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## Terms of reference

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### REVIEW OF THE MARINE INSURANCE ACT 1909

I, DARYL WILLIAMS, Attorney-General of Australia, acting pursuant to section 20 of the *Australian Law Reform Commission Act 1996* refer the following matter to the Australian Law Reform Commission:

The *Marine Insurance Act 1909* (the Act).

1. In carrying out its review of the Act, the Commission should comply with the requirements set out in sections 21 and 24 of the *Australian Law Reform Commission Act 1996* and the Commonwealth requirements for regulation assessment, including those set out in the Competition Principles Agreement. The Commission must report on the appropriate arrangements for regulation, if any, taking into account the following:
  - (a) any parts of the legislation which restrict competition should be retained only if the benefits to the community as a whole outweigh the costs; and if the objectives of the legislation can be achieved only by restricting competition;
  - (b)
  - (c) the desirability of having a regime consistent with international practice in the marine insurance industry, noting in particular that the Act is based very closely on the Marine Insurance Act 1906 (UK) and whether any change to the Act might result in a competitive disadvantage for the Australian insurance industry;
  - (d)
  - (e) the effects on the environment, welfare and equity, occupational health and safety, economic and regional development, consumer interests, the competitiveness of business, including small business and efficient resource allocation;
  - (f)
  - (g) compliance costs and the paper work burden on small business should be reduced where feasible.
2. The Commission in its report should also:
  - (a) identify the nature and magnitude of the social, environmental or economic problems that the Act seeks to address;

- (b) clarify the objectives of the Act;
  - (c)
  - (d) assess alternatives, including non-legislative alternatives to the Act;
  - (e)
  - (f) analyse, and as far as reasonably practicable quantify the benefits, costs and overall effects of the Act and any proposed alternatives to it.
3. The Commission must invite submissions from the public and may hold public hearings.
  4. The Commission is to draft any appropriate legislation and explanatory memorandum to give effect to the recommendations in its report under this reference.
  5. The Commission is to report not later than 31 December 2000.\*

Dated: 21 January 2000

[signed]  
Daryl Williams  
Attorney-General

\* The Attorney-General extended the deadline for reporting to 30 April 2001.

# Participants

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## **The Commission**

The Division of the Commission constituted under the *Australian Law Reform Commission Act 1996* (Cth) for the purposes of this reference comprises the following:

### **President**

Professor David Weisbrot

### **Deputy President**

Dr Kathryn Cronin

### **Members**

Ian Davis (full-time Commissioner from 13 June 2000)

Brian Opeskin (full-time Commissioner from 31 July 2000)

Justice John von Doussa (part-time Commissioner)

Justice Ian Coleman (part-time Commissioner)

Justice Mark Weinberg (part-time Commissioner)

### **Officers**

#### ***Legal Officers***

Bruce Alston

Alison Creighton (to July 2000)

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The Hon Justice Ken Carruthers QC  
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Mr Ron Salter, Partner, Phillips Fox  
The Hon Ian Sheppard  
Mr Alexander Street SC, Barrister  
The Hon Justice Brian Tamberlin, Federal Court of Australia  
Dr Michael White QC, Executive Director, Centre for Maritime Law, University of Queensland  
Mr Mark Zanker, Attorney-General's Department

## Abbreviations

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ALRC 16	Australian Law Reform Commission Report 16 <i>Insurance Agents and Brokers</i> AGPS Canberra 1980
ARLC 20	Australian Law Reform Commission Report 20 <i>Insurance Contracts</i> AGPS Canberra 1982
ALRC 33	Australian Law Reform Commission Report 33 <i>Civil Admiralty Jurisdiction</i> AGPS Canberra 1986
ALRC 48	Australian Law Reform Commission Report 48 <i>Criminal Admiralty Jurisdiction and Prize</i> ALRC Sydney 1990
ARLC DP 7	Australian Law Reform Commission Discussion Paper 7 <i>Insurance Contracts</i> Sydney 1979
ALRC DP 63	Australian Law Reform Commission Discussion Paper 63 <i>Review of the Marine Insurance Act 1909</i> ALRC Sydney 2000
AMSA	Australian Maritime Safety Authority
APRA	Australian Prudential Regulatory Authority
BILA	British Insurance Law Association
C&F	Cost and Freight
CEFOR	Norwegian Central Union of Underwriters
CFR	Cost and freight
CIF	Cost, insurance and freight
CLERP	Corporate Law Economic Reform Program
CMI	Comité Maritime International
COGSA	<i>Carriage of Goods by Sea Act 1991</i> (Cth)
ETA	<i>Electronic Transactions Act 1999</i> (Cth)
FCA	Free carrier
FOB	Free on board
FSRB	Financial Services Reform Bill
IABA	<i>Insurance (Agents and Brokers) Act 1984</i> (Cth)
ICA	<i>Insurance Contracts Act 1984</i> (Cth)
ICC	Institute Cargo Clause(s)
ISM	International Safety Management
ITC	Institute Time Clause(s)
IUA	International Underwriters Association
IUMI	International Union of Marine Insurance
IVC	Institute Voyage Clause(s)
MAT	Marine Aviation and Transport (or Transit)
MIA	<i>Marine Insurance Act 1909</i> (Cth)
MIA (Can)	<i>Marine Insurance Act 1993</i> (Can)

MIA (NZ)	Marine Insurance Act 1908 (NZ)
MIA (UK)	Marine Insurance Act 1906 (UK)
MLAANZ	Maritime Law Association of Australia and New Zealand
NZLC	The Law Commission of New Zealand
P&I	Protection and Indemnity
QCFO	Queensland Commercial Fishermen's Organisation
SOLAS Convention	Safety of Life at Sea Convention
TPA	<i>Trade Practices Act 1974 (Cth)</i>
UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development



# 1. Executive summary

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## **Introduction**

### **Terms of reference**

1.1 On 21 January 2000 the Attorney-General, the Hon Daryl Williams AM QC MP, asked the Commission to review the *Marine Insurance Act 1909* (Cth) (MIA). The terms of reference<sup>1</sup> required the Commission to review the MIA, taking into account

- any parts of the legislation which restrict competition
- the desirability of having a regime consistent with international practice in the marine insurance industry, and whether any change might result in a competitive disadvantage for the Australian insurance industry
- the effects on the environment, welfare and equity, occupational health and safety, economic and regional development, consumer interest, the competitiveness of business, including small business and efficient resource allocation
- compliance costs on small business.

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<sup>1</sup> The complete terms of reference are set out at p 3.

1.2 The terms of reference also required the Commission to

- identify the nature and magnitude of the social, environmental or economic problems that the Act seeks to address
- clarify the objectives of the Act
- assess alternatives, including non-legislative alternatives to the Act, and
- analyse and quantify the benefits, costs and overall effects of the Act and any proposed alternatives to it.

1.3 The Commission was also required to draft any appropriate legislation and explanatory memorandum to give effect to the recommendations in this Report. The Commission was required to report by 30 April 2001.<sup>2</sup> This Report sets out the results of the Commission's research and consultations and its recommendations for amendments to the MIA and to the *Insurance Contracts Act 1984* (Cth) (ICA).

1.4 The Attorney-General's Department examined the MIA in 1997 and produced an issues paper with a view to determining the precise scope and nature of any reform warranted. This initiative was in response to concerns that the MIA was out of date with commercial realities and that, in particular, the warranty provisions were unduly harsh on insureds.<sup>3</sup> The Commission took over this review upon the issue of the terms of reference from the Attorney-General in January 2000.

### **This report**

1.5 A summary of the Commission's recommendations is found in chapter 2. If adopted, they would involve significant amendment to the MIA. However, the Commission anticipates that the impact in practice on Australia's marine insurance industry is less than that which the scale of the changes to the wording of the MIA might suggest. The amendments would be made within the existing structure and layout of the MIA, which are familiar to the industry both within Australia and, because of the MIA's similarity to cognate legislation overseas, in foreign jurisdictions. A consolidated version of the MIA incorporating the changes recommended in this report is found in Appendix B.

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2 The terms of reference originally required the Commission to report not later than 31 December 2000. However, this deadline was extended to 30 April 2001 to enable the report to take into consideration international harmonisation initiatives which were considered by the Comité Maritime International at its conference in Singapore in February 2001.

3 Attorney-General's Department Issues paper *The Marine Insurance Act 1909* March 1997. The Queensland Commercial Fishermen's Organisation (QCFO) made a submission to the Attorney-General, complaining that there was unfair treatment of fishing vessels by insurers who relied on breaches of warranty to deny liability for claims where the breach was trivial or not causally connected to the loss. The QCFO is now known as the Queensland Seafood Industry Association.

1.6 This inquiry is the most recent in a line of such inquiries in various areas of insurance and maritime law that intersect in the area of marine insurance. The topic of marine insurance was omitted from the Commission's earlier inquiries into the law of insurance because, it was said, marine insurance was a discrete area with special significance for international trade and commerce.<sup>4</sup> Because it was not considered in previous reviews, the history of marine insurance law and the MIA and the international context in which it operates are considered in some detail in chapters 4–7.

1.7 In chapters 8–11 the report deals with the four areas that generated the most concern in the literature or that came to be of central importance during the course of the review. They are the coverage of the MIA; warranties and other statutory provisions with similar effect; non-disclosure, misrepresentation and the obligations of utmost good faith; and the requirement for an insurable interest. The later chapters (chapters 12–15) deal with a number of other areas that also merit specific attention, notably the documentary requirements set out in the MIA.

1.8 As required by the terms of reference, the Commission has prepared a draft Bill to give effect to the recommendations in this report and an explanatory memorandum to accompany that Bill (see Appendices C and D).

### **Advisory Committee**

1.9 The Commission arranged for an Advisory Committee consisting of judges, lawyers, insurers and others to assist on this reference. A list of the Advisory Committee members appears at page 6. Members of the Advisory Committee were asked to read and comment upon draft chapters of the Discussion Paper and the Report, and gave generously of their time. Some members had to travel extensively to attend meetings. The Advisory Committee considered and commented upon final recommendations contained in this Report and was influential in the shape of these final recommendations. The Commission derived enormous assistance from the Advisory Committee and extends its deep appreciation to its members for their time, patience and generosity.

### **Consultations and submissions**

1.10 The Commission conducted an extensive series of consultations around Australia and received a number of written submissions, a list of which is set out in Appendix A.

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<sup>4</sup> Australian Law Reform Commission Discussion Paper 7 *Insurance contracts* Sydney 1979 (ALRC DP 7) 5.

1.11 The Australian Law Reform Commission Discussion Paper 63, *Review of the Marine Insurance Act 1909* (ALRC DP 63) was published in July 2000 and was a major focus of subsequent consultations.

1.12 Because marine insurance is an inherently international business, there is a strong call for Australian law and practice to be consistent with overseas, especially UK, law and practice, at least in general approach. The Commission was, therefore, keen to canvass opinion from overseas sources as well as Australian. Accordingly, the Commission met with representatives of Lloyd's of London and the London insurance market, and was represented at the conference of the Comité Maritime International in Singapore in February 2001 in order to inform others in the international marine insurance community of the Commission's work and to solicit commentary from non-Australian sources that could be used as points of comparison with Australian and UK law and practice.

### **The approach to reform**

1.13 Chapter 3 deals with a major threshold issue: whether to retain the MIA, with either minimal or more significant amendment, or to repeal it entirely and include marine insurance within the scope of the ICA.

1.14 Although the amendments proposed by the Commission would reduce the differences between the MIA and the ICA, the Commission considers that the familiarity of practitioners both within Australia and overseas with the basic structure of the MIA warrants its retention as a separate scheme as the amendments are more readily identifiable and accommodated by those practitioners. Furthermore, if all marine insurance contracts were covered by the ICA regime, many sections of the MIA would have to be re-enacted in the ICA to retain certain distinctive provisions that underpin marine insurance contracts both in Australia and in other countries whose legislation is based on the Marine Insurance Act 1906 of the United Kingdom. Accordingly, the Commission does not recommend the repeal of the MIA.

### **The coverage of the *Marine Insurance Act***

1.15 This area is covered in chapter 8 of the report. The first principal reform relating to the scope of the MIA is the removal from it to the ICA of contracts for the transportation of goods for non-commercial purposes. This is consistent with the overall approach that consumer contracts of insurance should be covered by the ICA (although that Act also covers many forms of commercial insurance) and extends the refinement in this area commenced by the enactment in 1998 of ICA s 9A, pursuant to which the insurance of pleasure craft was moved from the MIA to the ICA. Consistently with that amendment, the Commission recommends that a new s 9B be inserted into the ICA rather than amending the MIA itself.

1.16 The second principal change in the coverage of the MIA is to extend it to include adventures on inland waters. At present, the Act's operation is confined to maritime adventures (that is, sea voyages) and incidental non-maritime risks. There is some difficulty in determining the point at which a contract covering numerous and varied insurance risks ceases to be covered by the MIA and is therefore covered by the ICA. Although the statute cannot be re-worded so as to avoid all further uncertainty, the modest expansion recommended in this regard removes some areas of uncertainty. It is also consistent with the overall philosophy that consumer insurance of a maritime nature should be covered by the ICA but that commercial marine insurance should be covered by MIA. The distinction between insurance covered by the two Acts is not arbitrary but is based on the commercial or non-commercial nature of the insured activities.

## **Warranties**

1.17 Warranties are discussed at length in chapter 9 of the report. The Commission's recommendations in relations to warranties have two purposes. The first is to soften the often harsh and disproportionate impact on an insured of the remedies currently provided by the MIA in favour of insurers. Secondly, and consistently with certain other recommendations, the amendments will force warranties, including implied warranties, onto the face of the contract so that both parties, and the insured in particular, can be under no misapprehension as to the content of the contract, the terms that they are required to comply with and the ramifications of any breaches.

1.18 To this end, the Commission recommends the abolition of the concept of warranties. However, in place of express warranties, the Commission proposes a regime under which the insurer has a number of structured remedies available to it should there be a breach of any express term of the contract by the insured.

1.19 The Commission also recommends that the implied warranties of seaworthiness and legality be removed. However, the Act should specifically permit contracts of marine insurance to include express terms relating to the seaworthiness of a ship and in relation to the legality of the purpose of the insured voyage and the manner in which it is carried out. In order to obtain the protection that is currently available to them under the MIA (to the extent that it is preserved under the amendments), insurers should be required to reword their documentation so that all terms on which they wish to rely appear on the face of the contract. Modern insurance practice often includes express terms dealing with these matters which, to the extent of any inconsistency, override the implied warranties. Accordingly, the amendments may in fact force fewer changes in practice than might first be imagined.

1.20 The remedies for a breach of an express term relating to the seaworthiness of a ship are essentially the same as for a breach of any other express term except that the insurer is no longer liable to indemnify the insured for loss which is ‘attributable’ to the breach. The term ‘attributable’ has been used to better reflect the current position and in contrast to the stricter test of proximate causation. Therefore, a causal connection between the unseaworthiness of the ship and the loss that is looser than that required in relation to other express terms will entitle an insurer to relief. However, this applies only if the breach of a term relating to unseaworthiness arises where the insured was aware of the facts constituting the unseaworthiness, that those facts constituted unseaworthiness, and failed to take whatever steps might reasonably have been available to it to remedy the position. Thus, insureds who do not know of the unseaworthiness, or were in no position to do anything about it once it arose, will nonetheless be covered. This reflects with some modification the current position in relation to time policies.

1.21 As a matter of public policy, the Commission has recommended that an insurer be relieved of all liability under a contract of marine insurance if the insured voyage is carried out for an illegal purpose, at least to the extent that the insured was in a position to control the matter. In that event, the premium is not returnable as the breach can be regarded as serious as fraud. If, on the other hand, the voyage is not carried out in a legal manner, which may involve only a relatively slight technical breach of regulation, the insurer is only relieved of liability to indemnify the insured for any loss attributable to the breach. Accordingly, trivial or purely technical breaches which do not themselves lead to loss will not prejudice an insured if loss is caused by some other insured peril.

1.22 One major criticism of the operation of warranties in the MIA is that any breach, however trivial and unrelated to any loss, entitles the insurer to be relieved automatically of all liability under the policy from the date of the breach, although without prejudice to any liabilities that may have arisen prior to the breach. There is no capacity for the insured to remedy the breach, and the remedies available to the insurer are the same whether or not the breach was in any way causative of the loss, fraudulent or negligent (with some qualifications). The proposed remedy for breach of an express term is that the insurer, although not discharged from liability under the policy as a whole, is discharged from all liability to indemnify the insured for any loss which was proximately caused by the breach. The policy otherwise remains on foot. In this way, the insured cannot benefit from its breach but retains the benefit of the policy as a whole. On the other hand, the insurer is not bound to indemnify the insured for a loss caused by the insured’s own breach of contract. Although not stated in the amended MIA, the insured acquires the ability to remedy a breach of a contractual term before loss as a logical consequence of these amendments.

1.23 The statutory provisions may be modified by the contract but the Act prevents a term being included in a contract of marine insurance that provides for remedies more favourable to the insurer.

1.24 If there is a breach of an express term of any sort, the insurer will be entitled to avail itself of a new statutory right of cancellation of the policy, subject to anything to the contrary in its contract. At present, the MIA does not have any provision granting the insurer the right to terminate the contract if there is a breach by the insured although such provisions were introduced into the ICA. The Commission considers that the MIA and ICA should be parallel in this respect.

