability Insurance* (1990) pp 718-719.

[8] The Australian reform, including the distinction between conduct by the insured which cannot in principle cause a loss and conduct which can is used as a model for reforms proposed by the National Consumer Council. The NCC Report notes, however, that this distinction "is causing real difficulties of construction in Australia".

the insurer may not refuse to pay the claim by reason only of the act.

(6) A reference in this section to an act includes a reference to -

(a) an omission; and

(b) an act or omission that has the effect of altering the state or condition of the subject-matter of the contract or of allowing the state or condition of that subject-matter to alter.

1.8 Provided the act or omission could not be regarded as capable of causing or contributing to a loss, the insurer cannot refuse to pay any part of the loss, but can reduce its liability by an amount representing the extent to which its interests were prejudiced as a result of the act.[9] Where the act or omission is capable of causing or contributing to the loss, the insurer can refuse to pay the claim unless the insured proved it did not actually cause the loss. Where part of the loss was not caused by the insured's act, the protection of the section is still applicable to that part.[10] It is not clear whether the section can be used in relation to claims made policies.[11]

NEW ZEALAND,[12] THE AUSTRALIAN CAPITAL TERRITORY AND NEW SOUTH WALES

1.9 Section 9 of the New Zealand Law Reform Act 1936 allows third parties who have suffered loss due to the fault of a wrongdoer to recover directly from the wrongdoer's insurer. The third party's right is a right to enforce a statutory charge over the insurance money equal to the amount of compensation owed by the insured to the third party and is not restricted to circumstances where the insured

[9] On the question of where the onus lies in proving prejudice, it has been said of the Australian legislation that the burden "rests primarily on the insured but not to establish a negative proposition of the absence of prejudice. It is enough in itself without proof if that is a natural inference from the circumstances and the onus then shifts to the insurer to establish it by evidence rather than by conjecture through argument". See Derrington and Ashton, *The Law of Liability Insurance*, p 363 referring to *Findlay v Madill* (1980) 111 DLR (3d) 180. If the breach made the risk uninsurable, the claim would be reduced to nothing *(Ferrcom Pty Ltd v Commercial Union Assurance Co of Australia Ltd* (1989) 5 ANZ Insurance Cas 60-907).

[10] It has been suggested that the distinction between acts which cause or contribute to loss "is conceptually difficult and may one day give rise to interesting questions of causation". See Minter Ellison, *The Insurance Contracts Act 1984*, (2nd ed 1996) p 70.

[11] In *Seery v John A Carr & Associates Pty Limited* (Supreme Court of New South Wales, unreported 3 November 1995) the claimants sought to rely on section 54 to excuse a failure of the insured or of "some other person" to notify the insurer under a claims made policy of circumstances which might give rise to a claim. Giles CJ refused leave on the basis that the claimants did not have a relevant interest in the insurance contract.

[12] In recent years, there has been significant legislative intervention in insurance law in New Zealand, including the introduction of a no fault, state-run accident compensation scheme. See the Accident Compensation Act 1972 and the Accident Rehabilitation and Compensation Act 1992. The options available to third parties to whom an insured has incurred liability may, therefore, be broader than under English law. Most actions under s 9 of the Law Reform Act involve professional liability claims. See, generally, AA Tarr and JA Kennedy, *Insurance Law in New Zealand*, (2nd ed 1992) and Rishworth [1990] NZ Recent Law Review 109, at pp 116-119.

has been declared bankrupt or wound up.[13] Similar provisions have been adopted in New South Wales (in section 6 of the Law Reform (Miscellaneous Provisions) Act 1944) and the Australian Capital Territory (in section 25 of the Law Reform (Miscellaneous Provisions) Act 1955).

