LEGAL DEVELOPMENTS RELATING TO LOSS ALLOCATION

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KEYSTONE LAW

SITUATIONS WHERE THE DATE OF LOSS IS BEYOND DETERMINATION

- Scrutinised in detail in the context of mesothelioma
- Mesothelioma: an “indivisible” disease (severity does not increase with increased exposure)
- Contrast Silicosis: a “divisible” disease (severity proportionate to exposure)
- Need to prove causation in line with established principles a major stumbling block, since it is impossible to demonstrate which period of exposure actually caused mesothelioma

LEGAL DEVELOPMENTS SINCE 2000

- To address this, judicial creativity has resulted in the adoption of a "material increase of risk" test for the purpose of establishing employer liability towards mesothelioma victims
- **Fairchild v Glenhaven Funeral Services Ltd** [2002] UKHL 22; House of Lords
- Was there a "material increase of risk" during the period when a mesothelioma victim was employed by employer A and in that period exposed to asbestos fibres ?
- 'Fairchild" principle extended to lung cancer resulting from exposure to asbestos fibres: **Heneghan v Manchester Dry Docks Ltd**; [2016] EWCA Civ 86; Court of Appeal

LEGAL DEVELOPMENTS SINCE 2000

continued

- Is each responsible employer liable only for a proportionate share of the loss (determined by reference to length of employment as a proportion of overall period of employment)?
- **Compensation Act 2006**: each employer jointly and severally liable for 100% of the loss (irrespective of length of employment)

BASIS OF INSURER LIABILITY

- **Employers' liability insurance**: on what basis does it respond?
- Difficulty arising from insurance policy coverage being defined by reference to terms such as "*injury sustained", "disease contracted"* and *"bodily injury or disease suffered"*
- In the context of mesothelioma, how is compliance with such terms to be demonstrated?
- **BAI (Run Off) Ltd v Durham**; [2012] UKSC 14; Supreme Court; **the "Trigger Litigation"** – these terms are to be understood and applied by reference to a "weak" causation test
- Insurers liable by reference to asbestos exposure, bodily injury being regarded as having occurred at the time of exposure
- Not the manifestation of lung damage (invariably too late to trigger insurance cover in respect of mesothelioma victims)

EXTENT OF INSURER LIABILITY

- See **Zurich Insurance plc UK Branch v International Energy Group**; [2015] UKSC 33; Supreme Court
- Insurer provided employers liability insurance cover for only part of employee's employment during which exposure to asbestos fibres occurred
- Employer was either uninsured for the rest of that period, or was insured by an insurer which had become insolvent
- Primary issues: did the insurance cover respond

  a) to the full extent of the employer's liability to the employee, or only

  b) to a proportionate part of that liability, determined by reference to the periods of cover for which premiums were assessed and paid?

ZURICH v IEG

Relevant facts

- Victim exposed to asbestos for 27 years (1961 – 1988). Later developed mesothelioma.
- Intensity of exposure assumed to be the same each year.
- Zurich's predecessor on risk for 6 years, another insurer for 2 years. No insurance at all for remaining 19 years.
- Relevant employer sought to recover entire liability from Zurich.

ZURICH v IEG *continued*

Supreme Court

- (4:3 majority) held the Fairchild principle should be extended to employers' liability insurance.
- The logic of Fairchild was that every exposure gave rise to liability. It therefore followed that Zurich faced 100% liability in every year it was on risk. No 'time on risk' apportionment of liability between insurers.