### **Utmost good faith**

1.25 Chapter 10 deals with the issues of utmost good faith. The reforms in this area recommended by the Commission fall into two broad categories: reform of the basic nature of the obligations of utmost good faith and reforms relating to the specific duties of the insured in relation to complete and accurate disclosure of material circumstances before the contract is concluded.

1.26 At present, the MIA provides that utmost good faith is the basis of every contract of marine insurance and that, if one party does not observe the utmost good faith in relation to the other, the other party may avoid the contract entirely. This remedy is, however, of almost no value to insureds, who in most cases would want the contract to remain on foot if there has been any breach by the insurer so that the insured gets the benefit of indemnity if there is any loss. The avoidance of the policy and return of the premium would often be of little, if any, assistance.

1.27 This concept was amended in relation to non-marine insurance with the enactment of the ICA, which makes the duty of utmost good faith an implied term of the contract. As a result, if there is any breach of the duty of utmost good faith, a much wider range of remedies is available to a court than is currently provided by the MIA. Most notably, the award of damages may much more effectively compensate the innocent party.

1.28 Under the amended MIA, a breach of the obligations of utmost good faith by the insured entitles the insurer to cancel the policy under the new statutory right of cancellation, subject to anything to the contrary in the contract.

1.29 The amendments in relation to the obligations for complete and accurate disclosure (which require full disclosure of all material circumstances and prohibit misrepresentation) before the contract is concluded have been modified to accommodate two problematic areas. Firstly, the current regime requires an insured (or its agent) to disclose accurately all material circumstances. Circumstances are material if they would influence a prudent insurer in determining whether it will

accept the risk and, if so, on what terms. They do not have to have a decisive influence on the prudent insurer. This imposes on the insured an obligation to understand what is material to a prudent insurer. Secondly, prior to the decisions of the House of Lords in *Pan Atlantic Insurance Co Ltd v Pine Top insurance Co Ltd*<sup>5</sup> and the Supreme Court of Victoria in *Akedian Co Ltd v Royal Insurance Australia Ltd, Sun Alliance Australia Ltd*<sup>6</sup> there was no requirement that the actual insurer be induced by the non-disclosure or misrepresentation to enter into the contract. Accordingly, an imprudent insurer could avoid the consequences of its imprudence by relying on the objective standard of a prudent insurer.

1.30 The Commission's recommendations modify the requirement of disclosure and prohibition of misrepresentation so that the insured is required only to disclose those circumstances which it knows to be material or which a reasonable person in its position would know to be material. The test of materiality is itself unchanged.

1.31 However, except in the case of fraud, the insurer is no longer entitled to avoid any liability unless it was actually induced by the non-disclosure or misrepresentation to enter into the contract. If the misrepresentation or non-disclosure is fraudulent, the insurer is entitled to avoid the contract entirely and to keep the premium. If the breach is not fraudulent but the insurer would not have entered into the contract at all, the insurer is entitled to avoid the policy but must return the premium. If it would have entered into the contract but on different terms, the insurer is not relieved from liability under the contract as a whole. However, it does not have to indemnify the insured for any loss attributable to the matter which was the subject of the misrepresentation or non-disclosure, and can modify any liability it does have to the insured to take into account any additional premiums, deductible or excess that may have been imposed.

1.32 In the event of any breach of the obligations of non-disclosure and accurate representation, the insurer is also entitled to cancel the contract under the Act, subject to anything to the contrary in the contract.

## **Insurable interest**

1.33 Chapter 11 of the report reviews the requirement under the MIA that an insured have an insurable interest in the insured property at the time of loss. Although this interest is not required when the contract is concluded, the insured must nonetheless have at that time an expectation of acquiring an insurable interest.

1.34 These requirements were abolished by the ICA in relation to non-marine insurance. It is sufficient for an insured to recover under a non-marine policy if it

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5 [1995] 1 AC 501.

6 (1997) 148 ALR 480.



has suffered a pecuniary or economic loss as a result of loss of or damage to the insured property. Those changes do not appear to have resulted in any difficulty or problems since enactment over 15 years ago.

1.35 The requirement for an insurable interest appears to create problems in two sets of circumstances. The first is that insureds that purchase goods on FOB, C&F or CFR terms do not have an insurable and an insured interest in the goods prior to loading aboard a ship (even if they have paid for them before this time) unless that policy includes both a 'lost or not lost' clause and warehouse-to-warehouse cover. Secondly, the assignment of a policy of marine insurance can be ineffective if it is assigned when the insured has already parted with or lost its insurable interest.

1.36 However, the insurance industry has strongly advocated the retention of the requirement for an insurable interest as it is said to be an integral part of marine insurance. The Commission is not convinced that the requirement for an insurable interest is necessary to preserve marine insurers' legitimate rights. Their position is protected by the fundamental principle that an insured can only be indemnified for loss that it has actually suffered and by the requirement that the insured have suffered an economic or pecuniary loss due to the loss of or damage to the insured property. The Commission recommends that the requirement for an insurable interest be abolished.

1.37 However, acknowledging the strength of the opposition to change in this area, the Commission has made a number of alternative recommendations that modify some aspects of the requirement for an insurable interest while leaving the requirement basically intact.

## **Subrogation**

1.38 The various issues surrounding the basic concept of the insurer's rights of subrogation are discussed in chapter 12. The Commission's recommendations propose changes on two topics.

1.39 The MIA is silent on the distribution between the insurer and insured of money recovered from third parties, whether by the insurer pursuing its rights of subrogation or by the insured itself. The common law provides only limited guidance and the ICA, although modifying the common law in relation to non-marine insurance, does not provide a comprehensive regime. The Commission's proposals set out a complete system for the distribution of money received from third parties, though this may be modified by agreement between the parties.

1.40 The second area of proposed change is the insertion into the MIA of a new section reflecting the provisions of ICA s 68. This relates to the effect on an insurer's rights of subrogation of contracts entered into by the insured with third

parties that limit or exclude the insured's rights of recovery from that third party in the event of loss of or damage to the insured property. Such contracts also limit or exclude the insurer's right to recover from the third party under the insurer's rights of subrogation. ICA s 68 prevents an insurer from relying on a term of the policy that limits its liability to indemnify the insured by reason of the existence of any such third party contract unless that the insurer clearly informed the insured of that term before the contract of marine insurance was concluded. Section 68 also stipulates that the existence of such contracts does not have to be disclosed by the insured before the contract of marine insurance is concluded.

## **Intermediaries**

1.41 This topic is discussed in chapter 13. The MIA contains several provisions dealing with the role of agents and brokers. Sections 25–26 relate to an agent's obligations of pre-contractual non-disclosure and accurate representation. Section 58 deals with the obligation to issue a policy once premium has been paid or tendered. Sections 59–60 deal with the relationship between the intermediary and the insurer and insured in relation to the payment of money. There is no comprehensive scheme covering the relationship between the intermediaries and the principal parties to the contract.

1.42 The ICA contains very little about intermediaries because the subject is covered comprehensively in relation to non-marine insurance in the *Insurance (Agents and Brokers) Act 1984* (Cth) (IABA). The IABA provides a thorough and considered scheme governing the relationship of the various parties whereas the MIA offers a partial scheme only. However, there is some doubt as to the extent to which the IABA also covers marine insurance.

1.43 The IABA is to be repealed when the Financial Services Reform Bill (FSRB) becomes law. The FSRB provides for a licensing regime for financial service providers, which will cover all insurance brokers. However, marine insurance is excluded from the operation of the portion of the FSRB which covers other aspects of the relationship between the parties to the insurance contract.

1.44 The Commission considers that there is no reason in principle why the regulation of the business of marine insurance in Australia should be different from that of non-marine insurance. Its recommendation is that the IABA or its successor legislation should cover marine insurance as well as non-marine insurance and should be amended accordingly.

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## **Choice of law and jurisdiction**

1.45 Chapter 14 discusses the issues surrounding questions of the contractual freedom to choose the law governing contracts of marine insurance and the jurisdiction in which disputes should be determined.

1.46 In regard to both questions, the Commission concludes that the international nature of marine insurance generally warrants the retention of the parties' contractual freedom to choose the governing law of their contract and the jurisdiction in which their disputes will be heard. The flexibility of the MIA is widely seen as one of its strengths but there was concern that any advantages that reform to the MIA might bring could be sidestepped by parties choosing another system of law. The ICA expressly prevents the application of foreign law where the proper law of the contract (determined without reference to any express choice of law in the contract itself) would be the law of an Australian state or territory. It also prevents parties from contracting out of the application of the ICA if that would be to the advantage of the insurer. The Commission does not consider that this approach is appropriate for marine insurance.

1.47 The Commission also recommends that the MIA be amended to give the Federal Court of Australia jurisdiction in all marine insurance matters, to be exercised concurrently with the courts of the states and territories.

## **Policies and contracts**

1.48 Chapter 15 covers a number of issues which go to the formalities of the contracts and policies of marine insurance, and the structure and language of the MIA.

1.49 MIA s 28(1) prevents the admission into evidence of any contract of marine insurance unless a policy has been issued in an action for recovery under a policy. The policy is the physical embodiment of, but distinct from, the contract, which is concluded as soon as the insurer accepts the insured's proposal. The origin of the restriction in s 28 lies in the protection of stamp duty revenue. That purpose no longer being necessary, the Commission recommends that the relevant portion of s 28 be repealed.

1.50 For similar reasons, the Commission recommends the repeal of the prohibition in MIA s 31 of time policies for periods over 12 months. This provision was also originally designed to protect stamp duty revenue and is also outdated.

1.51 The Commission also recommends changes to MIA s 35 to expand the statutory acceptance of floating policies to cover annual and open cover in order to remove any uncertainty about their status as policies within the meaning of the MIA.

1.52 The Commission considers it important that the law governing the formalities of contracts and policies of marine insurance be amenable to electronic commerce. However, after considering the provisions of the *Electronic Transactions Act 1999* (Cth), the Commission has concluded that no further amendment to the MIA itself is needed and that the *Electronic Transactions Act 1999* is sufficient to provide appropriate flexibility to, and protection for, the parties.

1.53 After considering the possible overall modernisation of the wording of the MIA itself, the Commission has rejected the idea that the wording to the Act should be corrected, for example, to remove inappropriate gender references, unless the provisions in question are being amended for other reasons. Possibly obsolete terms and provisions (such as ‘barratry’ and ‘vermin’) have not been deleted as the concepts that they describe still arise from time to time.

1.54 However, a small change to the provisions relating to mutual insurance has been recommended to bring it more into line with contemporary practice.

1.55 The Commission recommends the repeal of the antiquated specimen policy wording found in the second schedule to the MIA, which has its origin in the 17th century, but the retention of the Rules for Construction which form part of it as they provide definitions for some commonly used terms in policies of marine insurance.

## 2. Summary of recommendations

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### **Introduction**

2.1 The Commission's recommendations resulting from its inquiry into the *Marine Insurance Act 1909* (MIA) are set out in summary form in this chapter.

2.2 The Commission proposes that the amendments recommended by it should apply to contracts of marine insurance concluded or renewed on or after the day on which the amendments take effect. With one qualification, the Commission proposes that the proclamation date be set to give time to the marine insurance industry to adjust to the changes, particularly as they will require some careful reconsideration of the standard and other common terms of its contracts.

2.3 The terms and the timing of the commencement of the amendments to the MIA s 59 and 60 are more complex as they both depend on the fate of the *Insurance (Agents and Brokers) Act 1984* (IABA) and the Financial Services Reform Bill 2000 (FSRB). The wording of the bill amending the MIA and the date on which amendments to s 59–60 will commence will depend on when the FSRB is passed and whether it or the IABA are amended to remove the exclusion of marine insurance from their operation.

## **The approach to reform**

1. The MIA should be retained as a separate legislative regime for marine insurance with the changes recommended elsewhere in this report.

## **The coverage of the *Marine Insurance Act***

2. The ICA should be amended to cover contracts of insurance for the transportation by water of goods other than goods being transported for the purposes of a business, trade, profession or occupation carried on or engaged in by the insured. This amendment will have the effect of removing the insurance of the carriage of goods for non-commercial purposes from the MIA. MIA s 7 should be amended to state that it is subject to s 9A and the proposed s 9B of the ICA.
3. MIA s 8(1) should be amended to refer expressly to losses arising from any air risk incidental to a sea voyage.
4. MIA s 8(2) should be amended to refer expressly to losses arising from the repair of a ship.
5. The MIA should be amended so that, subject to the terms of the contract, marine insurance covers risks on inland waters and that where appropriate the 'sea' and the 'seas' should be read as including inland waters.
6. MIA s 8(2) should be amended to delete the reference to 'a policy in the form of a marine policy' and to state that the risks referred to in it are covered by the MIA unless the contract states otherwise.

## **Warranties**

7. The concept of warranties, both express and implied, as used in the law of marine insurance should be abolished and replaced with a system permitting the subject matter currently covered by them to be the subject of express terms of the contract. Except as provided by the Act as amended and subject to the terms of the contract, a breach by the insured of an express term (including those replacing warranties) will entitle insurers to be relieved of liability to indemnify the insured for a loss where the breach is causative of that loss.

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**Express warranties**

8. Obligations currently covered by express warranties should be dealt with as express terms of the contract.
9. Subject to the contract, the MIA should be amended so that an insurer is entitled to be discharged from liability to indemnify the insured for any loss proximately caused by a breach by the insured of any express term of the contract.

**Warranty of seaworthiness**

10. The MIA should be amended to repeal the implied warranties of seaworthiness. Obligations of seaworthiness should be dealt with as express terms of the contract.
11. The MIA should be amended so that an insurer is discharged from liability to indemnify the insured for any loss attributable to a breach of an express term of the contract relating to the seaworthiness of a ship where the insured knew or ought to have known of the relevant circumstances and that they rendered the vessel unseaworthy and where the insured failed to take such remedial steps as were reasonably available to it.

***Alternative recommendation***

12. If recommendations 10 and 11 are not adopted, the distinction between time and voyage policies with regard to the warranty of seaworthiness should be abolished and the formulation in MIA s 45(5) should be the basis of a common statement of the warranty. The implied warranty in MIA s 46(2) should be removed.

**Warranty of legality**

13. The MIA should be amended to repeal the implied warranty of legality. Obligations of legality should be dealt with as express terms of the contract.
14. The MIA should be amended so that where the insured is in breach of an express contractual term to the effect that, so far as the insured can control the matter, the insured adventure shall have no unlawful purpose, the insurer is discharged from all liability under the contract.
15. The MIA should be amended so that where the insured is in breach of an express contractual term to the effect that, so far as the insured can control the matter, the insured adventure shall be carried out in a lawful manner, the

insurer is discharged from liability to indemnify the insured in relation to any loss that is attributable to that breach.

### **Change of voyage**

16. The provisions of the MIA s 48 and 51–55 relating to change of voyage, deviation and delay should be repealed, permitting these concepts to be dealt with as express terms of the contract. MIA s 49–50, which deal with the attachment of the risk, should be retained.

### **Interpretation of express warranties**

17. The provisions of the MIA dealing with the warranties of neutrality, nationality and good safety (MIA s 42–44) should be repealed as redundant because they are rarely used in practice and can be the subject matter can be dealt with by express terms.

### **Cancellation rights**

18. The MIA should be amended to include new provisions based on ICA s 59–60 stipulating the insurer's rights of cancellation. These rights are subject to the terms of the contract. They arise when the insured has failed to comply with a term of the contract, breached the duty of utmost good faith, made a fraudulent claim under the contract or where otherwise permitted by the Act as amended in accordance with these recommendations. Written notice must be given to the insured. The cancellation may take effect either three business days after the insured received that notice or earlier if replacement insurance comes into effect before then.

### **Burden of proof**

19. The MIA should be amended to include new provisions that
- (1) the insurer bears the burden of proving that there was a breach of a term of the contract and
  - (2) the insured bears the burden of showing that the loss for which it seeks to be indemnified was not proximately caused by or attributable to (as the case may be) the breach.

These provisions are not intended to alter the burdens of proof provided for elsewhere by common law or statute.



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## **Duty of utmost good faith**

### **General**

20. MIA s 23 should be amended to provide that there is implied in a contract of marine insurance a provision requiring each party to act towards the other party with utmost good faith in the terms of ICA s 13 and 14.
21. The MIA should be amended to provide that the duties of utmost good faith extend for the life of the relationship between the parties to any contract of marine insurance, except in relation to any claim or other aspect of that relationship which is the subject of litigation between the parties. In such cases the duties of utmost good faith cease when one party commences litigation against the other but only in relation to the claim or other aspect of the relationship which is the subject of that litigation.