1.10 Section 9 provides that:

> 9.-(1) If any person (hereinafter in this Part of this Act referred to as the insured) has, whether before or after the passing of this Act, entered into a contract of insurance by which he is indemnified against liability to pay any damages or compensation, the amount of his liability shall, on the happening of the event giving rise to the claim for damages or compensation, and notwithstanding that the amount of such liability may not then have been determined, be a charge on all insurance money that are or may become payable in respect of that liability.
>
> (2) If, on the happening of the event giving rise to any claim for damages or compensation as aforesaid, the insured has died insolvent or is bankrupt or, in the case of a corporation, is being wound up, or if any subsequent bankruptcy or winding-up of the insured is deemed to have commence not later than the happening of that event, the provisions of the last preceding subsection shall apply notwithstanding the insolvency, bankruptcy, or winding up of the insured.
>
> (3) Every charge created by this section shall have priority over all other charges affecting the said insurance money, and where the same insurance money is subject to 2 or more charges by virtue of this Part of this Act those charges shall have priority between themselves in the order of the dates of the events out of which the liability arose, or, if such charges arise out of events happening on the same date, they shall rank equally between themselves.
>
> (4) Every such charge as aforesaid shall be enforceable by way of an action against the insurer in the same way and in the same Court as if the action were an action to recover damages or compensation from the insured; and in respect of any such action and of the judgment given therein the parties shall, to the extent of the charge, have the same rights and liabilities, and the Court shall have the same powers, as if the action were against the insured:
>
> Provided that, except where the provisions of subsection (2) of this section apply, no such action shall be commenced in any Court except with the leave of that Court.
>
> (5) Such an action may be brought although judgment has been already recovered against the insured for damages or compensation in respect of the same matter.

[13] However, unless the insured has been declared bankrupt or wound up, the third party's right of action against the insurer is subject to a leave requirement: s 9(4). See paras 1.12-1.13 below.

(6) Any payment made by an insurer under the contract of insurance without actual notice of the existence of any such charge shall to the extent of that payment be a valid discharge to the insurer, notwithstanding anything in this Part of this Act contained.

(7) No insurer shall be liable under this Part of this Act for any sum beyond the limits fixed by the contract of insurance between himself and the insured.

The statutory charge

1.11 The statutory charge attaches on the date of the event giving rise to liability.[14] The attachment of the charge does not give third parties an absolute right to recover that money, however. In *FAI (NZ) General Insurance v Blundell*,[15] Hardie Boys J said that, "Until liability of insured to plaintiff, and of insurer to insured, is established, the charge remains in a sense conditional." It appears that the insurer can probably rely on breaches of the insurance contract after the attachment of the charge to justify a refusal of cover.[16]

The leave requirement

1.12 Under section 9(4), the third party's right of action is subject to a leave requirement unless the insured has been declared bankrupt or wound up.[17] Section 9 does not specify any criteria for the grant or refusal of leave,[18] but it appears that

[14] It has been suggested, therefore, that if the plaintiff in *Bradley v Eagle Star Insurance Co Ltd* [1989] 1 AC 957 had been proceeding under the New Zealand legislation, her action would have succeeded. See Rishworth [1990] NZ Recent Law Review 116, at 119: "If the New Zealand legislation had applied, then one would have been on good ground in arguing that a charge was created on the insurance proceeds in favour of the injured party right back at the time when the event giving rise to the claim occurred. The subsequent liquidation of the wrongdoer before any liability could be fixed upon it would not have made any difference: the action could proceed against the insurer".

[15] [1994] 1 NZLR 11.

[16] See the decisions of the New Zealand court in *State Insurance v Maaka* (1989) 5 ANZ Insurance Cases 60-943 and *Registered Securities Ltd (in liq) v Brockett* (unrep HC ChCh CP 293, 87, 17 October 1991. Cf the approach taken by the New South Wales court in *New South Wales Medical Defence Union Ltd v Crawford* [1993] 31 NSWLR 469. But, see also *New South Wales Medical Defence Union Ltd v Bailey* 1995 18 ACSR 521 and *McMillan v Mannix* (1993) 31 NSWLR 538. See also Rishworth [1990] NZ Recent Law Review 116, at 117.

[17] Referring to the insolvency exception, Richardson J in FAI (NZ) *General Insurance v Blundell* [1994] 1 NZLR 11 said: "No doubt that is for the obvious reason that in the absence of a financially viable insured the claimant should then have direct access to the insurance moneys and not be an ordinary creditor in the bankruptcy". Section 6(4) of the New South Wales legislation and s 26(3) of the Australian Capital Territory legislation provides that leave is not required if the insured is a company which has been wound up.