ZURICH v IEG – SUPREME COURT

- According to Lord Mance:
  - "…*having, for wholly understandable reasons, gone down the Fairchild route, the common law must, in my view, face up to the consequences, if necessary, by further innovation…*
  - *Once one accepts that causation equates with exposure, in tort and tort liability insurance law, there is no going back on this conclusion simply because there was exposure by the insured of the victim both within and outside the relevant insurance period."*

ZURICH v IEG – SUPREME COURT

continued

- However, note the reasoning of the minority, expressed by Lord Sumption:
  - *"I cannot agree with the reasons given by the majority, which seem to me to be contrary to a number of basic principles of the law of contract and to be productive of uncertainty and injustice. Suppose that an insolvent employer had tortiously exposed his employee to asbestos for, say, 30 years before going out of business. The employer had failed to insure his liabilities at all for years 1 to 20. Insurer A insured his liability on an occurrence basis in year 21. Insurer B insured his liabilities under successive annual policies for years 22 to 30, but insurer B is insolvent….*

ZURICH v IEG – SUPREME COURT

continued

- *The majority would hold that, in a case governed by the 2006 Act, insurer A is liable for the entire loss incurred over the 30 years of exposure, although he was only on risk for one….The effect, and as I understand it, the object, of this is to make insurer A, who is solvent, answerable (i) in respect of periods when insurer A was not on risk but insurer B was and (ii) for the failure of the employer to insure at all in the first 20 years……*

- *In my opinion, the correct result in this situation is that insurer A is liable for a proportionate part of the loss in respect of the one year out of 30 when he was on risk. The employee is entitled to recover insurer B's proportion under the statutory compensation scheme established under section 213 of the Financial Services and Markets Act 2000 for cases of insurer insolvency.*

ZURICH v IEG – SUPREME COURT

continued

- *In respect of the 20 years when there was no insurance, he is entitled subject to the statutory conditions of eligibility to recover under the statutory compensation scheme established under the Mesothelioma Act 2014 for cases where there is no insurance. The effect of the majority's view is simply to transfer risk from the statutory compensation schemes which were created to assume that risk, to an arbitrarily selected solvent insurer who has not agreed to do so.*

ZURICH v IEG – SUPREME COURT

continued

- *The liabilities of an insurer are wholly contractual. The answer to the questions now before the court necessarily depends on the construction of the contract and on nothing else. Under an annual policy of insurance written on an occurrence basis, the insurer's liability is limited to occurrences caused during the contractual term….*
- *The suggestion that an insurer who was on risk for only part of the period of exposure, however brief, can be liable as if he had been on risk for the entire period, is contrary to the express terms of the contract and to the nature of annual insurance. The suggestion that some doctrine of law can be devised which imposes on an insurer in one year the risk that insurers of other years may become insolvent or that in other years the employer may fail to insure at all, is both unprincipled and unjust.*

ZURICH v IEG – SUPREME COURT

continued

- *…the incidents of liability in tort are the creation of rules of common law, whereas the extent of a contractual liability depends on the intentions of the parties. The scope for judicial inventiveness is therefore necessarily more limited in the latter context than in the former."*

IMPLICATIONS FOR REINSURANCE

- Does the approach adopted in **Zurich v IEG** carry over into reinsurance contracts, enabling an insurer to obtain reinsurance recovery for the entirety of its loss, even if derived from exposure beyond the period of cover?
- Or does the incoming tide of *Fairchild* jurisprudence fall short of reinsurance?
- See **Equitas Insurance Ltd v Municipal Mutual Insurance Ltd**; [2019] EWCA Civ 718; Court of Appeal; April 2019.
- Concerned with employers' liability insurance policies issued by Municipal Mutual Insurance (MMI) to local authorities and other public bodies between 1950 and 1981.

IMPLICATIONS FOR REINSURANCE

continued

- The policies provided cover in respect of liability for an employee sustaining bodily injury or disease arising out of, or in the course of, employment.
- MMI's reinsurance was with Lloyd's Syndicates, whose liabilities were later transferred to Equitas.

EQUITAS v MMI

- The reinsurance comprised a programme of vertical layers of cover, each layer providing a monetary band of cover "*on account of each and every accident but unlimited as to the number of accidents*".

- In handling claims by its local authority insureds, provided MMI had granted cover for some of the relevant exposure period, each MMI policy providing cover was 100% liable for the claim.