### **Non-disclosure and misrepresentation**

22. MIA s 24(1) and 26(1) should be amended to provide that an insured must disclose accurately all circumstances that it knows, or a reasonable person in its position would know, to be material.
23. MIA s 24(1) and 26(1) should be further amended by deleting the references to the insurer's right to avoid and a new provision should be inserted to set out the insurer's modified rights covering both non-disclosure and misrepresentation. (See recommendation 25.)
24. MIA s 25(a) should be amended
  - (1) to provide that an agent must disclose all circumstances that it knows, or a reasonable person in its position would know, to be material, to reflect the amended obligation owed by the insured (see recommendation 22) and
  - (2) by deleting 'or to have been communicated to', removing the insured's agent's obligation to disclose what ought to have been communicated to it.
25. The MIA should be amended to insert new provisions which provide that if the insured has breached its duties relating to non-disclosure and misrepresentation

- (a) (1) if the breach is fraudulent, the insurer is entitled to avoid the policy from its outset with no return of premium.
  - (2) if the breach is not fraudulent
    - (a) where the insurer would not have entered into the contract if it had known of the undisclosed circumstance or the truth of the misrepresented circumstance, the insurer is entitled to avoid the policy from its outset but with a return of premium
    - (b) where the insurer would have entered into the contract but on other conditions, the insurer is not entitled to avoid the policy but
      - (i) is not liable to indemnify the insured for a loss proximately caused by the undisclosed or misrepresented circumstance
      - (ii) is entitled to vary its liability to the insured to reflect the amount of any variation in premium, deductible or excess that would have been imposed if it had known of the undisclosed circumstance or the truth of the misrepresented circumstance and
      - (iii) is entitled to cancel the policy in accordance with the other provisions of the MIA on cancellation which are the subject of recommendation 18.
26. The MIA should be amended to include a provision based on ICA s 12 that the only duty of pre-contractual disclosure is that provided by MIA s 24–26 and that a contract of marine insurance may not impose a greater duty, or provide for remedies more favourable to the insurer, than those stipulated by the MIA as amended in accordance with these recommendations. The MIA should also be amended to permit express terms in contracts of marine insurance which provide for the insured’s post-contractual duty of disclosure.
27. The MIA should be amended to provide that following insurers are deemed to have been induced to enter into a contract if all leading insurers were induced.

### **Insurable interest**

28. MIA s 10–12 should be amended to be consistent with ICA s 16–17 in relation to the requirements for an insurable interest. That is, the MIA should provide that

- (c) (1) a contract of marine insurance is not void by reason only that the insured did not have an interest in the subject matter of the contract at the time when the contract was entered into; and
- (2) where the insured under a contract of marine insurance has suffered a pecuniary or economic loss by reason of damage to the insured property, the insurer is not relieved of liability under the contract by reason only that the insured did not have an interest at law or in equity in the property.

(Note alternative recommendations 30–31.)

- 29. MIA s 13–21, 57 and 90(3)(c) and (d), which rely on the concept of insurable interest, should be repealed as a consequence of the abolition of the requirement for an insurable interest.

***Alternative recommendations***

- 30. If recommendation 28 is not adopted and the requirement for insurable interest is retained, a new provision should be inserted into the MIA providing that a purchaser of insurable property acquires an insurable interest in that property by no later than the time when it pays for the property or when it becomes bound to pay for the property provided that it subsequently pays for it.
- 31. If recommendation 28 is not adopted and the requirement for insurable interest is retained, MIA s 16 should be amended to cover secured loans over insurable property generally, not just bottomry and respondentia.

**Subrogation**

- 32. The MIA should be amended to provide that, subject to any agreement between the insured and insurer, money recovered from third parties either by the insurer under its rights of subrogation or by the insured is distributed in the following order:
  - (1) The party or parties funding the recovery action are reimbursed for the administrative and legal costs of that action, pro rata if there is more than one such party and there are insufficient funds to reimburse them in full.
  - (2) (a) If the insurer has funded the recovery action, it is entitled to retain an amount equivalent to the amount it has paid to the insured under the contract of marine insurance. The insured is

- then entitled to be paid an amount so that the total amount that it receives under the contract of marine insurance and from the recovery action equals its total loss.
- (b) If the insured has funded the recovery action, it is entitled to retain an amount so that the total amount that it receives under the contract of marine insurance and from the recovery action equals its total loss. The insurer is then entitled to be paid an amount equal to the amount that it has paid under the contract of marine insurance.
  - (c) If the insurer and the insured have both funded the recovery action, they are entitled to the amounts referred to in (a) and (b) above, pro rata if there are insufficient funds to reimburse them in full.
- (3) Any excess or windfall recovery is paid to the parties in the same ratio that they contributed to the administrative and legal costs of the recovery action.
  - (4) Notwithstanding the statements of principle above, any separate or identifiable component in respect of interest should be paid to the parties in such proportions as fairly reflect the amounts that each has recovered and the periods of time for which each lost the use of its money.
33. ICA s 68 should be re-enacted in the MIA as a new s 85A to provide that
- (c) (1) the insurer cannot rely on a term of a contract of marine insurance that has the effect of limiting or excluding the insurer's liability under the contract of marine insurance because the insured is party to an agreement with a third party that limits or excludes its rights to recover damages from the third party unless the insurer clearly informed the insured of that term before the contract of marine insurance was concluded and
  - (c) (2) such agreements with third parties do not have to be disclosed by the insured before the contract of marine insurance is concluded.

## **Intermediaries**

34. The *Insurance (Agents and Brokers) Act 1984* (IABA) and its successor provisions in the Financial Services Reform Bill should be amended to remove the provisions which exclude from their operation insurance in relation to which the MIA applies. As a consequence, MIA s 59 and 60 should be repealed with effect from the date on which the changes to the

IABA, or the relevant portions of the Financial Services Reform Bill, take effect.

### **Choice of law and jurisdiction**

35. The law of marine insurance in Australia should not restrict the right of parties to choose some other body of law as the governing law of the contract or to decide that disputes be resolved by a foreign court or other forum.
36. The MIA should expressly invest the Federal Court with jurisdiction in marine insurance matters generally (other than state insurance) as an incident of admiralty and maritime jurisdiction, to be exercised concurrently with state and territory courts.

### **Policies and contracts**

37. MIA s 28 should be amended to permit a contract of marine insurance to be admissible in evidence in legal proceedings as evidence of the contract.
38. MIA s 31(2), which restricts time policies to 12 months in duration, should be repealed as unnecessarily restrictive.
39. The existing MIA s 29 should become s 29(1) and a new subsection 29(2) should be inserted stating that no marine policy is invalid by reason only that it does not comply with the existing formal requirements in s 29(1).
40. MIA s 35(1) should be amended to include open and annual policies and to make all necessary changes to the description of the subject matter in s 35(1) and to the heading to s 35.
41. MIA s 35(3) should be amended to make it clear that the words ‘Unless the policy otherwise provides’ extend to the opening clause of the second sentence so that they apply to the requirement that all declarations under floating, open or annual policies must comprise all consignments within the terms of the policy.
42. MIA s 56 should be amended to include assignment of contracts as well as policies. If, contrary to recommendation 29, MIA s 57 is not repealed, it should also be amended to include assignment of contracts as well as policies. The words ‘or contract’ should be inserted into these sections and the heading wherever reference is made to a policy.

43. MIA s 36 and the Form of Policy contained in the Second Schedule of the MIA should be repealed. The Rules for Construction of Policy in the Second Schedule should be re-enacted in a new s 3A in the MIA.
44. MIA s 91(1) should be amended to refer expressly to an association formed by two or more persons in order to insure each other.

## 3. The approach to reform

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### **Introduction**

3.1 This chapter examines factors that have informed the overall approach to reform adopted by the Commission and which are reflected in the recommendations presented in the following chapters and in the provisions of the draft bill (Appendix C).

3.2 An important threshold issue is the extent to which the law of marine insurance should continue to differ from the law applying to most other contracts of general insurance under the *Insurance Contracts Act 1984* (ICA). Marine insurance could be subsumed, partially or completely, within the law applying to non-marine general insurance. Another possible framework for reform would be a combined transport insurance regime, covering marine, aviation and land transport insurance (an MAT Act). For the reasons set out in this chapter, such fundamental change has not been embraced by the Commission, which recommends the retention of a distinct marine insurance legislative regime, though one more similar to the ICA.

3.3 A number of factors dictate that reform of the *Marine Insurance Act 1909* (MIA) should be approached with care. The present codification of marine insurance law and practice is long established and well known, at least to those within the insurance industry, contributing to a business environment in which the meaning of contracts is well understood and is backed up by comprehensive case law. In Australia prior to 1985, and to the current day in the United Kingdom, the common law of insurance contracts generally very closely reflected the MIA and,

except where comprehensive statutory schemes intervened, such as in workers compensation, the law covering marine and non-marine general insurance was essentially the same.<sup>7</sup>

3.4 The MIA is said to have stood the test of time. If that expression means that it has survived a long time without change, then it is accurate. However, it has not done so without criticism, especially over the last 20 years, and in that sense it now runs the risk of failing that test.

3.5 It is feared that radical unilateral changes to Australian marine insurance law may impact adversely on and isolate the Australian market by severing the association between Australian and United Kingdom law and practice, a link shared with marine insurance regimes in other common law systems and, in practice if not in law, in many other countries as well. The Commission's research has shown that although there is a common basis of the law of marine insurance found in many countries, particularly those in the common law world, there is certainly no uniformity and it is clear that the international marine insurance market tolerates a wide degree of variation in law and practice. Reform of the MIA must also take into account possible moves towards harmonisation of international marine insurance regimes, particularly those initiated by the Comité Maritime International (CMI), discussed in paragraphs 7.24–7.30 below.

3.6 The influence of these factors and other reform initiatives overseas on the Commission's conclusions is examined in this chapter. As will be seen, important as these moves may be, they could not produce substantial results in time to influence this report though they are developments that both government and industry within Australia should continue to monitor.

## **Marine and non-marine insurance**

### **Australian insurance law regimes**

3.7 Australia has several insurance law regimes. The MIA governs contracts of marine insurance. This provides a partial code and touches on all major aspects of modern marine insurance law. Common law rules, in so far as they are not inconsistent with the express provisions of the MIA, continue to apply to contracts of marine insurance.<sup>8</sup>

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7 In this report the term 'general insurance' is used to cover non-marine insurance other than life insurance, reinsurance and those areas of insurance covered by their own statutory schemes.

8 MIA s 4.



3.8 Most non-marine insurance is governed by the ICA, including the insurance of risks in respect of commercial aircraft and land transport.<sup>9</sup> The ICA does not apply to contracts covered by the MIA.<sup>10</sup> In 1998 the insurance of pleasure craft was excluded from the MIA and brought within the ICA.<sup>11</sup> As with the MIA, the ICA does not purport to be a complete or exclusive code in relation to insurance contracts.<sup>12</sup>

3.9 A range of insurance contracts is covered by neither the ICA nor the MIA. The ICA specifically excludes contracts of health insurance, insurance relating to workers compensation and third party injury motor vehicle insurance.<sup>13</sup> Some of these, such as workers compensation and third party injury motor vehicle insurance, are governed by comprehensive state or federal legislative schemes.<sup>14</sup> Reinsurance is also specifically excluded from the ICA and is governed by the common law or the MIA. The MIA does not exclude reinsurance if it otherwise covers maritime perils.

### The MIA and the ICA

3.10 While the drafters of the MIA sought to restate rather than change the general law of marine insurance, the ICA intentionally and extensively modifies common law principles.<sup>15</sup> Australia is unique in the common law world in having a comprehensive legislative regime covering non-marine general insurance. The existence of the ICA necessarily colours the approach to reform of any aspect of insurance law in this country, not least by forcing reformers to justify the existence of disparate regimes of insurance law more than might be the case elsewhere.

3.11 There are significant differences between the MIA and the ICA, for example in relation to insurable interests, the duty of utmost good faith, warranties and the remedies for breach of warranty. Marine insurance is said to be ‘in a class by itself and is subject to its own long standing code which has the dual advantages of internal consistency and of detail’.<sup>16</sup> In general the MIA provisions, as compared with those of the ICA, favour the interests of the insurer over the insured.

9 However, a contract of marine insurance may cover mixed sea and land risks: MIA s 8. See para 8.9, 8.36, 8.39 and 8.43.

10 ICA s 9(1)(d).

11 ICA s 9A inserted by the *Insurance Laws Amendment Act 1998* (Cth). See para 3.13 and 8.14–8.16.

12 ICA s 7.

13 ICA s 9.

14 eg third party motor vehicle: *Motor Accidents Act 1988* (NSW); *Transport Accident Act 1986* (Vic); workers compensation: *Workers Compensation Act 1987* (NSW); *Accident Compensation Act 1985* (Vic); *Safety Rehabilitation and Compensation Act 1988* (Cth); *Seafarers Rehabilitation and Compensation Act 1992* (Cth). The insurance of commercial aircraft between 1986 and 1997 came under the common law as it was outside the ICA: *Statute Law (Miscellaneous Provisions) No 1 Act 1986* (Cth). The insurance of commercial aircraft is now once more covered by the ICA: *Financial Laws Amendment Act 1997* (Cth).

15 ICA s 7, LBC *The Laws of Australia* vol 22 Insurance and Income Security ‘22.1 Insurance’ para 2.

16 LBC *The Laws of Australia* vol 22 Insurance and Income Security ‘22.1 Insurance’ para 269 (specifically in the context of reform of the concept of insurable interest).

### The commercial orientation of the MIA

3.12 Marine and non-marine insurance contracts are subject to different legal regimes not simply because of historical accident but because the issues, players and markets are different. This is reflected in the commercial focus of the MIA and the consumer orientation of the ICA.

3.13 This distinction between the MIA and ICA was accentuated by an amendment to the ICA in 1998 which moved the insurance of pleasure craft from the MIA to the ICA.<sup>17</sup> The explanatory memorandum to the Insurance Laws Amendment Bill 1997 noted that the MIA was ‘primarily designed to cover insurance contracts relating to the international carriage of goods’ and the intention was that individuals who owned pleasure craft should receive the consumer protection benefits of the ICA.<sup>18</sup> This amendment placed insurance of the largest group of non-commercial vessel interests into the ICA and arguably removed from the MIA those insurance contracts that most needed consumer protection. Insurers and others have told the Commission that prior to this reform the market was already applying ICA principles to pleasure craft insurance.<sup>19</sup> If this is so, the amendment did little more than reflect that practice and could not be regarded as radical. Indeed, it appears to have given rise to no adverse comment either at the time or subsequently.

3.14 With the exception of the carriage of domestic and household goods, the MIA is essentially left to govern only commercial insurance. This is one reason why it is argued that marine insurance should continue to be subject to its own regime. The question of the carriage of non-commercial goods is dealt with at paragraphs 8.24–8.29.

3.15 In consultations, insurers and others have highlighted the need to retain a distinction between insurance covered by the ICA, which often involves ordinary consumers, and the commercial focus of insurance under the MIA regime.<sup>20</sup> The idea of subsuming, partially or completely, marine insurance within the law applying to non-marine general insurance was not embraced in consultations or submissions, not even by those most critical of particular aspects of the MIA and in favour of far-reaching amendments to it in those areas.

3.16 Instead, submissions strongly favouring the retention of the MIA as a separate regime and emphasised that the MIA and ICA serve different functions

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17 ICA s 9A.

18 Explanatory memorandum: Insurance Laws Amendment Bill 1997. The memorandum also noted that the MIA had not been amended since its enactment due to ‘international constraints’.

19 Legal practitioners *Consultation* Sydney 1 May 2000; Insurers and legal practitioners *Consultation* Sydney 15 May 2000.

20 eg Insurers and broker *Consultation* Sydney 27 March 2000; Judge *Consultation* Brisbane 11 May 2000; Lawyers and insurers *Consultation* Sydney 15 May 2000; Insurers *Consultation* Melbourne 6 June 2000.

and interests. The consumer protection provisions in the ICA were generally considered inappropriate for marine insurance, where the interests of the parties in retaining flexibility and full freedom of contract should be the paramount consideration.<sup>21</sup> The following comments reflect the overall tenor of the submissions.

Simply merging the MIA into the ICA is not a viable option. ICA was conceived for non-marine, principally domestic, insurances and contains many provisions which are unacceptable in the world of marine insurance. ICA is too rigid and lacks the flexibility and freedom to contract the MIA allows. I strongly favour continuing to have a legal distinction for marine insurance, however accept that the MIA needs modernising.<sup>22</sup>

3.17 The fact that the MIA essentially governs only commercial insurance is not by itself a sufficient reason to reject the idea of bringing marine insurance within the ICA. Many insurance contracts governed by the ICA are clearly commercial in nature, including aviation and most inland transport insurance.<sup>23</sup> As the Commission observed in its 1982 report *Insurance Contracts*,<sup>24</sup> the idea that legislation reforming insurance law should be restricted to certain categories of insurance so as, for example, to exclude transactions involving corporate insured parties raises the following question.

If the general law of insurance is unfair to individuals, why is it not unfair to individuals when they are in business? Most businessmen are not legal experts. Nor are they insurance experts.<sup>25</sup>

3.18 However, the commercial orientation of the MIA means that less weight needs to be given to consumer protection concerns and more to the interests of the marine insurance industry in having a regime consistent with international practice.

3.19 In examining reform options, the provisions of the ICA were a central consideration. In principle, greater consistency between the law governing marine insurance and non-marine general insurance is desirable. In many areas the Commission examined whether provisions based wholly or in part on the ICA model should be adopted in the MIA. In some of these areas the Commission recommends that reform follow the ICA model (for example in relation to the nature of the obligations of utmost good faith). In others, such as in relation to

21 eg P Grieve *Submission 6*; Law Society of WA *Submission 7*; K Carruthers *Submission 9*; Law Council of Australia *Submission 10*; Insurance Council of Australia *Submission 11*; MLAANZ *Submission 12*.