[18] Cf s 6(4) of the New South Wales Law Reform (Miscellaneous Provisions) Act 1946 and s 25 of the Australian Capital Territory Law Reform (Miscellaneous Provisions) Act 1955 which both provide that "leave shall not be granted in any case where the court is satisfied that the insurer is entitled under the terms of the contract of insurance to disclaim liability, and that any proceedings, including arbitration proceedings, necessary to establish that the insurer is so entitled to disclaim, have been taken".

leave will be refused if the insurer can show that he is entitled to disclaim liability[19] or if the third party could proceed against an alternative, common law defendant.[20]

1.13 The leave requirement has raised questions as to when the limitation period governing the third party's right of action against the insurer begins to run. It appears that that the limitation period governing the third party's action against the insurer may expire at the same time as his claim against the insured.[21]

Multiple claimants against the insurance fund

1.14 Specific provision is made in section 9 for the distribution of insurance money to multiple third party claimants. Section 9(3) of the Law Reform Act 1936 provides:

> ... where the same insurance money is subject to 2 or more charges by virtue of this Part of this Act those charges shall have priority between themselves in the order of the dates of the events out of which the liability arose, or, if such charges arise out of events happening on the same date, they shall rank equally between themselves.[22]

The ability of insurers to rely on policy defences

1.15 Section 11 of the New Zealand Law Reform Act 1977 prevents insurers from relying on breaches to exclude or limit liability "if the insured proves on the balance of probability that the loss in respect of which the insured seeks to be indemnified was not caused or contributed to by the happening of such events or the existence of such circumstances."

SOUTH AFRICA

1.16 Section 156 of the South African Insolvency Act 1936[23] provides third parties with a right of direct action against insurers in cases where the insured is insolvent.[24]

[19] *State Insurance General Manager v Maaka* (1989) 5 ANZ Insurance Cases 60-943. See also *AFG Insurances Ltd v Andjelkovic* (1981) 1 ANZ Insurance Cases 60-443 and *Yorkville Nominees Pty Ltd (in liq) v Lissenden* (1986) 4 ANZ Insurance Cases 60-692.

[20] *Campbell v MLC Fire and General Insurance Co (NZ) Ltd* (1971) NZLR 240 at p 243. See also Kirby P in *Oswald v Bailey* (1987) 4 ANZ Insurance Cases 60-807, at 74, 946.

[21] See *FAI (NZ) General Insurance v Blundell* [1994] 1 NZLR 11. See also *New South Wales Medical Defence Union Ltd v Bailey* (1995) 18 ACSR 521 and *Grimson v Aviation & General Underwriting Pty Ltd* (1991) 25 NSWLR 422 and para 27-510 of the Australian and New Zealand Insurance Reporter. Cf the approach taken by the New South Wales Court of Appeal in *New South Wales Medical Defence Union v Crawford* (1993) 31 NSWLR 469, at 490 where the court held that the time for the third party's action against the insurer did not begin to run until leave had been granted. Kirby P, who had dissented in *Grimson v Aviation & General Underwriting Pty Ltd* (1991) 25 NSWLR 422, said: "I consider that such leave is a necessary part of the cause of action which is thereby conferred by statute upon a person wishing to bring proceedings against an insurer to enforce the charge. Until such leave is given, the cause of action is not complete. The claimant may not prosecute it in the courts. Time does not run against the claimant".

[22] See s 6(3) of the New South Wales legislation and s 25(3) of the Australian Capital Territory legislation. It has been suggested that this provision "has the potential to operate unfairly by denying claimants in leading actions, who pursue those actions diligently and take a significant financial risk, the prospect of a full reward for their efforts". See Drummond and Mann, "Abolish section 6" Insurance Law Journal, Vol 8, no 2, April 1997.

[23] 24 of 1936.

Third parties need not obtain judgment against the insured before acquiring a right of action against insurers under the Act.

Section 156 provides:

> 156.-Whenever any person (hereinafter called the insurer) is obliged to indemnify another person (hereinafter called the insured) in respect of any liability incurred by the insured towards a third party, the latter shall, on the sequestration of the estate of the insured, be entitled to recover from the insurer the amount of the insured's liability towards the third party but not exceeding the maximum amount for which the insurer has bound himself to indemnify the insured.[25]

Establishing the liability of the insured

1.17 When proceeding against the insurer, the third party must establish both the liability of the insured to him and the liability of the insurer under the insurance contract. The third party is not required to join the insured to his action against the insurer. We understand[26] that, although the third party could join the insured to his action under section 156 should he wish to do so, this does not happen in practice.