- MMI made no attempt to apportion claims to individual policies or periods. There was no reason to apportion, since each policy was liable in full.

- MMI presented reinsurance claims either against the reinsurance in force in the first year in which it was exposed to an inwards claim, or, if that would not provide a full recovery, against the reinsurance in force in the year which would give MMI the fullest recovery.

EQUITAS v MMI *continued*

- Equitas disputed MMI's entitlement to choose to present an entire claim to any one year of reinsurance ("spiking").
- Instead, Equitas argued that MMI was only entitled to claim under each reinsurance contract a pro rata proportion of the loss attributable to the underlying claim, calculated on a 'time on risk' basis.

EQUITAS v MMI – COURT OF APPEAL (APRIL 2019)

On appeal from the ruling of Flaux LJ (judge-arbitrator) in favour of MMI, the Court of Appeal held that:

- "…*to make the [reinsurance] contracts work as consistently as is possible with the parties' presumed intention and reasonable expectations, it is necessary to imply a term which restricts the exercise of the reinsured's power to select how it will present its claim as between policy years.*" (Leggatt LJ).

- "*I think it clear that the way in which reasonable parties would have intended the reinsurance contracts at issue in this case to work if they had contemplated the legal regime which now applies within the Fairchild enclave, is by requiring the insurer/reinsured to present its claims in a way which spreads its ultimate net loss across the period covered by the EL policies under which it is liable to indemnify-*

EQUITAS v MMI – COURT OF APPEAL (APRIL 2019) *continued*

- *-its insured. Such an apportionment matches the claim as closely as possible to the underlying risk……..”* (Leggatt LJ).

- “*…a principled solution has been proposed by Equitas which does not allow the reinsured to select the period and policy to which the whole of its loss attaches – contrary to the basis on which the reinsurance was placed. The proffered solution also does not allow the reinsured to obtain under a contract to provide cover for one year an indemnity for the whole of a loss which arises from risks extending over a number of years – a result which, as Lord Sumption put it, ”entirely severs the functional connection between premium and risk”…..”* (Leggatt LJ).

JAMES CRABTREE

James Crabtree is a member of the Insurance and Reinsurance practice at Keystone Law, London.

He is a co-author of *International Sale of Goods* (Croner Publications) and of the *New Appleman on Insurance Law Library Edition* (LexisNexis)

He has practised as a solicitor since 1988 and has advised numerous major companies underwriting risk, or managing exposures in the worldwide insurance and reinsurance markets (including within the run-off sector) on insurance and reinsurance claims, contractual coverage questions and disputes, and on the contractual terms and conditions of many varieties of insurance and reinsurance cover. He has handled claims of many different kinds arising in many different contexts and parts of the world: e.g. marine, offshore energy, construction and engineering, mining, political risk, bank lending risk, long tail liabilities (such as asbestos and environmental pollution), professional liability.

JAMES CRABTREE *continued*

He has also advised banks and other corporate entities on insurance matters and early in his career was seconded to a major US bank.

He has handled numerous disputes resolved by arbitration or by court proceedings and has been involved in proceedings before the Commercial Court, the Court of Appeal and the House of Lords (now the Supreme Court), as well as engaged in disputes entailing proceedings in other jurisdictions.

He has lectured extensively in London and in many different parts of the world, including major cities in Europe, the USA and the Far East.

JAMES CRABTREE *continued*

According to the legal directories (Chambers and Legal 500), James Crabtree is

> *"outstanding"* and *"highly experienced and solution-oriented"* ,*"technically very strong with good attention to detail", "strategic and business orientated"* , *"receives high praise from clients, who consider him an extremely savvy and well-versed lawyer, familiar with the intricacies of the field"* and a *"very deliberating lawyer, who is calm under pressure"* and *"provides legal solutions which are both effective and commercial."*

He is listed in Who's Who Legal, Insurance & Reinsurance, 2018 and in Expert Guides, 2018.

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