22 P Grieve *Submission 6*.

23 The ICA distinguishes between certain types of insurance and operates differentially among them. For example, certain of its consumer protection provisions apply only to contracts prescribed by regulation, including motor vehicle insurance, home buildings and contents insurance, sickness and accident insurance, consumer credit insurance and travel insurance: see ICA Part V; Insurance Contracts Regulations 1985.

24 ALRC 20.

25 *Ibid* para 26.

marine insurance warranties, some elements of the ICA model have been adopted but not others.

3.20 There was no support at all for the proposition that the MIA be repealed entirely and that marine insurance simply join all other general insurance under the ICA. Such a move would have the theoretical attraction of reducing the diversity of insurance law within Australia but on balance has little else to recommend it. Doing so would have accommodated many of the concerns expressed by the Commission and others about key areas for potential reform such as warranties and the obligations of utmost good faith. However, there are many provisions within the MIA that have not been the subject of any, or any major, criticism and which are not the subject of any recommendations in this report. Among them are s 61-94, which deal with loss and abandonment, measure of indemnity, subrogation, return of premium, mutual insurance and other peripheral matters. The majority of these would have required re-enactment in the ICA if the MIA had been repealed. For the most part, these provisions deal with concepts that are unique to marine insurance and maritime adventures (although their parallels could exist elsewhere) and underpin the operation of policies written under the MIA, whether or not those in the industry are conscious of that on a day-to-day basis.

3.21 Furthermore, if those provisions were re-enacted, the threshold question of what is marine insurance remains; it is merely transported to a different location. As will be seen in chapter 8 of this report, Australian insurance law presents a unique problem in relation to determining the scope of marine insurance. This can only be removed if there is one statutory regime covering all general insurance. As long as there are any aspects of insurance law that distinguish between marine and non-marine insurance, this threshold question persists.

3.22 The alternative, to retain the MIA but to amend it to improve its operation and fairness, has the advantage of limiting the apparent scale of the amendments. If the existing structure is retained, it is relatively easy for practitioners in the industry familiar with the current Act to identify, understand and bring their operations into line with the changes. This is perhaps a stronger consideration for non-Australian practitioners who have to deal with Australian insurance and who might well be familiar with the MIA (or parallel legislation overseas) but who would find the ICA quite novel. The source of the law remains the same even if its content has changed in areas that can be quickly identified.

3.23 On balance, therefore, the Commission recommends that the MIA be retained as a separate insurance regime though other recommendations in this report have the effect of modifying the range of contracts to which it will apply and the way in which it will apply to them.

**Recommendation 1. The MIA should be retained as a separate legislative regime for marine insurance with the changes recommended elsewhere in this report.**

## Marine, aviation and transport insurance

3.24 In the Discussion Paper, the Commission asked whether the MIA should be replaced with a single comprehensive marine, aviation and transport (MAT) insurance regime and, if so, whether such a regime should cover all MAT insurance or deal primarily with cargo insurance.<sup>26</sup> The Commission noted that in the UK, for some limited purposes, MAT insurance is a recognised category of insurance, a statutory definition of which is the effecting and carrying out of contracts of insurance

- (a) Upon vessels used on the sea or on inland water or upon the machinery, tackle, furniture or equipment of such vessels and against damage arising out of or in connection with the use of vessels on the sea or on inland water, including third party risks and carrier's liability;
- (b) Upon aircraft or upon the machinery, tackle, furniture or equipment of aircraft or against damage arising out of or in connection with the use of aircraft, including third-party risks and carrier's liability;
- (c) Against loss of or damage to railway rolling stock;
- (d) Against loss of or damage to merchandise, baggage and all other goods in transit, irrespective of the form of transport;
- (e) Against death or personal injury sustained as a result of travelling as a passenger on any of the forms of transport mentioned above.<sup>27</sup>

3.25 The UK Law Commission, in excluding MAT insurance from its 1980 recommendations for reform of insurance law, provided reasons for the continued separation of MAT from other general insurance.

<sup>26</sup> ALRC DP 63 para 2.37–2.45; Question 6.

<sup>27</sup> Insurance Companies (Classes of General Business) Regulations 1977 (UK) SI No 1552, para 3, sch 1 and 2. The UK Law Commission expressed some reservations about adopting this definition of MAT insurance as it includes death or injury to passengers but does not include offshore installations such as oil rigs, nor insurance against financial loss connected with the use or operation of ships, offshore installations or aircraft such as loss of freight on salvage: The Law Commission *Insurance Law — Non-disclosure and Breach of Warranty* HMSO 1980, Cmnd 8064, Law Com No 104, 16.

- The law and practice in this area appeared to be working satisfactorily and were not in need of reform. The MIA (UK) together with subsequent case law contained comprehensive provisions which provide a context of certainty of law and practice.
- In view of London's position as a leading centre for marine and transport insurance in a competitive international market it would be undesirable to disturb this certainty.<sup>28</sup>
- Contracts of marine, aviation and transport insurance are generally effected by 'professionals' whose everyday business dealings involve making and carrying out insurance contracts and who 'operate in a market governed by longstanding and well known rules of law and practice'.<sup>29</sup>

3.26 In Australia, the MIA, the ICA and the common law all govern various aspects of MAT insurance. If part of the rationale for maintaining the MIA as a separate regime rests on the commercial nature of the transactions governed by it, then the same argument may also be advanced for removing aviation and transport insurance from the ICA and into the MIA.

The insurance of aviation risks has historically developed from the marine market as a distinct class of business. Much of the terminology and practices of the aviation market derive from the marine market and therefore need to be understood by reference to the equivalent terminology and practices of the marine market although there are differences between them, not least, that the marine market is governed by the codifying statute, the Marine Insurance Act 1906, whereas there is no similar statute governing the non-marine market which includes aviation.<sup>30</sup>

3.27 In the Discussion Paper, the Commission noted that introducing a regime covering all commercial MAT insurance may have particular advantages in relation to cargo insurance where transport is commonly multimodal and that, in practice, the same person at the same desk can be writing all forms of MAT insurance, particularly in relation to cargo insurance.<sup>31</sup>

28 Issues of certainty and international competitiveness are discussed in ch 7.

29 The Law Commission *Insurance Law — Non-disclosure and Breach of Warranty* HMSO 1980, Cmnd 8064, Law Comm No 104, 14–15.

30 *Kuwait Airways Corporation v Kuwait Insurance Company SAK* [1999] 1 Lloyd's Rep 803, 809 (Hobhouse LJ). The Commission has heard that the aviation and marine hull insurance markets are 'completely separate' and that aviation hull insurers are 'comfortable' outside the marine market: Insurers *Consultation* Melbourne 6 June 2000; Insurers *Consultation* Melbourne 7 April 2000. In London marine and aviation hull insurance are treated as part of the same market. This is said to be for historical rather than business reasons. There is little connection between the marine and the aviation hull or cargo markets in Norway, France and the US: Insurers *Consultation* Melbourne 6 June 2000.

31 ALRC DP 63 para 2.42. In its submission the Maritime Law Association of Australia and New Zealand (MLAANZ) confirmed that as a matter of practice air cargo insurance is written on marine terms: MLAANZ *Submission 12*. Therefore, a MAT regime may reflect market practice better than the current combination of separate MIA and ICA regimes.

3.28 Support was expressed in submissions and consultations for the idea that an MAT regime should be examined, at least to cover all cargo insurance.<sup>32</sup> The Insurance Council of Australia stated that, from the perspective of cargo insurance, there ‘seems no reason why sea, air and inland transits should not be covered by the same legislation’ and confirmed that it is common practice for these transits to be covered under the same policy.<sup>33</sup> An insurer who strongly supported the creation of MAT legislation based on a reformed MIA stated

The MIA is concerned only with a maritime adventure which is effectively confined to insurance of vessels themselves, maritime liabilities, freight and cargo transits by sea, and land transits where a sea transit is also contemplated. Marine insurance [practice] today has a much wider scope and on a worldwide scale includes transit by air and, in many places, Australia included, inland transit of cargo. There is therefore a supportable case for extending the MIA to cover MAT (Marine Aviation and Transit).<sup>34</sup>

3.29 Others specifically expressed support for bringing aviation cargo insurance within the MIA.<sup>35</sup> Including aviation cargo insurance within the MIA would not cause any practical problems for the insurance industry as most international cargo policies cover both air and sea carriage. The fact that the MIA does not cover aviation cargo has been identified by insurers as problematic given that the parties to international cargo insurance contracts generally intend that all their cargo insurance be subject to the same law and practice.<sup>36</sup> An MAT regime would eliminate the existing uncertainties that may be caused by the overlapping coverage of the MIA and the ICA in respect of mixed risks or the uncertainty as to which regime applies (see chapter 8).

3.30 It is clear that at present the law in the area of transport insurance is split in Australia but that practice does not conform to this split perfectly. The Australian approach is of necessity different from that in the UK. Although air and other transport insurance may be descended from marine insurance, their present forms and law show significant divergence from their marine heritage.

3.31 The argument that cargo insurance covering all modes of transport should be governed by a single insurance law regime raises the prospect that other forms of insurance associated with transport could also be governed by the same regime. Alternatively, there may well be good reasons why aviation hull insurance and

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32 P Grieve *Submission 6*; Insurance Council of Australia *Submission 11*. Justice Carruthers submitted that no case has been made out for an MAT regime: K Carruthers *Submission 9*.

33 Insurance Council of Australia *Submission 11*. However this practice may create uncertainty in relation to the respective coverage of the MIA and ICA: see ch 8.

34 P Grieve *Submission 6*. In its submission MLAANZ confirmed that as a matter of practice air cargo insurance is written on marine terms: MLAANZ *Submission 12*. Therefore, an MAT regime may reflect market practice better than the current MIA and ICA regime.

35 *Advisory Committee meeting* 18 December 2000.

36 *Ibid.*

marine hull insurance should be handled differently. Similar questions arise in relation to liability insurance. The insurance of trucks (in other words, 'hull' insurance for land transport) is already covered by other legislative schemes.

3.32 An inquiry of the scope needed to fully review the possibility of instituting a comprehensive MAT scheme is beyond the Commission's present terms of reference, and a much broader inquiry than the Commission has been able to achieve would be needed. However, consideration should be given to replacing the MIA with legislation covering all or some aspects of marine, aviation and other transport insurance, which have much in common, not least the way in which the market deals with them.

3.33 Such a change to existing Australian insurance legislation would involve the repeal or extensive amendment of both the MIA and ICA. As with the idea of subsuming marine insurance within the ICA, the interest of the marine insurance industry in having a regime consistent with international practice also militates against creating a general MAT regime at present without any more widespread call for such a regime. However, combining international air cargo insurance with marine insurance could well be much more acceptable to the relevant international markets. However, removing a significant portion of insurance from the ICA to the MIA in Australia needs to be carefully considered. Bearing in mind the terms of reference, the Commission considered that it was not a matter that could or should be dealt with in depth by this inquiry. It is appropriate, however, to note that the concept has its supporters and may well be ripe for more detailed consideration in the future. It is one of a number of areas in which the Commission would encourage further consideration and the monitoring international developments.

3.34 Consultations have indicated that the incorporation of air cargo insurance (or international air cargo insurance) into the MIA would be welcomed by the Australian marine insurance industry although this does not extend to other aspects of aviation insurance, which is currently covered by the ICA. The Commission has been told that this expansion of the MIA's coverage would be uncontroversial.<sup>37</sup> The Commission anticipates that this may well be so and sees the logical force of such a move. However, the Commission has not been able to undertake a review of the depth that would allow it to be confident about making such a recommendation at this stage. However, the Commission would also encourage further close consideration of this option.

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37 M Hill *Correspondence* 19 April 2001.



## Reform of the *Marine Insurance Act*

3.35 Possible reforms to the MIA vary from radical reform of substantive provisions to modernisation of the MIA with few substantive changes. In the Discussion Paper the Commission asked whether changes to the law of marine insurance should be restricted to selected areas only or alternatively, should the MIA simply be updated to reflect modern industry practices without changing significantly the law or practice of marine insurance.

3.36 Insurers, lawyers, judges and fishing industry organisations expressed overall satisfaction with the current regime, while focusing their attention on specific areas of the MIA that may require reform. These areas include those that are the major focus of this report. The Commission found broad support for reform in most of these areas, aimed at making the MIA fairer and more equitable and at removing uncertainties in the practical application of the law. For example, the Insurance Council of Australia stated that it recognised the need for reform of certain important precepts contained within the Act, such as those relating to warranties and the duty of disclosure,<sup>38</sup> and the National Bulk Commodities Group agreed that some aspects of the MIA are clearly in need of reform.<sup>39</sup> Submissions sounded consistent notes of caution and stressed the need for measured reform. The Maritime Law Association of Australia and New Zealand (MLAANZ) argued that any changes to the law should be

restricted to those areas which have been subject to significant criticism, namely the scope of the duty of disclosure, the remedy for breach of the duty of disclosure, the nature and operation of the doctrine of warranties and the remedy for breach of warranty.<sup>40</sup>

3.37 Only one submission rejected reform of the MIA outright. The Law Council of Australia stated that reform of the MIA is ‘premature’.

The law of marine insurance is a highly technical area, and the law in turn is simply one part of the environment in which the Australian marine insurance market operates. The consequences for Australians involved in international trade and business, and for the Australian marine insurance market, of any law reform is potentially unpredictable, and the Law Council does not consider that change is appropriate at this time.<sup>41</sup>

3.38 The Commission found no significant support for comprehensive modernisation of the language of the MIA. Insurers and lawyers emphasised the

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38 Insurance Council of Australia *Submission 11*.

39 National Bulk Commodities Group *Submission 14*.

40 MLAANZ *Submission 12*. See also Law Society of WA *Submission 7*; K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*.

41 Law Council of Australia *Submission 10*.

utility of the MIA, particularly the definitions contained in the Act, in codifying the law and as a guide to interpreting contracts.<sup>42</sup> MLAANZ stated that

[t]he result of minor tinkering with language would be increased uncertainty for all parties concerned and a consequent increase in litigation and therefore insurance premiums.<sup>43</sup>

3.39 Similarly, the Law Society of Western Australia stated that the MIA ‘can be “modernised” without any wholesale or radical amendments’.<sup>44</sup>

3.40 The approach to reform taken by the Commission is generally consistent with that suggested in the submissions. The overall effect of the recommendations of this report is to retain the MIA in its familiar structure but incorporating a series of substantive amendments in important areas.

3.41 The Commission has made no systematic attempt to modernise the structure or the language of the MIA. There are a number of drafting changes but these have been approached with some reserve and are generally limited to provisions where there has been substantive change as well. For example, while it is recommended that the Second Schedule (the Lloyd’s SG Policy wording) be repealed, it is recommended that the important and well understood terms and concepts defined in the Rules for Construction found at the end of that wording be reincorporated into the Act so the body of law based on them remains reflected in the amended MIA.

## **International marine insurance law**

3.42 The terms of reference required the Commission to consider the desirability of having a regime consistent with international practice in the marine insurance industry. In approaching this inquiry the Commission has recognised that issues related to the international marine insurance market may place limits on the desirable scope of reform (see chapter 7).

## **Influence of United Kingdom law and practice**

3.43 The marine insurance market, long dominated by Lloyd’s and London, is still strongly influenced by UK law and practice.<sup>45</sup> While there are other important

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42 For example, in relation to partial and total loss and salvage charges: Insurers, brokers and legal practitioners *Consultation* Perth 29 March 2000; Insurers *Consultation* Melbourne 7 April 2000; Legal practitioners *Consultation* Sydney 13 April 2000.

43 MLAANZ *Submission 12*.

44 Law Society of WA *Submission 7*.

45 ‘London’s Maritime Services Make US\$1,450 million’ (June 2000) *Asia Insurance Review* 48.

insurance law regimes, such as the French and Scandinavian regimes,<sup>46</sup> the London market and United Kingdom law have been the leading influence in the global marine insurance market. Australia has a close association with marine insurance law and practice in the United Kingdom and many other common law jurisdictions, including New Zealand, Canada, Singapore, Malaysia, Hong Kong and India, have legislation derived from the MIA (UK).<sup>47</sup>

3.44 The prices set by an insurer in London are influential on competing insurers in other countries and, through the International Underwriters Association and the Institute Clauses,<sup>48</sup> London sets the terms and conditions for policies that are used all around the world. These clauses form the basis of most marine insurance policies underwritten in Australia, and are widely used, not only in common law countries whose legislation is based on the MIA (UK), but also in the USA, Japan and China. Other model cargo clauses are not widely used.

3.45 Until quite recently, the law of marine insurance in the United Kingdom was not expected to be the subject of any major push for reform. The United Kingdom itself had decided against recommending changes to the existing law of marine insurance.<sup>49</sup> In 1980, the UK Law Commission stated that the MIA (UK) provided certainty of law and practice and that, in view of London's position as a leading centre for marine and transport insurance in a competitive international market, it would be undesirable to disturb this certainty. However, in 2000 a wide-ranging review of insurance law and practice was commenced in London. It is too early to ascertain what, if any, reforms might be recommended by that review.<sup>50</sup>

3.46 Any significant divergence in Australia from UK law and practice may create a real or perceived risk of uncertainty for insureds, and proposals for change to the MIA have to take account of possible flow-on effects on existing clauses and their interpretation. Submissions and consultations confirmed that maintaining a high level of consistency with UK law, and international practices based on it, was seen as necessary if insurers are to compete in the international marine insurance market.<sup>51</sup>

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46 A survey of European civil code jurisdictions concluded that, except for the Scandinavian countries, they do not share any 'common marine insurance system', their laws differing significantly both in material solutions and in approach: T-L Wilhelmsen 'The Marine Insurance System in Civil Law Countries — Status and Problems' *Paper Marine Insurance Symposium Oslo 4–6 June 1998*.