The rights of the insurer against the third party

1.18 In defending an action under section 156, the insurer may rely on any defence which he would have had against the insured.[27] In *Przybylak v SANTAM Insurance Ltd*,[28] the court referred to the English legislation and to decisions reached by the English court in *Post Office v Norwich Union Fire Insurance Society Ltd* and *Farrell v Federated Employers Insurance Association Ltd* with approval:

> In England similar provisions are contained in the Third Parties (Rights Against Insurers) Act 1930. In interpreting these provisions it has been held that it is open to the insurer to rely as against a third

[24] It is not clear whether s 156 confers a new statutory right on third parties or transfers the insured's existing rights. In *Gypsum Industries Ltd v Standard General Insurance Co Ltd* 1991 1 SA 718, at 722, the court distinguished the judgment of Lord Denning in *Post Office v Norwich Union Fire Insurance Society Ltd*, holding that: "The clear wording of s 156 of the Insolvency Act creates and confers upon the third party a right which did not exist prior to insolvency. Unlike the English statute it does not transfer to, nor vest the existing rights of an insolvent in, the third party. The concepts of the liability of the insurer and the rights of the insured referred to by Denning MR are alien to and do not exist in s 156. Unlike the English provisions, s 156 eliminates the insolvent estate entirely upon insolvency supervening, and all the concomitant pitfalls and dangers of litigation against an insolvent estate". Cf *Hockley's Insolvency Law* (6th ed 1996), at p 51: "the third party, being vested with the insolvent's rights, may proceed directly against the insurer and not obtain judgment against the insolvent estate or enter into an agreement with the trustee".

[25] In *Woodley v Guardian Assurance Co of South Africa Ltd* 1976 (1) South Africa 758 (W), it was held that section 156 applies to companies as well as to individuals.

[26] From Messrs Shepstone and Wylie, South African attorneys.

[27] See also *Supermarket Haasenback (Pty) Ltd v Santarn Insurance Ltd* 1989(2) South Africa 790(W).

[28] 1992 1 SA 588 (C)

party on any defence which would have been available against the insured.

NIGERIA

1.19 Section 68 of the Insurance Decree 1997[29] allows third parties to join insurers into proceedings against the insured in certain circumstances. It provides:

> 68.-(1) Where a third party is entitled to claim against an insured in respect of a risk insured against, he shall have a right to join the insurer of that risk in an action against the insured in respect of the claim.
>
> (2) A third party shall, before bringing an application to join the insurer, give to the insurer at least 30 days notice of the pending action and of his intention to bring the application.[30]

The nature of the third party's right

1.20 There has been some debate as to whether section 68 confers a substantive or merely a procedural right on third parties. It appears that third parties may only have a procedural right under section 68 and that they may only be able to join insurers as defendants to their proceedings against the insured where they have an existing substantive right against the insurer under sections 73 and 67 of the Insurance Decree 1997. These sections provide third parties, respectively, with rights against motor insurers in cases involving personal injury and death[31] and with rights against fire insurers.

The ability of the insurer to rely on policy defences

1.21 Section 68 does not affect the ability of the insurer to rely on policy defences,[32] although it has been suggested that, in practice, joinder may have this effect.[33]

[29] Which re-enacts s 58 of the Insurance Decree of 1991.

[30] It appears that the court may not have a discretion to refuse the third party's application to join the insurer, however. See Dr Omogbai I Omo-Eboh, "Rights of third parties against insurers in Nigeria" [1996] ILIJ 276, at 285.

[31] In *Unity Life and Fire Insurance Company Ltd v Ladega & Others* (1996) 1 NWLR (Part 427) 426, the Nigerian Court of Appeal held that the provision confers on third parties a procedural right to join insurers only when they have existing substantive rights. The third party may also be required to give 7 days notice to the insurer before or after the commencement of proceedings under s 73 of the 1991 Insurance Decree. See Afalabi Elebiju Olaniwun Ajayi & Co, "Sections 53 and 54 Insurance Act 1990" [1996] 11 Int ILR G-202.

[32] In *Unity Life and Fire Insurance Company Ltd v Ladega & Others* (1996) 1 NWLR (Part 427) 426, the Court of Appeal allowed the appeal of an insurer against an order that it be joined to proceedings started by a third party on the ground that the insurer had not been served with the requisite seven day notice. See n 31 above.

[33] See Dr Omogbai I Omo-Eboh, "Rights of third parties against insurers in Nigeria" [1996] ILIJ 276, at 285: "For example, it may no longer be open to an insurer to rely on the insured's breach of condition to refer all disputes to arbitration since the insured may be willing to do this even though the insurer has been brought to court by a third party. Furthermore, the notice of proceedings required to be given by the third party under section 58 of the Insurance Decree (now s 68 of the 1997 Decree) may always satisfy the condition requiring notification of loss or proceedings contained in most liability policies

THE UNITED STATES OF AMERICA.

1.22 The principle of privity of contract is generally observed in US law, which also maintains the distinction between liability and indemnity insurance, a distinction which has been blurred in English law.[34] However, the effect of some of the specific regimes of third party rights which have been introduced in some states may be to remove this distinction.[35] The rights of third parties against insurers vary greatly from state to state. In some states, they have a right of direct action against the insurer without having first to establish the liability of the insured. In others, they must establish the liability of the insured first. Their right of action may or may not be dependant on the insolvency of the insured. In many cases, such statutes were introduced because of concern over the inclusion of "no action" clauses in insurance contracts. These provided that the insurer would only reimburse the insured after the insured had paid the injured party. If the insured was insolvent, the injured party would not be compensated.[36] Examples of different regimes of third party rights are discussed briefly below.

Louisiana[37]

1.23 The Louisiana Direct Action Statutes state that, "all liability policies are executed for the benefit of all injured persons to whom the insured is liable." It allows third

unless compliance is made personal to the insured or is required 'immediately' or 'as soon as possible'".

[34] See para 1.11 above. Under US law, a cause of action accrues under a liability policy when the liability attaches; the insured need not have suffered actual financial loss. Under an indemnity policy the insured must have suffered an actual money loss before the insurer is liable. See *American Jurisprudence*, Vol 29A section 1485 which states that, as there is no privity of contract and no right of action, "it follows therefore, that the injured person in such cases cannot join the insured and liability insurer as parties defendant". See also *CBF Trading Co, Inc v Hanover Ins Co,* 603 F Supp 685 and *Hartford Ins Co v Henderson & Son,* 1988, 371 Se 2d 401, 258 Ga 493.

[35] See Appleman, *Insurance Law and Practice*: Vol 8, Chapter 200 "The general rule is that because there is no privity of contract, a party may not bring a direct action against a liability insurer of the party who allegedly caused damage unless there is unsatisfied judgment against insured or it is specifically permitted either by statute or a provision in the policy". See also *Continental Oil Co v Bonanza Corp* 677 F. 2d 455 (5th Cir 1982), at 459-460.

[36] See Viqar M Shariff, *Grubbs v Gulf International Marine Co: the Louisiana Supreme Court declares the direct action statute applicable to marine P & I Insurance*, 68 Tul L Rev 1653, 1655 (1994). We discuss at para 5.58 above the use of pay to be paid clauses in this country.

[37] See Alston Johnson, "The Louisiana Direct Action Statute 1983" Louisiana Law Review, 1455; McKenzie and Johnson, "Louisiana Civil Law Treatise" Insurance Law and Practice, 1986, Vol 15, 19. The Wisconsin Direct Action Statute 260.11 also provides third parties with a right of direct action against insurers. It appears that third parties can proceed against the insurer alone (see *Prisuda v General Cas Co* 1957, 83 NW 2d 739) but that fewer restrictions are placed on the ability of insurers to rely on policy defences than is the case in Louisiana (see *Hunt v Dollar* 1937, 271 NW 405, at 408. In Rhode Island, third parties may proceed directly against liability insurers if they cannot effect service on the insured. See
RI Gen Laws Ann s 27-7-2(1956).

parties to proceed against both the insurer and the insured and against the insurer alone if the insured is insolvent or dead.[38]

1.24 The statute provides that the third party has a right of action provided that it is "within the terms and limits of the policy" and that any action "shall be subject to all of the lawful conditions of the policy contract and the defences which could be urged by the insurer to a direct action brought by the insured".[39] However, the court has prevented insurers from relying on some policy defences which they could have used against the insured[40] or which the insured could have raised against the third party.[41] It has been suggested that, in fact, "the insurer can raise those defences which it could raise in an action against it by its insured which do not defeat the public policy underlying the right of direct action in the victim."[42]

Florida

1.25 In Florida, the right of a third party to proceed against both liability insurer and insured is a result of case law rather than legislation. In *Shingleton v Bussey*,[43] the Florida Supreme Court held that "the time has arrived when the legal reasons advanced in favour of joinder and direct action against an insurer outweigh and preponderate over the traditional notions asserted to justify precluding an injured third party from enjoying such rights."[44]

1.26 The third party cannot sue the insurer alone, but can join the insurer in an action against the insured.[45] The court can order separate trials, but will only do so if there is dispute as to the existence of insurance cover.[46]

[38] Or if the insured cannot be served or claim relates to an offence between children and their parents. See LA Rev Stat Ann para 22:655(B)(1)(a)-(f)(West Supp 1993).