47 See para 7.4.

48 Although the Institute of London Underwriters has been subsumed by the International Underwriters Association, the clauses discussed in this report are still known as the 'Institute clauses'.

49 UK Law Commission *Insurance Law — Non-disclosure and Breach of Warranty* Law Comm No 104 (1980).

50 See para 7.31–7.37.

51 Insurers and legal practitioners *Consultation* Sydney 15 May 2000; P Grieve *Submission 6*; Law Society of WA *Submission 7*; Insurance Council of Australia *Submission 11*.

3.47 These concerns have significantly influenced the Commission's approach to reform of the MIA. Leaving aside the possible commercial implications of divergence from UK law and practice, there is a benefit in retaining links with overseas case law developments, especially in view of the many marine insurance cases that come to trial in the UK as compared to Australia.<sup>52</sup>

3.48 However, the Commission's research has shown that it is manifestly wrong to assume that marine insurance law and practice, even within the common law world, is uniform or standardised. There are major differences in the statutes themselves and in the judicial interpretation of them. These differences are discussed throughout the report.

3.49 The area of warranties is a prime example. There has been significant statutory amendment in New Zealand, and in Canada and the USA the courts have departed substantially from the conventional Anglo-Australian view of warranties and the ability of insureds to remedy breaches prior to a loss occurring.<sup>53</sup>

3.50 Accordingly, it would be inappropriate to treat the MIA with excessive reverence. Other jurisdictions have seen fit to make major changes to the law. Although it is clear that international consistency was often considered when these changes were made, that was obviously not ultimately seen to be the determinative factor: getting the law right was.

3.51 The Commission has recommended changes to the MIA where this has been found to be necessary or desirable. Where possible, reform has built incrementally upon the existing language of the Act and the common law that has developed in Australia and overseas during the 20th century. For example, the Commission has recommended significant reform to the law relating to warranties while retaining basic concepts such as the 'proximate cause' and loss 'attributable' to unseaworthiness.<sup>54</sup> In other cases the Commission has drawn upon the wording of the ICA or other statutes to provide some consistency with concepts familiar in other contexts.

### **International harmonisation**

3.52 The broad interest in international harmonisation of marine insurance law has been an influence in the approach to reform taken by the Commission. For example, the desire not to place Australian law outside the mainstream on

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52 Justice Carruthers observes that, although judgments of the House of Lords and the Privy Council are no longer binding upon Australian courts, they have a 'peculiarly high persuasive value': K Carruthers *Submission 9*, citing *Viro v The Queen* (1978) 141 CLR 88.

53 See para 9.38–9.43.

54 See para 9.141, 9.150–9.152, 9.172 and 9.175, and rec 11 and 15.

international marine insurance law has been a factor in rejecting some elements of the ICA as a model for reform of the MIA.

3.53 Throughout this report the Commission has examined not only the existing law in Australia, the United Kingdom and other common law countries but also, where relevant, the law in selected civil code countries. In this context, the Commission agrees with the Law Council's submission that, although not easily done

reform efforts should promote unification and harmonisation internationally and facilitate trade through use of recognised principles.<sup>55</sup>

3.54 Where the Commission has concluded there is a need to reform the MIA, diverging to some extent from UK law as represented by the MIA (UK), the options favoured by the Commission have in some respects been significantly influenced by approaches taken in civil code countries, notably Norway. In particular, this influence can be seen in the recommendations concerning reform of the remedies for breach of the duty of disclosure (see paragraphs 10.66–10.68 and recommendations 22–25) and the implied warranty of seaworthiness (paragraph 9.145–9.149 and recommendations 10–12). In some respects, notably in recommending that insurers no longer be able to avoid all liability by reason of a breach of warranty by the insured unless the breach was causative of the loss, the Commission's recommendation, while diverging from UK law, would bring Australian law closer to an international civil law mainstream.<sup>56</sup>

#### ***Review by the Comité Maritime International***

3.55 The major current effort aimed at the international harmonisation of marine insurance law and practice is that of the Comité Maritime International (CMI),<sup>57</sup> which is currently examining the possibility of harmonisation of marine insurance law. The work of the CMI is described in more detail in chapter 7.

3.56 A recent conference resolved to continue the CMI's evaluation of the national laws of marine insurance, with the aim of identifying issues of marine insurance that are worthy and capable of harmonisation and those that ought best be left to national interpretation. The CMI's views on the desirable direction of reform are now not expected until its next conference in 2004.

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55 Law Council of Australia *Submission 10*.

56 To the extent that such a mainstream can fairly be said to exist. As noted in para 7.17–7.22, the public and private legislation relating to marine insurance in civil code countries produce distinct regimes.

57 The CMI is a non-governmental international organisation, the object of which is to contribute to the 'unification of maritime law in all its aspects': <http://www.comitemaritime.org> (4 May 1999).

3.57 The Attorney-General extended the reporting date for the Commission's present inquiry from 31 December 2000 to 30 April 2001 in order to allow the Commission to take further account of the CMI's deliberations. The Commission has carefully monitored the progress of the CMI's work and Ian Davis, the lead Commissioner, attended and spoke at the CMI's Singapore Conference in February 2001. However, given the timeframe of the CMI's work, the Commission's recommendations on reform of the MIA had to be made in the absence of any concluded CMI views on the desirable and feasible direction and scope of reform.

3.58 The CMI's work to date has served to highlight the diversity of international insurance law and considerable barriers to harmonisation. The civil law regimes, while sharing many common concepts, such as alteration of risk, take disparate approaches on the key issues. The Commission's impression is that, at least in the areas studied in detail by the CMI working group, the only legal regimes that substantially share the same law are those regimes based on the MIA (UK) that retain close links with the English common law.<sup>58</sup>

3.59 In theory, therefore, the MIA (UK) regime appears the only obvious starting point for harmonisation. In practice, its deficiencies and the fact that many MIA concepts are entirely foreign to the law of all the civil code countries makes broader harmonisation based on the MIA (UK) unlikely.

3.60 While it is not entirely clear what the final product of the CMI's review will be (see paragraph 7.24–7.30 below), it does appear certain that there is no prospect of the CMI promoting an international convention on marine insurance. A model law is also unlikely. Model clauses or rules of practice are much more likely. Such clauses featured in an earlier attempt at harmonisation under the auspices of the United Nations Conference on Trade and Development (UNCTAD).<sup>59</sup> Any new model clauses would not be binding on the parties to contracts of marine insurance and it is uncertain whether any such CMI initiatives would come to have any significant influence on marine insurance practice. Only time will tell.

3.61 The timeframe of the CMI's work means that Australia need not and should not wait for the outcome before proceeding with its own reforms. In any case, the Commission's recommendations for reform of the MIA do not detract from the moves towards harmonisation of marine insurance law. These measured reforms in no way place Australian law outside any international mainstream, to the extent that such a mainstream may be discerned.

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58 That is, the United Kingdom, Australia, New Zealand, Canada, Singapore, Malaysia, Hong Kong and India (see para 7.4). However, even as between these jurisdictions there are some significant differences in both the wording and interpretation of marine insurance Acts by the courts and in other legislation that may affect its operation (see para 7.4–7.16).

59 United Nations Conference on Trade and Development *Model Clauses on Marine Hull and Cargo Insurance* UN New York 1989.

3.62 In some important respects the recommended reforms may even contribute towards harmonisation, for example by reforming the law relating to warranties. Further, implementing the reforms recommended by the Commission constitutes a valuable opportunity for Australia to influence reform elsewhere, at least in the other common law jurisdictions.

## **Reform and international competitiveness**

3.63 The terms of reference required the Commission to consider whether any change to the Act might result in a competitive disadvantage for the Australian insurance industry.<sup>60</sup>

3.64 There are two important ways in which it is said changes to the MIA might result in a competitive disadvantage for Australian insurers. Firstly, premiums required by Australian insurers might rise in response to any actual or perceived increase in the risks insured under an amended MIA,<sup>61</sup> making it more attractive for prospective insured parties, either Australian or overseas, to insure in other markets. Secondly, overseas reinsurers of Australian risks might be hesitant to accept Australian risks or might be keen to devise special rates or charge additional premium to accept Australian risks, and Australian insureds and insurers might find themselves unable to insure, co-insure or reinsure on overseas markets, or required to do so on adverse terms.

3.65 Some submissions expressed concerns about possible increases in insurance and reinsurance premiums as a result of reform. For example, the National Bulk Commodities Group stated that before it could unequivocally support reforms to the law relating to warranties it would need to be satisfied that any increase in premiums would be more than offset by the benefits flowing from the changes.<sup>62</sup> The Law Council of Australia expressed its concern that

reinsurance premiums could rise if it becomes difficult to predict how the regime underpinning the contract of insurance will affect coverage, enforceability of policy exceptions, and exercise of rights of subrogation.<sup>63</sup>

3.66 In the Discussion Paper the Commission asked what, if any, changes to the MIA had the potential to place Australian insurers at a competitive disadvantage internationally. In response, submissions stressed the need to retain the flexibility and certainty of the current regime.<sup>64</sup>

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60 Terms of reference — Review of the Marine Insurance Act 1909 (Cth), see p 3.

61 If, for example, the MIA were to be amended as recommended by the Commission to restrict existing rights of insurers to avoid liability for breach of warranty or non-disclosure.

62 National Bulk Commodities Group *Submission 14*.

63 Law Council of Australia *Submission 10*.

64 P Grieve *Submission 6*; Law Society of WA *Submission 7*; Insurance Council of Australia *Submission 11*.

Above all, any reform ... must ensure flexibility, such that it will not inhibit the placing of marine insurance in Australia or make it more difficult or expensive for Australian marine insurers to obtain the reinsurance cover they need.<sup>65</sup>

3.67 The Law Council of Australia was insistent that before any change to the MIA is made the consequences for international trade should be thoroughly analysed.

The Law Council recommends that efforts be made to assess the likely impact of reform on industry, so that the Commission's report takes into account any impact of proposed reform on the competitiveness of the Australian marine insurance industry.<sup>66</sup>

3.68 While the Law Council cautioned that Australia does not have the 'opportunity to lead international reform by example', the Insurance Council of Australia noted that Australia's minor position in the world marine insurance market should not prevent the development of its marine insurance law to keep pace with contemporary practice and needs.<sup>67</sup>

3.69 The main means by which the Commission has sought to assess the likely impact on premium levels and international competitiveness of the proposed reforms to the MIA has been by comparison with the experience of the markets following the commencement of the ICA in 1986 and the transfer of pleasure craft insurance to the ICA in 1998. The Commission was interested in any reliable statistics that would enable a comparison of premium levels (or other important financial indicators) in the periods before and immediately after the 1986 and 1998 changes. In this context, relevant statistics were sought from the Insurance Council of Australia and the Australian Prudential Regulatory Authority (APRA). APRA statistics on premium revenue and claims expense for general insurance in the 1982–1988 period are presented in chapter 6 (see Table 3). The Commission was advised that more detailed statistics were not available and it has proved impossible to obtain useful empirical information elsewhere. Questions in the Discussion Paper about relevant market experience did not meet with any significant response in submissions.

3.70 However, the Commission's firm impression from its extensive consultations on this point is that the enactment of the ICA did not lead to any significant disruption in the Australian insurance market. Broadly speaking, insurers have indicated to the Commission that premiums rose when the ICA was enacted in anticipation of higher claims but that premiums soon stabilised at levels not significantly higher than pre-ICA levels. Similarly, when pleasure craft were bought under the ICA the insurance market in Australia and London adjusted

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65 Insurance Council of Australia *Submission 11*.

66 Law Council of Australia *Submission 10*.

67 Law Council of Australia *Submission 10*; Insurance Council of Australia *Submission 11*. For information about the place of Australian marine insurance within the international market see ch 6.



quickly and with little fluctuation.<sup>68</sup> The Commission is confident that if the changes in 1986 and 1998 had been accompanied by major problems, they would have been well documented and the Commission alerted to them.

3.71 In any event, radical reform to marine insurance law along the lines enacted by the ICA would certainly be familiar (even if unwelcome) to Australian insurers. Overseas insurers who write, co-insure or reinsure Australian non-marine risks are already dealing with them as well, although they may not be aware of that. As the Commission has pointed out to representatives of the London insurance market, the abolition of the requirement that the insured have an insurable interest, which was the area of possible reform that encountered most resistance in the current inquiry, is not a novel concept in Australia: it occurred over 15 years ago in relation to non-marine general insurance without major disruption to the Australian market.

3.72 Given that the changes to the law of marine insurance recommended by the Commission are much less wide-ranging than the 1986 enactment of the ICA, the Commission remains confident that, while the immediate effect of changes to the MIA might be to increase premiums in the short term, competitive pressures should prevent a long term rise.<sup>69</sup>

3.73 Concerns about the possible competitive disadvantage of changes to the MIA are hard to assess. However, the law of marine insurance differs substantially between national jurisdictions. The London market reinsures risks from many parts of the world, including risks underwritten in and subject to the laws of civil code jurisdictions which have different arrangements in relation to, for example, warranties and the duty of disclosure. Market practices appear to be sufficiently flexible to adapt rates and terms to take account of an amended Australian MIA.

3.74 In any event, changes to the substantive law of marine insurance that favour the insured could bring more business to Australian brokers and insurers. Further, existing uncertainties in Australian law, notably those concerning the extent of coverage of the MIA and ICA, may already place Australian marine insurers at a competitive disadvantage and would be addressed to some extent by the Commission's recommended changes.

3.75 Overall, the reforms recommended by the Commission are intended to reduce legal uncertainty, retain the flexibility of the MIA regime, preserve the MIA in a recognisable form, and maintain historical links with UK law and practice where departure from them is not warranted.

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68 Insurers and legal practitioners *Consultation* Sydney 15 May 2000.

69 Insurers, brokers and legal practitioners *Consultation* Perth 29 March 2000.

3.76 Interested observers overseas will, it is expected, readily understand the reforms and adjust appropriately. It will, however, be advisable for the Australian industry to actively inform overseas markets about the new regime. MLAANZ states that the impact in Australian and overseas markets of changes to the MIA may be lessened by providing sufficient information in advance and, in particular, ensuring that overseas markets are sufficiently educated about the changes.<sup>70</sup>

3.77 Few have argued that there should be no change to the MIA. It is clear that the international marine insurance market already tolerates a wide margin of divergence from a standard marine insurance contract, if one ever existed. There is no need to back away from change simply on the basis of an attachment to a perceived UK norm. Where appropriate, Australia should not be afraid to take a lead on reform of marine insurance law, where change is seen to be right. The issue is one of balance.

3.78 The Commission has concluded that the measured reforms it recommends will not result in any competitive disadvantage for the Australian insurance industry.

## **Competition policy**

3.79 The terms of reference directed the Commission to consider the competition policy implications of the MIA as part of this review. Issues concerning reform of the MIA and international competitiveness have been discussed in detail above. The terms of reference also expressly required the Commission to take national competition policy into account.<sup>71</sup>

3.80 Chapter 4 of the Discussion Paper discussed in some detail the competition policy implications of the MIA and observed that the question whether there are restrictions on competition in the marine insurance industry due to the MIA involves consideration of the barriers to entering the industry, constraints on the decision making of businesses, compliance requirements of the legislation and the benefits that may accrue to one type of business or consumer over another.

3.81 The Commission's initial examination of this issue did not identify any significant competition policy implications, either of the existing MIA or in relation to the proposed reforms. Generally, the MIA does not constrain the practice of marine insurance by imposing requirements on insurers or insured parties and most of the provisions of the MIA may be varied by contract. The MIA is not regulatory legislation. There are no legislative requirements placed on

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<sup>70</sup> MLAANZ *Submission 12*.

<sup>71</sup> Australia's national competition policy is based on an agreement between the Commonwealth, State and Territory governments, and complementary legislation, which adopt a national co-ordinated approach to reform: see ALRC DP 63 para 4.2–4.5.

insurers of marine risks beyond those required of insurers of other types of general insurance.

3.82 In the Discussion Paper the Commission asked for comments on whether the MIA restricts competition in the Australian marine insurance industry in any way and whether its operation affects competition in other Australian industries. The Commission sought specific comment from the Australian Competition and Consumer Commission and the National Competition Council.

3.83 In response, the Commission received no submissions or other comments suggesting the existence of significant competition policy issues. For example, the Law Society of Western Australia stated that the MIA does not restrict competition and encourages competition as a result of its flexible approach.<sup>72</sup> The Commission does not seek to reduce that overall flexibility.

3.84 The Insurance Council of Australia stated that it would be of ‘great concern if the MIA were challenged by another country before the WTO as constituting a barrier to trade’.<sup>73</sup> None of the reforms to the MIA proposed by the Commission are likely to lead to such challenge. In particular, the Commission is not proposing that reform restrict the right of parties to choose a particular body of law as the governing law of the contract.