[39] 1930 La Acts, No 55

[40] See *Edwards v Fidelity & Casualty Co* 217 La 189, where the insurer, who had not received notice of the claim until eleven months after the incident, despite the fact that the contract required "immediate written notice", claimed that notice was not "within the terms and limits of the policy". The court held that if the insurer's position was accepted, the right given to the injured party would depend upon the conduct of the insured, over whom the injured party had no control. The court said: "As between parties to a contract, the contract itself is the law of the case. Here, however, the law of the case is not found solely within the four corners of the policy of insurance, but is contained primarily in the statute to which we have referred". See also *West v Monroe Bakery Inc* 217 La 189, 46 So 2d 122 (1950) and *Chennault v Dupree*, 398 So 2d 169. Courts have allowed insurers to rely on some defences, such as prescription and contributory negligence, particularly where these relate to the conduct of the third party. See *Soirez v Great Am Ins Co* 168 So 2d 418 (1964).

[41] The courts have held that certain immunities (such as those between spouses) were "personal" to the insured and could not be used as defences by the insurer. See *Harvey v New Amsterdam Casualty Co*, 6 So 2d 774, *Deshotel v Travelers Ins Co*, 257 La 567, (1971); and *Von Dameck v St Paul Fire & Marine Ins Co*, 361 So 2d 283 (1978).

[42] McKenzie and Johnson, *Insurance Law and Practice*, Vol 15, p 56, n 21.

[43] 223 So 2d 713 (Fla 1969).

[44] The court relied on rule 1.210(a), 30 Florida Rules of Civil Procedure, which provided that "any person may be made a defendant who has or claims an interest adverse to the plaintiff".

[45] *Russell v Orange County* 237 So 2d 192 (Florida Court of Appeal, 1970).

New York[47]

1.27 Article 3420 of the New York Insurance Law 1984 allows third parties to proceed against liability and indemnity insurers once the insured is insolvent[48] and once judgment has been obtained against him. Third parties assume the rights of the insured against the insurer.[49]

FRANCE

1.28 French law is largely codified. Specific rules relating to insurance are contained in the Code des Assurances. The doctrine of privity of contract is part of French law[50] but has been eroded[51] and the courts have developed the concept of *action directe*[52] to allow a third party to proceed against the insurer of the person who caused him harm. Article L124-3 of the Code des Assurances provides:

> The insurer cannot pay to a party other than the wronged third party all or any part of the sums due by him until the third party has been indemnified for losses arising from the wrongful act causing the liability of the insured.

[46] Under rule 1.270(b). See *Stecher v Pomeroy* 244 So 2d 488 (Florida Court of Appeal, 1971).

[47] See also s 4203(3) of the Vermont Statutes which requires all insurance policies to provide that third parties can recover from the insurer if the insured is insolvent and has had judgment awarded against him.

[48] The insolvency requirement is broader than under the 1930 Act: it is not restricted to judicially declared insolvency, covering an insured who is in financial difficulties. See *Miller v Union Indemnity Co* 1924, 204 NYS 730, 209 App Div 455.

[49] *Coleman v New Amsterdam Casualty Co* 1928, 247 NY 271, 160 NE 367.

[50] Article 1165 of the Code Civil.

[51] See article 1121 of the Code Civil.

[52] Which stems from article 1641 of the Code Civil.

Establishing the liability of the insured and of the insurer

1.29 Third parties may proceed against the insured to establish his liability and then bring a separate *action directe* against the insurer or may proceed against both insurer and insured in the framework of the *action directe* proceedings.[53] Unless they have established the liability of the insured in separate proceedings,[54] it appears that third parties must usually join the insured in the *action directe* and establish the liability of both the insured and of the insurer.[55]

The rights of the insurer against the third party

1.30 Article L 112-6 of the Code des Assurances provides that the insurer can rely, as against third parties, on conditions which the insurer could have relied on against the insured.[56] The insurer can only rely, however, on breaches of conditions in the insurance contract which occurred prior to the incident giving rise to the insured's liability to the third party.[57] Article R 124-1 of the Code des Assurances provides that:

> Insurance policies relating to civil liability must provide that no breach by the insured of his obligations following the date of the event giving rise to liability shall be used as a defence against injured parties ...[58]

BELGIUM

1.31 Belgian law provides third parties with a right of direct action against insurers, regardless of the solvency of the insured. Article 86 of the law of 25 June, 1992 on terrestrial insurance provides:

[53] Michel Tournois, "Direct actions by victims against insurers of wrongdoers in France" [1996] IJIL 194, at 202.