## **Effects in other areas**

3.85 The Commission was required by its terms of reference to take into account the effects on the environment, welfare and equity, occupational health and safety, economic and regional development, consumer interests, the competitiveness of business, including small business, and efficient resource allocation with the aim of reducing compliance costs and the paperwork burden on small business.<sup>74</sup>

3.86 In the Discussion Paper the Commission sought information on the impact of the MIA on the environmental and safety concerns and any potentially adverse effects changes to the MIA could have in the other areas identified by the terms of reference.<sup>75</sup> Submissions responding to this issue suggested that the MIA, either in its present or amended form, was unlikely to have any significant implications in these areas.<sup>76</sup>

3.87 As discussed in chapter 9, the Commission concluded that the implied warranties of seaworthiness and legality required separate consideration in part

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72 Law Society of WA *Submission 7*.

73 Law Council of Australia *Submission 10*.

74 Terms of reference — Review of the Marine Insurance Act 1909 (Cth), see p 3.

75 ALRC DP 63 para 4.15–4.20.

76 P Grieve *Submission 6*; Insurance Council of Australia *Submission 11*.

because of their importance in promoting maritime safety. The Commission's recommended reforms largely maintain the deterrent effect of the consequences of breach of the implied warranties (see paragraphs 9.188–9.207).

## 4. Overview of the *Marine Insurance Act*

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### Background

4.1 This chapter is a review of the *Marine Insurance Act 1909* (MIA) in broad terms, describing its structure and the areas it covers (and omits to cover), and identifying those areas that are examined in greater detail later in the report.<sup>77</sup>

4.2 The MIA came into effect on 1 July 1910 and, with only one difference in substance, was a virtually identical replica of the United Kingdom parent legislation. The first six sections of the MIA are either preliminary provisions or reflect provisions found at the end of the MIA (UK), with the result that almost all the substantive provisions of the Australian Act are numbered six greater than their UK equivalents.

4.3 The MIA has been amended only twice. The first occasion was in 1966 to reflect the introduction of decimal currency into Australia.<sup>78</sup> The amendment was particularly trivial: it changed ‘per cent’ to ‘per centum’ and removed the words ‘per pound’ from the note at the end of the wording of the Lloyd’s SG policy, which is the Second Schedule to the MIA. The second amendment was the repeal of the index contained in s 2, apparently to reflect more contemporary drafting techniques in which the index to an Act is not enacted as a substantive provision.<sup>79</sup>

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<sup>77</sup> The MIA uses the term ‘assured’ to describe the insured party. That term has been preserved in the draft Bill and explanatory memorandum in Appendices C and D. However, this report uses the more modern term ‘insured’.

<sup>78</sup> See *Statute Law Revision (Decimal Currency) Act 1966* (Cth).

<sup>79</sup> See *Statute Law Revision Act 1973* (Cth) s 9(1) and 10.

Amendments made to the UK legislation in 1959 or to other similar legislation elsewhere have never been taken up in the Australian MIA.

4.4 The MIA is said to have codified the law of marine insurance when enacted. That is only true in part: s 4 specifically preserves the rules of the common law ‘including the law merchant’ except to the extent that it is inconsistent with express provisions of the Act. Thus, the developing common law continues to play a role in stating the law of marine insurance both in interpreting the legislation and in resolving issues on which the legislation is silent.

4.5 In many places the MIA specifically preserves the parties’ ability to agree on terms other than those set out in the legislation.<sup>80</sup> This often has the effect of permitting contracts which are more favourable to the insured because many standard terms offer cover in which the insurer relinquishes or modifies rights that it otherwise has under the Act. In this way, the MIA can be seen as the framework within which the parties have a fair degree of flexibility and freedom to contract, and each party (usually the insurer) is at liberty to waive or change its rights. However, the mere fact that insurers may not rely except in extreme cases on some of the harsher provisions of the Act which operate in their favour is no reason to leave the law unchanged where it is seen to operate unfairly.

## **Defining marine insurance**

4.6 Sections 7–10 of the MIA seek to define marine insurance in a series of cascading definitions. Marine insurance is said in s 7 to be a contract ‘whereby the insurer undertakes to indemnify the assured, in manner and to the extent thereby agreed, against marine losses, that is to say, the losses incident to marine adventure’. This expression incorporates a number of terms which are defined or described in the following sections. A ‘marine adventure’ is defined in s 9(2) to be where

- any ship, goods or other movables are exposed to maritime perils
- the earning of freight, passage, money, commission, profit or other pecuniary benefit, or the security for any advances or loans, or disbursements are endangered by the exposure of the insured property to maritime perils, or
- any liability to a third party may be incurred by the owner of, or other person interested in or responsible for, the insured property by reason of maritime perils.

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<sup>80</sup> See, eg, s 8, 15, 21, 22, 30, 33, 35, 38, 48, 51, 56, 58–59, 61–62, 66, 68, 71–72, 74–77, 79, 80, 82–83 and 93.

4.7 A marine adventure thus has a tripartite definition and refers to the exposure to risk of the insured property itself, of money that may be earned from that property or the adventure, and to liability that may arise to a third party if that property is lost or damaged.

4.8 An essential element throughout is that of maritime perils. These are defined in s 9(2)(c) to be the perils

consequent on, or incidental to, the navigation of the sea, that is to say, perils of the seas, fire, war perils, pirates, rovers, thieves, captures, seizures, restraints, and detentions of princes and peoples, jettisons, barratry and any other perils either of the like kind, or which may be designated by the policy.

4.9 This definition is not exhaustive. It allows other similar maritime perils to be included and allows the policy to define other perils, which, at least on one reading of this paragraph, do not have to be limited by the range of perils specified in s 9(2). Even so, the perils must be consequent on, or incidental to, the navigation of the sea. The 'sea', however, is not defined in this legislation.<sup>81</sup>

4.10 Nonetheless, a contract of marine insurance may deal with some land risks. Section 8(1) permits the contract, either by its express terms or by usage of trade, to be extended to protect the assured against losses on inland waters or on any land risk 'which may be incidental to any sea voyage'. It is clear, however, that the sea voyage must be the primary risk insured. If the policy does not make it clear that the maritime risk is predominant and not merely one of many risks, the contract will not be one of marine insurance<sup>82</sup> and will, therefore, be governed by the ICA.

4.11 The scope of maritime perils and, therefore, of marine insurance, is a critical threshold question regarding the application of the MIA to any given contract of insurance. It is hedged about by great uncertainty in relation to mixed risks, foreshore activities of various sorts, and offshore installations. This threshold question is perhaps more important in Australia than elsewhere in the common law world as the existence of the ICA means that if the policy is not one of marine insurance as defined by the MIA, it will be covered by the ICA and a significantly different regime will prevail. In other common law countries where there is no equivalent of the ICA, a contract of insurance not covered by marine insurance legislation is covered by the common law and the terms of the contract itself. In many cases, the difference between the common law regime and the statutory marine insurance regime is not great, or at least not as great as that between the two

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81 It is, however, defined in (or other relevant definitions are found in) maritime legislation such as the *Navigation Act 1912* (Cth) s 6 and the *Admiralty Act 1988* (Cth), in case law on admiralty legislation and, with a different purpose in mind and to different effect, in protection of the sea and law of the sea legislation. See generally ch 8.

82 *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur (Australia) Ltd* (1986) 160 CLR 226.

Australian Acts, and determining the demarcation between marine and non-marine insurance is not as critical.

### **Insurable interest required**<sup>83</sup>

4.12 Sections 10–21 of the MIA deal with a central issue, that of insurable interest. The requirement for an insurable interest has been abolished in relation to contracts governed by the ICA,<sup>84</sup> under which the insured need only suffer a pecuniary or economic loss in order to claim.<sup>85</sup> However, a contract of marine insurance is deemed to be a gaming or wagering contract, and therefore void, unless the insured party has an insurable interest in the insured property at the time of loss. Although the insured does not need to have such interest when the insurance is effected, it must have the expectation of acquiring one.<sup>86</sup>

4.13 The insured has an insurable interest if it is interested in a marine adventure: s 11(1). Section 11(2) specifies that a person is ‘interested’ in a marine adventure where he or she stands in

any legal or equitable relation to the adventure, or to any insurable property at risk therein, in consequence of which he may benefit by the safety or due arrival of insurable property, or may be prejudiced by its loss, or by damage thereto, or by the detention thereof, or may incur liability in respect thereof.

4.14 In essence, the insured must be exposed to the risk of suffering prejudice if the insured property is lost, damaged or detained. That prejudice would presumably be financial (or pecuniary or economic, to use the words of ICA s 17) or the exposure to liability to a third party.

4.15 The MIA goes on to specify a number of examples of insurable interests but these are not exhaustive. A defeasible, contingent or partial interest is insurable.<sup>87</sup> An insurer may reinsure its interest in a contract of marine insurance and has an insurable interest in doing so, though the original assured does not.<sup>88</sup> The lender of money secured by a (now obsolete) bottomry or respondentia bond has an insurable interest<sup>89</sup> though secured lenders generally are not referred to in the Act. The master and crew of a vessel have an insurable interest in their wages.<sup>90</sup> A person advancing freight has an insurable interest to the extent that the freight is not repayable in the event of loss.<sup>91</sup> Mortgagors and mortgagees have insurable

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**83** This topic is discussed in detail in ch 11.

84 ICA s 16.

85 ICA s 17.

86 MIA s 10 and 12.

87 MIA s 13(1) and 14.

88 MIA s 15.

89 MIA s 16.

90 MIA s 17.

91 MIA s 18.



interests. Both may insure property not only on their own behalf but for the benefit of any other interested person.<sup>92</sup>

4.16 An insurable interest may be assigned. However, an assignment of an insurable interest does not of itself transfer any rights under the contract of insurance unless that is also part of the agreement.<sup>93</sup> A policy of marine insurance is also assignable unless precluded by its express terms.<sup>94</sup> If the policy and the insurable interest are not transferred at the same time, problems may arise. If the insured loses or disposes of its insured interest before agreeing to assign the policy, any subsequent purported assignment of the policy is inoperative (although, it seems, the actual assignment can occur at a later time).<sup>95</sup>

4.17 In s 22, the Act sets out the insurable value of various types of insurable property.

### **Utmost good faith, disclosure and misrepresentation**<sup>96</sup>

4.18 Section 23 sets out the fundamental concept that a contract of marine insurance is one based on ‘utmost good faith’ and permits a party to avoid the contract if the other does not observe that utmost good faith. This is discussed at length later in this report.<sup>97</sup> Although in principle bilateral obligations with bilateral rights, the specific manifestations of utmost good faith stipulated by the MIA are visited upon the insured only. Section 24 sets out the insured’s obligation of full disclosure of all material circumstances prior to the conclusion of the contract, which is extended to cover the insured’s agent by s 25. The prohibition against misrepresentation by the insured and its agent during the negotiation of the contract is found in s 26. In the event of a breach of these obligations by the insured, the insurer is given the right to avoid the contract.<sup>98</sup>

4.19 Similarly, if the insured were to show a breach of utmost good faith by an insurer, it would be entitled to avoid the contract. Instances of this are few.<sup>99</sup> This right to avoid the contract is often a remedy without benefit as in most cases the insured would want the contract to remain on foot and to obtain the benefits of indemnity in the event of loss.

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92 MIA s 20.

93 MIA s 21.

94 MIA s 56(1).

95 MIA s 57.

**96 This topic is discussed in detail in ch 10.**

97 See ch 10.

98 MIA s 24(1) and 26(1).

99 But see eg para 10.7–10.8.

4.20 The MIA does not clarify the period of time for which the obligations of good faith extend although the House of Lords has recently clarified this in the UK.<sup>100</sup>

### Documentation<sup>101</sup>

4.21 The MIA deals with a number of documentary matters. Importantly, it distinguishes between a contract of marine insurance and its physical embodiment in a policy. This is made clear by s 27, under which a contract of marine insurance is deemed to be concluded when a proposal is accepted by the insurer even if the policy is not issued until a later time.<sup>102</sup> In order to prove this acceptance, reference may be made to a slip, covering note or other customary memorandum.<sup>103</sup> However, under s 28, a contract of marine insurance is not admissible in evidence *in an action for the recovery of a loss under the contract* unless the contract is embodied in a marine policy that complies with the Act. Thus the contract may exist but be unenforceable if the policy is not issued. It is common for a policy to be issued long after the contract is concluded.

4.22 Section 28 represents the only significant departure in substantive terms between the Australian and original UK Acts. Section 22 of the MIA (UK) omits the words in italics in the preceding paragraph and, therefore, no contract of marine insurance is admissible in a UK court for any purpose if the policy has not been issued. In Australia, it is admissible for any purpose other than a claim under the policy itself. Once the policy is issued, and in the UK stamped, reference can be made to the slip, covering note or memorandum in any legal proceeding.<sup>104</sup> This approach can only be justified on the basis that it preserves stamp duty revenue. It is telling, therefore, that this and certain other documentary requirements were repealed in the United Kingdom by the Finance Act 1959.

4.23 Section 29 sets out what a marine policy must specify: the names of the parties, the subject matter insured, the risks insured against, the sums insured and so on. All of these were repealed in the United Kingdom by the Finance Act 1959 except for the requirement that the name of the insured must be specified. However, the general law of contract and the requirement for reasonable certainty of the terms of a contract would no doubt also come into play in this area.

4.24 Section 32(1) and (2) require the subject matter to be designated with reasonable certainty although the insured's interest need not be. Under s 30, a

100 *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd* [2001] 1 All ER 743.

101 **This topic is discussed in detail in ch 15.**

102 See also *Benson-Brown v HHH Casualty and General Insurance* [2001] WASC 6 17 January 2001 (Wheeler J) para 104.

103 MIA s 27.

104 MIA s 95; MIA (UK) s 89. There have been significant changes in this area in New Zealand. See para 15.37.

marine policy must be signed by or on behalf of each insurer. If the insurer is a corporation, the corporate seal is sufficient but not necessary. Under s 30(2), if there are multiple insurers, each has a distinct contract with the insured unless the policy specifies otherwise. There is no comparable provision relating to policies with more than one insured.

## **Types of policy**<sup>105</sup>

4.25 The Act distinguishes a number of classes of policy. The most important distinction is that between voyage and time policies made in s 31. The names are self-explanatory. This distinction appears to have three purposes: the differentiation of the warranty of seaworthiness found in s 45, the definition of the implied condition as to the commencement of the risk in s 48, and the prohibition of time policies for periods exceeding twelve months in s 31(2). The last of these sections was enacted to preserve stamp duty revenue. It was also repealed in the United Kingdom by the Finance Act 1959 and in New Zealand by the Marine Insurance Amendment Act 1975. There is no equivalent in the Canadian Act.

4.26 A policy may be valued or unvalued: s 33 and 34. Floating policies, in which the insurance is described in general terms but which leave the name of the ship or ships and other particulars to be defined by subsequent declaration, are specifically provided for in s 35. The Act does not make it clear whether open, annual or similar umbrella policies are also valid. This is discussed below: see paragraph 15.47–15.57.

4.27 The Act permits, but does not require, a policy to be in the form of the wording found in the Second Schedule. This is the venerable Lloyd's SG policy whose origins date back to the 17th century. It is omitted from the Canadian and New Zealand legislation. Somewhat surprisingly given its archaic nature, the Commission has been informed that its wording is still used, though very rarely. Its only value today appears to lie in the seventeen Rules for Construction of Policy, which are in effect a series of definitions of terms used in a policy, whether or not in the SG policy form, unless the policy requires otherwise. Although some of these are fairly obvious or unlikely to be referred to often, some of them, notably 'perils of the seas', are phrases often debated in marine insurance claims. Even if there is no value in the retention of the policy wording itself, the definitions may nonetheless retain their value as even apparently superannuated expressions such as 'barratry' still arise for consideration from time to time as the activities they describe have not become extinct.

4.28 Premium need not be specified in the contract of insurance. If it is not, a reasonable premium is payable under s 37.

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<sup>105</sup> Some aspects of this topic are discussed in detail in ch 15.

4.29 The Act specifically contemplates the possibility of double insurance in s 38. If there is double insurance, the insured may claim payment from any insurer as it sees fit (unless the policy otherwise provides) but is not entitled to receive any sum in excess of the amount which indemnifies it for the loss: s 38(2). There is no prohibition on clauses in marine insurance policies limiting these rights, as is found in ICA s 45.

## **Warranties and other contractual obligations**<sup>106</sup>

4.30 One of the most controversial Divisions of the Act is that relating to warranties (s 39–47). The following Division (s 48–55), relating to the voyage and dealing with issues such as delay and deviation, raises similar problems. A warranty is an undertaking by the insured that something shall or shall not be done, that certain conditions will be fulfilled or that a particular state of facts exists or does not exist.<sup>107</sup> It may be express or implied.<sup>108</sup>

4.31 The main controversy lies in the consequences of a breach. A warranty must be exactly complied with, whether or not it is material to the risk. If there is a breach, the insurer is automatically discharged from liability from the date of the breach although without prejudice to any liability that may have been incurred by the insurer before that date.<sup>109</sup> The insurer is not required to elect to be discharged from liability but it may waive the consequences of the breach.<sup>110</sup> There need be no link, causative or otherwise, between the breach and any loss or claim under the policy. The breach cannot be remedied with the result or purpose of putting the policy back on foot before any loss occurs.<sup>111</sup> It matters not if the breach is trivial; the consequences remain the same.

4.32 Furthermore, the Act automatically implies into all contracts of marine insurance two warranties, the warranty of the seaworthiness of the vessel (though the terms of that warranty vary between time policies, voyage policies, and policies on goods) and the warranty of legality.<sup>112</sup> They may be amended by the contract. The Act also specifically interprets the warranty of neutrality and the warranty of good safety, if they are expressed in the policy.<sup>113</sup> The Act specifically negates the existence of any implied warranty as to nationality or change of nationality of an insured vessel.<sup>114</sup>

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**106** This topic is discussed in detail in ch 9.

107 MIA s 39(1).

108 MIA s 39(2).

109 MIA s 39(3).

110 MIA s 40(3).

111 MIA s 40(2).

112 MIA s 45, 46(2), 47.

113 MIA s 42 and 44.

114 MIA s 43.

4.33 Sections 48–55 deal with the voyage and, in particular, changes of voyage or changes of risk that arise after the policy has come into effect. In many respects, their operation and consequences of breaches are similar to those of warranties though they have not attracted the same degree of criticism. For example, an insurer is discharged from liability from the time when any determination to change the insured voyage is manifested, whether or not the vessel had in fact left the course of the voyage contemplated by the policy when the loss occurred.<sup>115</sup> Similarly, the insurer is discharged from liability from the time of any deviation from the voyage contemplated by the policy even if the vessel had regained its route before any loss occurred. In this case, however, the intention to deviate is irrelevant; there must be deviation in fact.<sup>116</sup> The MIA permits ‘reasonable’ delay but again discharges the insurer from liability once the delay becomes unreasonable.<sup>117</sup> Deviation and delay is excused by seven events specified in s 55(1) but, if they cease to operate, the voyage and proper course must be resumed with reasonable despatch.<sup>118</sup>

## Intermediaries

4.34 Sections 58–60 deal expressly with the obligations relating to the payment of premium as between insured, insurer and broker. These have been modified somewhat in New Zealand. In Australia, they may have been to a large extent overridden by the enactment of the *Insurance (Agents and Brokers) Act 1984* (Cth) (IABA), which deals extensively and in detail with the operation of insurance intermediaries and their obligations to the principal parties to the contract. The IABA applies to all contracts of insurance whether covered by the MIA or the ICA although it is expressed not to overrule any existing law unless that is expressed in the IABA or is its necessary intendment.<sup>119</sup> This is to negate the presumption that to the extent of any inconsistency between the IABA and MIA, there would be an implied repeal of s 58–60 of the MIA, though the scope of its effect is not clear.<sup>120</sup> Future changes planned for the law governing financial services may alter this position. These are discussed in detail below in chapter 13.

## Other provisions

4.35 The remainder of the Act (s 61–95) has, with few exceptions, not attracted any interest or commentary either during the Commission’s inquiry or in the literature generally. These provisions deal in greater or less detail with concepts peculiar to marine insurance such as loss and abandonment, the liability for loss

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115 MIA s 51(2).

116 MIA s 52.

117 MIA s 54.

118 MIA s 55(2)

119 IABA s 5.

120 See K Sutton *Insurance Law in Australia* 3rd ed LBC Information Services Sydney 1999, 472–473.

proximately caused by risks insured against, exclusion of liability for wear and tear and lawful misconduct, the concepts of partial loss, total loss and constructive total loss, the measure of indemnity in these various cases, partial losses with specific reference to salvage, general average, particular average and particular charges, and the return of premium in the event of failure of consideration or in the event of the avoidance of the policy.

4.36 Section 84 sets out the effect of a suing and labouring clause, if one appears in the policy. Its effect is supplementary to the contract of insurance itself and the insured may recover from the insurer any expense properly incurred pursuant to this clause over and above any payment by the insurer for a total loss. It is of interest to note that it has been reported in the press that some companies that spent significant amounts of money taking precautions against the Y2K bug are seeking indemnity from their insurers under suing and labouring clauses.<sup>121</sup> These clauses are presumably found in business interruption or similar indemnity policies. Although in every case recovery will depend on the existence and wording of any such clause in the policy, only where the policy is one of marine insurance will the additional effect of MIA s 84 arise (unless the contract has a term to similar effect). There is no equivalent provision in the ICA and accordingly, the right to recover properly incurred expenses over and above payment for total loss will not arise under non-marine policies unless based on an express contractual term.

4.37 The insurer's right of subrogation if it pays for a total or partial loss is specified in s 85. There has been some concern that the rights of the insured and its obligations in relation to the insurer's right to subrogation are not clearly stated and require elaboration. This is dealt with in detail in chapter 12.

4.38 Section 91 specifically contemplates mutual insurance where 'two or more persons' agree to insure each other against marine losses. The obvious example of mutual insurance in marine context is the P&I clubs although none is based in Australia and none of the P&I clubs offer insurance governed by Australian law. As the parties to mutual insurance are for the most part corporations rather than actual persons, it has been said that an amendment may be required here. This is discussed in chapter 15.

4.39 The First Schedule lists certain imperial and state Acts repealed upon the coming into effect of the MIA in 1910. The Second Schedule sets out the Lloyd's SG Policy wording and accompanying Rules for Construction (see paragraph 4.27).

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121 'Companies sue Insurers over Y2K' *The Australian* 26 December 2000.

## 5. The history of marine insurance law

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### **Introduction**

5.1 This chapter briefly sets out a history of marine insurance law: its origins in ancient marine codes and most recent codification in the United Kingdom and Australia, in 1906 and 1909 respectively. This report represents the latest stage in a quarter of a century of review of insurance and maritime law in Australia and this chapter also presents an overview of these related developments.

### **Ancient origins**

5.2 The history of marine insurance and the customs and laws that govern it was until comparatively recently the law of all insurance, and the law of maritime commerce was the law of commerce generally. For centuries, marine insurance was the only form of insurance available.

5.3 Contemporary marine insurance law has evolved from the ancient body of maritime law which developed from various marine codes. These codes derived from the customs of early Egyptians, Phoenicians and Greeks who traded extensively in the Mediterranean Sea. The earliest of these marine codes is thought to be Rhodian law (ca 800 BC). Tribunals were set up around Mediterranean port towns to settle seafaring disputes.<sup>122</sup>

5.4 It has long been speculated that marine insurance, or loss-shifting mechanisms similar to it, date from antiquity. Assiduous research in the 19th century attempted to find Roman roots for marine insurance but the evidence found

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122 Maritime Legal Resources 'History of Admiralty Law' <http://www.marlegal.com/mlhist.html> (2 November 2000).

showed no more than that the ancient Romans had usages that were similar to marine insurance but were not necessarily insurance in a form that would be familiar today.<sup>123</sup> It is no more than surmise, but perhaps a reasonable one, that the ancient Phoenicians used a prototype of marine insurance.<sup>124</sup> The independent contract of insurance probably evolved from marine loans, which were developed by the Babylonians in the 3rd millennium BC. These involved the payment of a 'premium' percentage of interest charged on a loan for the purchase of the goods to be traded. The lender thereby assumed the risk of goods in transit. Marine loans were embraced by the Venetians, Greeks and Romans, and were used and developed throughout the Middle Ages.

### Early Italian and English developments

5.5 In 1227 AD Pope Gregory IX prohibited maritime loans on the grounds of usury. Insurance in itself was not in conflict with canon law, so the loan contract was separated from the undertaking to assume risk, leading to the independent contract of insurance. The first premium-based insurance policies covering sea traffic appear to have been developed in Italy by the Lombards in medieval times.<sup>125</sup> Some commentators suggest that this practice was adopted by the Lombards from Jewish refugees expelled from France in 1182 although it is not clear whether those refugees in fact adopted a practice then in use in northern Italy.<sup>126</sup> As the Lombards extended their interests northwards they came into contact with the merchants in the north of Europe who had formed the Hanseatic League.<sup>127</sup> The members of the Hanseatic League probably also adopted the Lombards' system of marine insurance<sup>128</sup> and other European nations followed.<sup>129</sup>

5.6 For a while marine insurance practice was governed by mercantile custom but this was superseded by the establishment of public offices to regulate these practices. These were in turn formalised into codes or ordinances passed by various commercial city authorities, the earliest recorded being Barcelona in 1434.<sup>130</sup> There

123 C McArthur *The Contract of Marine Insurance* 2nd ed Stevens and Sons London 1890, xix–xx; W Gow *Marine Insurance: A Handbook* 4th ed Macmillan & Co Ltd London 1917, 1–3.

124 H Turner *The Principles of Marine Insurance* Stone and Cox Ltd London 1938[?] 7.

125 J Hare 'The Omnipotent Warranty: England v the World' *Paper International Marine Insurance Conference* University of Antwerp November 1999.

126 C McArthur *The Contract of Marine Insurance* 2nd ed Stevens and Sons London 1890, xx; W Gow *Marine Insurance: A Handbook* 4th ed Mcmillan and Co Ltd London 1917, 3.

127 The Hanseatic League was an alliance formed by certain German cities for the mutual protection and furtherance of their commercial interests, in the twelfth century. The Hanseatic League framed and promulgated a code of maritime law, which was known as the 'Laws of the Hanse Towns': *Black's Law Dictionary* 4th ed West Publishing Co St Paul, Minn 1968, 846.

128 A Parks *The Law and Practice of Marine Insurance and Average* London Stevens & Sons 1988, 4.

129 Notable marine codes include The Ordinances of Barcelona, 1434, 1458, 1461 and 1484; The Ordinances of Florence, 1523; The Ordinances of Bilbao, 1560; Ordonnance de la Marine, 1681; A Parks *The Law and Practice of Marine Insurance and Average* Stevens & Sons London 1988, 5.

130 W Gow *Marine Insurance: A Handbook* 4th ed Macmillan & Co Ltd London 1917, 5; C McArthur *The Contract of Marine Insurance* Stevens & Sons Ltd London 1890, xxi.



is evidence of merchants' associations carrying on insurance business from the 15th century. However, insurance companies proper were first established in Italy in the 17th century and developed in the second half of the 18th century.<sup>131</sup>

5.7 Marine insurance was thought to have been introduced into England by the Hansa merchants. Lombard traders had also been active in England from the middle of the 13th century. Lombard traders were granted a section of the City of London by Henry IV, and Lombard Street was to become famous in the history of marine insurance. They began to leave England during the reign of Elizabeth I, but by the time of their departure marine insurance was well established in London.<sup>132</sup> The earliest extant English policy of marine insurance dates from 1555 and refers to Antwerp conditions recognised in England. This is early evidence of the international nature of marine insurance law and practice but ironically reverses the subsequent trend for England to dominate in this respect. Indeed, in 1622 a policy issued in Antwerp referred to the practice in Lombard Street.<sup>133</sup>

5.8 Very few marine insurance cases are found in the admittedly sparse legal records of the next two centuries. Disputes were, it seems, resolved by arbitration by men of business rather than by the courts.<sup>134</sup> The earliest case reported by Coke was in 1589.<sup>135</sup> In 1601 a statute passed in the 43rd year of the reign of Elizabeth I established the Court of Policies of Assurance specifically to try marine insurance cases. By the time that this Act was passed marine insurance had existed since 'tyme out of mynde' and was described in its preamble as a

means whereof it cometh to pass that upon the loss or perishing of any ship there followeth not the undoing of any man, but the loss lighteth rather easily upon many than heavy upon few, and rather upon them that adventure not than upon those who do adventure; whereby all merchants, specially those of the younger sort, are allured to venture more willingly and more freely.<sup>136</sup>

5.9 However, the new court was not a success. Between its establishment and 1720, by which time it had fallen into disuse, it heard no more than 60 cases.<sup>137</sup> In contrast to commercial centres in Europe, no attempt was made in England to regulate the content on insurance policies or the rights of the parties to them. On the other hand, European centres continued to pass various codes concerning marine insurance throughout the 15th, 16th and 17th centuries. This is said to have reached a high point in the Ordonnance de la Marine passed by Louis XIV in

131 G Boi 'The Marine Insurance System in Italy: Its Present, its Future' in M Huybrechts E Van Hooydonk & C Dieryck (eds) *Marine Insurance at the Turn of the Millennium* vol I Intersentia Antwerp 1999, 393.

132 A Parks *The Law and Practice of Marine Insurance and Average* London Stevens & Sons 1988, 6.

133 W Gow *Marine Insurance: A Handbook* 4th ed Macmillan & Co Ltd London 1917, 4.

134 C McArthur *The Contract of Marine Insurance* Stevens & Sons Ltd London 1890, xxi.

135 (1589) 6 Coke Rep 47b.

136 H Turner *The Principles of Marine Insurance* Stone and Cox Ltd London 1938[?] 7.

137 W Gow *Marine Insurance: A Handbook* 4th ed Macmillan & Co Ltd London 1917, 7; C McArthur *The Contract of Marine Insurance* Stevens & Sons Ltd London 1890, xxii.

France in 1681, and which was adopted in large part by Napoleon when he instituted the Code de Commerce in 1807.<sup>138</sup>

5.10 In London, business was conducted informally by brokers who arranged for policies to be underwritten. Edward Lloyd established a coffee house in Tower Street which was first mentioned in the *London Gazette* in its issue of 18–21 February 1688, by which time it had come to be a meeting place for men of commerce. About three or four years later Lloyd moved his establishment to the corner of Abchurch Lane and Lombard Street. It developed a reputation for trustworthy shipping news and became the recognised place for obtaining marine insurance.<sup>139</sup> It came to be a place for the exchange of business and continued in that role until the establishment of the Royal Exchange in 1720. By the 1690s usages had standardised somewhat to provide some certainty and justice in disputes, albeit of a rough and ready kind. By the eighteenth century London had become the central market for marine insurance. In 1769 a society of underwriters with fixed rules was formed and in 1779 its members agreed on a standard form ‘Lloyd’s Policy’.<sup>140</sup> With a modest change to its opening words, the wording has survived to the present day and is currently preserved in schedules to the United Kingdom and Australian Marine Insurance Acts.

5.11 The first companies to write marine insurance were established by charter in 1720<sup>141</sup> but the duopoly created by this legislation was revoked in 1824, with a consequent expansion of marine insurance business generally. The process leading to the codification of English marine insurance began with the Marine Insurance Act 1745 (19 Geo 2, c 37), which provided a limited prohibition on wagering policies and reinsurance. This was followed by the Marine Insurance Act 1788 (28 Geo 3, c 56), which required the name of the assured to be inserted in all policies. These Acts were limited in their operation and were ultimately repealed by the Marine Insurance Act 1906 (UK).<sup>142</sup>

5.12 Developments in marine insurance commerce were matched in part by a greater sophistication in marine insurance law. Lord Mansfield became the Lord Chief Justice of the Queen’s Bench Division in 1756 and brought learning and consistency to the subject, and the law of marine insurance became increasingly stabilised. It would be some time, however, before it was systematically codified.

138 W Gow *Marine Insurance: A Handbook* 4th ed Macmillan & Co Ltd London 1917, 6.

139 Ibid 11; A Parks *The Law and Practice of Marine Insurance and Average* Stevens & Sons London 1988, 8; C McArthur *The Contract of Marine Insurance* Stevens & Sons Ltd London 1890, xxiii.

140 W Gow *Marine Insurance: A Handbook* 4th ed Macmillan & Co Ltd London 1917, 9; C McArthur *The Contract of Marine Insurance* Stevens & Sons Ltd London 1890, xix, xxiv–xxv.

141 6 Geo 1 c 18.

142 S Derrington ‘Does the Marine Insurance Act 1909 (Cth) Still Serve the Needs of the Business Community?’ (1995) 7 *Insurance Law Journal* 31.

## Chalmers' masterpiece

5.13 In 1894, the Chancellor, Lord Herschell, introduced a bill into the Parliament at Westminster to codify the common law of marine insurance. After it had been subjected to a 'most rigorous examination by the most important commercial, legal and insurance associations of the United Kingdom' lasting over a decade, it became law on 21 December 1906 and took effect on 1 January 1907 as the Marine Insurance Act 1906 (MIA (UK)).<sup>143</sup>

5.14 This Act codified the existing common law and the rules and principles used in the marine insurance community. Its draftsman, Sir Mackenzie Chalmers, stated that the object of the Act 'was to reproduce as exactly as possible the existing law, without making any attempt to amend it.'<sup>144</sup> The Act has been described as a 'partial codification of the common law'.<sup>145</sup> This Act has been copied by several other jurisdictions, including Australia. It is a testament to Sir Mackenzie's drafting skill, and to the stability (and perhaps conservatism) of the system that it underpins, that the Act remains virtually intact today and operates by custom or contractual incorporation in numerous countries, not only those that have inherited the English legal system generally.