[54] Or where the insurer has recognised that the insured is liable. In cases where the liability of the insured is not seriously disputed, the third party may choose instead to proceed by way of reference action (*refere*) against the insurer without joining the insured. The third party may then obtain a form of interim order, (an *ordonnance de refere*) which might persuade the insurer to pay the indemnity to the third party. The third party will not then be obliged to proceed by way of *action directe*.

[55] Article R 114-1. See Michel Tournois, "Direct actions by victims against insurers of wrongdoers in France" [1996] IJIL 194, at pp 196 and 210 and Cour de Cassation, Civ., 17 July 1911, D.P. 1912.1.81, S. 1915.1.145 and Cour de Cassation, Civ, 11 July 1932, RGAT 1930.983. It has also been pointed out that another advantage of joint proceedings is that if the third party is only partly indemnified for his losses (because, for example, of restrictions in the insurance policy), he may be able to obtain additional sums from the insured. See Yvonne Lambert-Faivre, *Droit des assurances* (8th ed) p 455. In some cases, the principle of French law known as *contradictoire* may, in any event, necessitate the joinder of both insured and insurer. This principle provides that, in cases where the harm suffered by the third party is caused not by the insured himself, but by persons for whom the insured is responsible or by things over which he exercises control, the insured must be joined in to any *action directe* against the insurer so that he can draw attention to anything in his interest.

[56] Including defences of misrepresentation and non-disclosure: articles L 113-8 and L 121-3.

[57] See Cour de Cassation, 15 June 1931.

[58] In such cases, the insurer can seek an indemnity from the insured. See Yvonne Lambert-Faivre, *Droit des assurances* (8th ed) p 451.

> The insurance creates a personal right against the insurer for the benefit of the victim.
>
> The indemnity due by the insurer belongs to the victim alone, with the exclusion of the other creditors of the insured.

Establishing the liability of the insurer and of the insured

1.32 The third party can proceed directly against the insurer. He need not pursue the insured as well but the insured may intervene in the proceedings.[59] The insurer can also apply for the insured to become a party to the proceedings.[60] We understand that, in most cases, the third party, the insured and the insurer are parties to the action.

The ability of the insurer to rely on policy defences

1.33 The ability of the insurer to rely on policy defences varies according to whether or not the insurance is compulsory or non-compulsory. In the case of compulsory insurance, the insurer cannot rely on any policy defences, whether they arose prior to or after the incident giving rise to the liability of the insured.[61] Where insurance is non-compulsory, the insurer can rely on policy defences arising prior to the incident giving rise to the liability of the insured.[62]

The right of the insurer to an indemnity from the insured

1.34 The insurer can recover from the insured sums which he has paid to a third party under article 86 and which he could have refused to pay to the insured under the insurance contract.[63]

CANADA

1.35 Insurance law in Canada is governed by provincial legislation, but there is considerable uniformity across the provinces. A third party must have obtained a judgment against the insured and the insured must have failed to satisfy that judgment before he can proceed against the insurer.

Right to enforce judgment against the insurer

1.36 Section 132 of the Ontario Insurance Act 1924[64] provides:

[59] By way of a *requete in intervention volontaire*.

[60] By way of a *citation en intervention et garantie*.

[61] Unless the insurance contract was rescinded prior to the incident giving rise to the liability of the insured: Art 87 of the law of 25 June 1992.

[62] Art 87(2) of the law of 25 June 1992. Provision is made in art 87(2) for the treatment of compulsory insurance policies to be extended to other categories of insurance.

[63] Art 88 of the law of 25 June, based on art 16 (2) of the law of 21 November, 1989 on the compulsory insurance of motor vehicles.

[64] See also s 219 of the Alberta Insurance Act, s 26 of the British Colombia Insurance Act, s 104 of the New Brunswick Insurance Act, s 13 of the Newfoundland Insurance Act, s 28 of the Nova Scotia Insurance Act, s 122 of the Saskatchewan Insurance Act, s 56 of the Northwest Territories Insurance Act and s 55 of the Yukon Territory Insurance Act.

> 132.-(1) Where a person incurs a liability for injury or damage to the person or property of another, and is insured against such liability, and fails to satisfy a judgment awarding damages against him in respect of his liability, and an execution against him in respect thereof is returned unsatisfied, the person entitled to the damages may recover by action against the insurer the amount of the judgment up to the face value of the policy, but subject to the same equities as the insurer would have if the judgment had been satisfied.
>
> (2) This section does not apply to motor vehicle liability policies.[65]

1.37 It appears that, in the action against the insurer, the third party need not usually prove the case against the insured again,[66] but must prove that he obtained judgment and that there was insurance cover.[67] The ability of the third party to proceed against the insurer may be limited to certain types of claim in some provinces.[68]

Multiple claimants

1.38 It appears that an insurer may pay the full amount of the policy to a third party claimant, even if it knows of other claims pending[69] and even though the court has power to apportion the sum amongst claimants.[70]

[65] Legislation provides third parties with rights of direct action against insurers in such cases. See s 226 of the Ontario Insurance Act, s 320 of the Alberta Insurance Act, s 252 of the British Colombia Insurance Act, s 258 of the Manitoba Insurance Act, s 250 of the New Brunswick Insurance Act, s 26 of the Newfoundland Insurance Act, s 133 of the Nova Scotia Insurance Act, s 210 of the Saskatchewan Insurance Act, s 155 of the Northwest Territories Insurance Act and s 153 of the Yukon Territory Insurance Act.

[66] Although the insurer may be able to reopen the merits of the original claim if it produces appropriate evidence. *Carwold (Carwald) Concrete & Gravel Co v General Ins Co of Canada* (1985) 42 Alta LR 224 (CA).

[67] *Sedam v Simcoe & Erie Ins Co* (1983) 45 BCLR 120 (SC). In *Satter v Pafco Insurance Co Ltd* [1993] ILR 2524, the insurer relied on the insured's failure to co-operate with the insurer in his defence as a defence to the third party's claim.

[68] In Ontario, a third party may only be able to claim for injury to the person or damage to property, not for pure economic loss: *Perry v General Security Insurance Co of Canada* (1984) 7 CCLI 231 (Ont CA 1985). Cf *Kallos v Sask Govt Insurance* (1983) 3 CCLC 65, where the Saskatchewan court allowed a third party to claim against a solicitors' liability insurer.

[69] *Bartkow v Merit Insurance Company* 29 DLR (2nd) 322.

[70] See s 110(3) of the Ontario Insurance Act.

APPENDIX G
LIST OF INDIVIDUALS AND ORGANISATIONS WHO HAVE ASSISTED WITH THE PROJECT

Association of British Insurers

De Bandt, Van Hecke & Lagae

Barlow Lyde & Gilbert

Professor John Birds, University of Sheffield

Adrian Briggs

Mr Registrar Buckley

City of London Law Society's Insurance Committee

Dr Malcolm Clarke, St John's College, Cambridge

Department of Trade and Industry

Department of the Environment, Transport and the Regions

Professor Bill Dyfwa, University of Stockholm

Ebsworth & Ebsworth

Richard Eveleigh, Berrymans Lace Mawer

Pete Farthing, Clyde & Co

L J Foster

Mr Justice B H Giles

Peter Goldsmith QC

Ian Govey, Corporations Law Simplification Program, Australia

Alison Green, British Insurance Law Association

Ray Hodgin, University of Birmingham

The Insolvency Service

Insurance Ombudsman Bureau

International Group of P&I Clubs

Ethne Harkness, Queens University of Belfast

Law Society Consumer and Commercial Law Committee, Insurance Law Sub-Committee

Le Boeuf Lamb Greene & Macrae

Andrew Legg, Linklaters and Paines

Edward Lewis

Lloyd's of London

Lord Chancellor's Department

Mr Justice Mance

Mathew Marshall, Institute of London Underwriters

Minter Ellison

Dr Micheal Muller-Stuler

National Consumer Council

Nigerian Law Reform Commission

Pat Northey, Russell Mc Veagh

Dr Omogbai I Omo-Eboh

Dr Roy Palmer, Medical Protection Society

Policyholders Protection Board

Peter Rees, Norton Rose

Professor Len Sealy, Gonville and Caius College, Cambridge

Robert Seward, Tindall Riley & Co

Shepstone & Wylie

Christopher Symons QC

Christian Wells, Lovell White Durant

David Wolfson