5.15 There have been minor amendments to the MIA (UK). In 1959, the provision rendering time policies for periods over 12 months invalid was repealed.<sup>146</sup> The same amending legislation also removed the statutory requirement for marine policies to specify the subject matter insured and the risk insured, the voyage or period of time covered, the sum insured, and the name or names of the insurers.<sup>147</sup>

## Enactment of the *Marine Insurance Act* in Australia

5.16 The purpose of the Act was set out in the second reading speech by the then Attorney-General, Mr Groom.

At the present time, in each of the States of Australia any one who desires to ascertain what the law as to marine insurance is, has to consult common law authorities and decisions. Of these there are no less than 2,000 in existence. Under these circumstances, of course the law is in cases difficult to ascertain. In some instances, the authorities are uncertain; on some points where certainty is required, no certainty can be gathered; and some decisions rest upon old conditions which have now become obsolete ... Marine insurance is a highly technical branch of the law. It requires for

143 W Gow *Marine Insurance: A Handbook* 4th ed Macmillan & Co Ltd London 1917, 9, 433 (Addenda).

144 E Cattell Jr 'An American Marine Insurance Act: An Idea Whose Time Has Come' [1995] 20 *Tulane Maritime Law Journal* 1.

145 *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd* [1995] 1 AC 501, 518 (Lord Mustill).

146 Finance Act 1959 (UK), repealing MIA (UK) 25(2) cf MIA s 31(2).

147 Finance Act 1959 (UK), repealing MIA (UK) 23(2)–(5) cf MIA s 29(b)–(e).

the complete mastery of it years of careful research and practice. At the same time it is a branch of the law which greatly affects the commerce of our people. It is, therefore, above all things highly desirable that this branch of the law should be made clear, definite and certain.<sup>148</sup>

5.17 The *Marine Insurance Act 1909* (Cth) (MIA) is virtually identical to the MIA (UK) with only one substantive change found in MIA s 28 (the equivalent of MIA (UK) s 22) and differing in the use of subjunctive. As noted above there have been minor amendments to the MIA (UK) but no equivalent changes have been made to the MIA in Australia. The Australian MIA has remained basically untouched despite extensive statutory reforms in general insurance law in Australia<sup>149</sup> and in relation to marine insurance in other countries.

## Review of insurance and maritime law in Australia

### Insurance law

5.18 Prior to the enactment of the *Insurance Contracts Act 1984* (Cth) (ICA) the Australian law of insurance contracts was a mixture of common law principles and a number of imperial, federal and state statutes. Until the Commission commenced its review of insurance contracts in 1976, there had been no coherent scrutiny of the adequacy and appropriateness of these principles and statutes.

5.19 The review of the general law of insurance began in September 1976 when the Commission was given a reference by the then Attorney-General which required it to report on the adequacy of the law governing contracts of insurance. The Commission was required under the terms of its reference to have regard to the interests of the insurer, the insured and the public. One focus of the review was to ensure fairness having regard to the relative bargaining power between insurers and insureds.<sup>150</sup>

5.20 This review resulted in two related but self-contained reports from the Commission, namely Australian Law Reform Commission Report 16 *Insurance Agents and Brokers* (ALRC 16) relating to the conduct and regulation of insurance intermediaries, and Australian Law Reform Commission Report 20 *Insurance Contracts* (ALRC 20) relating to insurance contracts.

5.21 The main recommendations in ALRC 16 and ALRC 20 were adopted and implemented in the *Insurance (Brokers and Agents) Act 1984* (Cth) (IABA) and the ICA respectively.

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148 L Groom *Hansard* (H of R) 6 October 1908, 764.

149 The MIA was amended by the *Statute Law Revision (Decimal Currency) Act 1966* (Cth) and s 2 was repealed by the *Statute Law Revision Act 1973* (Cth). See para 4.3.

150 ALRC 20, Terms of reference.

***ALRC 16 and the Insurance (Agents and Brokers) Act 1984 (Cth)***

5.22 The review of the law relating to insurance intermediaries took place when a number of major defaults by insurance brokers had occurred, causing loss to the public and affecting the good name of the insurance industry. Between 1970 and 1979, at least 44 broking firms had become insolvent resulting in premium losses involving millions of dollars.<sup>151</sup> In determining the changes to be made to the law, the Commission was particularly concerned with the need to protect innocent purchasers from losses which occur as a result of marketing methods, to promote an informed choice among insureds, and to encourage competition.

5.23 The IABA, which implemented most of the Commission's recommendations, is aimed at

- strengthening the financial stability of the insurance industry
- protecting the insuring public against the negligence or misconduct of an agent or broker
- the minimisation of practices harmful to the insuring public, and
- the maintenance of standards of conduct of, and quality of advice offered by, agents and brokers.<sup>152</sup>

5.24 Its main provisions deal with insurers' responsibility for the conduct of intermediaries, misrepresentations by intermediaries, regulation of brokers and payments to intermediaries.

5.25 As the IABA applies to all contracts of insurance governed by Australian law, some of its provisions, for example, those relating to payments to intermediaries, may overlap with those in the MIA relating to agents and brokers.<sup>153</sup> This is dealt with in detail in ch 13.

***ALRC 20 and the Insurance Contracts Act 1984 (Cth)***

5.26 Reform to the general law of insurance was considered necessary as insurance contracts were subject to a bewildering variety of laws which gave rise to anomalies and uncertainties. Those laws had not kept pace with social and economic developments in the community. The level of complaints from dissatisfied policy holders showed a need for change.<sup>154</sup> To some extent the complaints which generated the Commission's earlier inquiry and the subsequent legislation were repeated in the Commission's current review of the MIA.

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151 *Hansard* (H of R) 4 June 1984, 2826.

152 Explanatory memorandum, Insurance (Agents and Brokers) Bill 1984 (Cth).

153 See MIA s 58–60. See ch 13.

154 *Hansard* (H of R) 29 May 1984, 2230.

5.27 The terms of reference specifically excluded marine insurance as it was regarded as a discrete area of insurance with special significance for international trade and commerce.<sup>155</sup> The reasoning that led to that conclusion has never been enunciated in detail. Even if the conclusion is valid, the omission of marine insurance from the earlier review has meant that many of the concerns dealt with in this report cover the same or similar points raised twenty years ago. The recommendations in this report reduce, but do not remove, the differences between the two statutes.

5.28 In ALRC 20 the Commission recommended the making of a national law regulating insurance contracts that would be superimposed on existing laws.

5.29 The Commission saw a need to promote an informed choice of insurance and to avoid unfair burdens to the insureds in respect to the remedies available to insurers for misrepresentations, non-disclosure and breach of contract.<sup>156</sup> It was noted that ‘a system which persistently disappointed the reasonable expectations of insureds can hardly claim to represent a fair balance between the competing interests of insurers and insureds’.<sup>157</sup>

5.30 Many of the Commission’s recommendations adopted in the ICA were intended to improve the operation of the insurance market by ensuring that necessary and adequate information is available to prospective insureds and to provide a fairer set of rules governing the relationship between insureds and insurers.<sup>158</sup> For example, one of the Commission’s recommendations which was adopted in the ICA involved the abolition of the requirement for an insurable interest in general insurance contracts as the Commission found that the indemnity principle and gaming and wagering legislation already provided sufficient protection to insurers against destruction of the subject matter of insurance.<sup>159</sup> Another key recommendation was the abolition of the insurer’s automatic right to avoid a contract in all cases of non-disclosure or misrepresentation regardless of actual loss as this was considered to be out of all proportion to the harm caused by the insured’s breach.<sup>160</sup> Both of these issues, among others, arise again for consideration in this report.

5.31 In 1998 the ICA was amended by the *Insurance Laws Amendment Act 1998* (Cth) to exclude pleasure craft insurance from the operation of the MIA.<sup>161</sup>

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155 Australian Law Reform Commission Discussion Paper 7 *Insurance contracts* Sydney 1979 (ALRC DP 7) 5.

156 ALRC 20, Summary of recommendations.

157 Ibid 10.

158 Ibid Summary of recommendations.

159 Ibid.

160 Ibid 118.

161 See para 8.14–8.16

## **Maritime law**

### ***ALRC 33 and the Admiralty Act 1988 (Cth)***

5.32 Prior to the enactment of the *Admiralty Act 1988* (Cth), the development of admiralty jurisdiction in Australia was prevented by the Colonial Courts of Admiralty Act 1890 (UK), an imperial statute applying to Australia which limited admiralty jurisdiction to matters within the admiralty jurisdiction in England in 1890. This resulted in many obscurities and uncertainties about the scope of the jurisdiction in Australia, and placed many unjustified limitations on the subject matter of the jurisdiction.<sup>162</sup>

5.33 On 23 November 1982 the then Attorney-General asked the Commission to review and report on all aspects of admiralty jurisdiction. The review resulted in two separate reports on admiralty jurisdiction, Australian Law Reform Commission Report 33 *Civil Admiralty Jurisdiction* (ALRC 33) and Australian Law Reform Commission Report 48 *Criminal Admiralty Jurisdiction and Prize* (ALRC 48).

5.34 In its review, the Commission was particularly mindful that international business expectations had been created by the long history of admiralty as a distinct jurisdiction and that there was a need to strike a fair balance between the interests of ship owners and those dealing with the ships. The recommendations of the Commission were directed largely at clarifying the broad framework of admiralty jurisdiction rather than a substantive overhaul of the law.<sup>163</sup>

5.35 The recommendations of the Commission were accepted and implemented in the *Admiralty Act*, which primarily provides for and regulates the admiralty jurisdiction of the courts but, with the exception of s 34, does not create any new causes of action or new substantive rights. Under the previous law a party was only liable for damages for unjustified arrest in cases of gross neglect. Section 34 creates a more extensive liability for damages for unjustified arrest of, or unjustified refusal to release, a ship or other property under the Act.<sup>164</sup> The main provisions of the *Admiralty Act* clarify the type of claims which are subject to admiralty jurisdiction, confer admiralty jurisdiction on the Federal Court of Australia and the state and territory Supreme Courts, and provide for uniform rules of procedure to be made dealing with distinctive aspects of admiralty procedure.

5.36 Although not relevant to questions of insurance, these reviews demonstrate the Commission's active role in reforming maritime as well as insurance law. These two strands intersect in the present review.

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162 Australian Law Reform Commission Report 33 *Civil Admiralty Jurisdiction* AGPS Canberra 1986 (ALRC 33), Summary, xv.

163 ALRC 33, Summary.

164 Explanatory memorandum, Admiralty Bill 1988.

### ***Other recent reviews of maritime law***

5.37 Other significant areas of reform in maritime and relevant aspects of commercial law over the last 25 years include the following.

- The *Carriage of Goods by Sea Act 1991* (Cth) (COGSA) sets out Australia's marine cargo liability regime and sets statutory minimum levels of carrier liability for loss, damage or delay to sea cargoes. International conventions impose terms regulating the contractual relationship between shippers and carriers. The main conventions are the Hague or Hague-Visby Rules and the Hamburg Rules.<sup>165</sup> COGSA provided for the amended Hague Rules to apply, but the then government envisaged that the Hamburg Rules would apply once they had been adopted by Australia's major trading partners. A working group was formed in 1995 to develop an appropriate cargo liability regime for Australia. COGSA was amended in 1997, and regulations were introduced in 1998 to implement a package of measures developed by the working group.<sup>166</sup> These regulations modified the operation of the amended Hague Rules as they apply in Australia.
- Commonwealth legislation has been enacted to protect the marine environment and to adopt international conventions governing marine pollution. A package of 'protection of the sea' legislation was enacted in 1981 which implemented international conventions and provided funding for a national plan to deal with oil and chemical spills by imposing levies.<sup>167</sup> Other legislation includes the *Protection of the Sea (Prevention of Pollution from Ships) Act 1983* (Cth)<sup>168</sup> and the *Protection of the Sea (Oil Pollution Compensation Fund) Act 1993* (Cth).<sup>169</sup>
- Australia is party to several international conventions concerned primarily with the safety of ships. The Safety of Life at Sea (SOLAS) Convention is regarded as the most important. The SOLAS Convention mandates the International Safety Management Code (ISM Code), which provides an

165 See ALRC DP 63, para 1.30.

166 Department of Transport and Regional Services 'Australia's Cargo Liability Regime' <http://www.dotrs.gov.au> (12 February 2001).

167 This package included *Protection of the Sea (Powers of Intervention) Act 1981* (Cth), *Protection of the Sea (Civil Liability) Act 1981* (Cth), *Protection of the Sea (Shipping Levy) Act 1981* (Cth) and the *Protection of the Sea (Shipping Levy Collection) Act 1981* (Cth). Details of the national plan are set out in 'Australia's National Plan to Combat Pollution of the Sea by Oil and other Noxious and Hazardous Substances' Australian Maritime Safety Authority <http://www.amsa.gov.au/me/natplan/overview.htm> (12 February 2001).

168 This Act implements parts of the MARPOL Convention relating directly to prevention of pollution. The *Navigation Act 1912* (Cth) implements those provisions of MARPOL relating to ships, including ship construction and survey.

169 This Act, together with the *Protection of the Sea (Civil Liability) Act 1981* (Cth), implements the CLC/Fund Conventions.



international standard for the safe management and operation of ships. The SOLAS Convention is implemented by Part IV of the *Navigation Act 1912* (Cth).

- Part X of the *Trade Practices Act 1974* (Cth) (TPA) regulates the market conduct of international liner cargo shipping companies which form conferences to coordinate joint services, share capacity and agree on freight rates. Part X provides conditional exemptions from Part IV of the TPA (restrictive trade practices) to registered shipping conferences. It has been reviewed and amended a number of times since enactment. Most recently, the Productivity Commission undertook a review of Part X and reported in September 1999. On the Productivity Commission's recommendation, the government retained Part X but with some additional amendments to improve the application of competition policy to international liner cargo shipping. These changes were implemented by the *Trade Practices Amendment (International Liner Cargo Shipping) Act 2000* (Cth).<sup>170</sup>
- The *Shipping Registration Act 1981* (Cth) sets out the conditions for registration of ships in Australia. In 1997 the Government completed a competition policy review of the Act. That review confirmed the need for a national ship registration system but recommended restructuring the Register into a number of parts so as to provide greater flexibility and reduce costs of registration for some vessel owners.
- The *Navigation Act 1912* (Cth) is the main piece of Commonwealth legislation which regulates various matters including ship safety, coastal trade, employment of seafarers and shipboard aspects of the protection of the marine environment. It also regulates wrecks and salvage operations, passengers, tonnage measurement of ships and a range of administrative measures relating to ships and seafarers. There have been over 70 amendments to the Act since its enactment, around 50 of which have been in the last 20 years.<sup>171</sup> The most recent and wide-ranging review of the Act has been conducted jointly by the Department of Transport and Regional Services (Cross-Modal and Maritime Transport Division) and the Australian Maritime Safety Authority.<sup>172</sup>

170 Department of Transport and Regional Services 'Review of Part X of the Trade Practices Act 1912' <http://www.dotrs.gov.au> (12 February 2001).

171 Department of Transport and Regional Services and Australian Maritime Safety Authority *Review of the Navigation Act 1912* Final Report June 2000, 184.

172 Department of Transport and Regional Services and Australian Maritime Safety Authority *Review of the Navigation Act 1912* Final Report June 2000. This review did not consider Part VI dealing with the coastal trade. Coastal trade issues were reviewed by the Shipping Reform Group, which reported in March 1997.

The review noted that the *Navigation Act* does not have a stated objective but covers a range of subjects, reflecting its origins and development as an omnibus piece of legislation covering shipping regulation. The review recommended that the legislation have stated objectives and that matters not directly related to ship safety and marine environment protection should be repealed or relocated in more appropriate legislation. It recommended that the objectives of the legislation should be to enhance ship safety and protection of the marine environment, facilitate international shipping trade, and provide safe conditions for seafarers.

The review suggested that the extent of changes proposed supports the development of new shipping legislation rather than amendment of the *Navigation Act*. The review proposed a staged approach be taken, with progressive repeal of the *Navigation Act* as new legislation is drafted.<sup>173</sup>

- Electronic commerce generally has been assisted by the enactment of the *Electronic Transactions Act 1999* (Cth) (ETA).<sup>174</sup> The ETA was the result of recommendations made by the Electronic Commerce Expert Group which was established by the Attorney-General to report on the legal issues arising from the development of electronic commerce.<sup>175</sup> Each state and territory is enacting uniform legislation based on the ETA. Changes have also been made to the laws governing carriage of goods by sea to accommodate electronic transactions. The uniform Sea-Carriage Documents Acts enacted in all states and the Northern Territory to replace old bills of lading legislation specifically cover electronic bills of lading, as does the *Carriage of Goods by Sea Act 1991* (Cth).<sup>176</sup>

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173 Department of Transport and Regional Services and Australian Maritime Safety Authority *Review of the Navigation Act 1912* Final Report June 2000, executive summary.

174 See para 15.58–15.72.

175 Expert Group to the Attorney General *Electronic Commerce: Building the Legal Framework* Report of the Electronic Commerce Expert Group to the Attorney General, Attorney-General's Department 31 March 1998.

176 See para 15.58–15.72.

## 6. An international market

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### Introduction

6.1 This chapter examines the international marine insurance market and the place of Australian marine insurance both within the international market and as part of the domestic insurance industry generally. The economic importance of encouraging Australian importers and exporters to arrange insurance with Australian insurers is also discussed.

### The international market

6.2 Marine insurance is inherently international. A shipowner or an importer or exporter of goods to or from Australia can choose to insure with an Australian, United Kingdom, USA or other overseas-owned insurer. Contracts of co-insurance may be made where, for example, 40% of the risk is insured in Australia, 40% in New Zealand and 20% in Singapore, each contract being subject to the laws and practices of the country in which the insurance is placed.<sup>177</sup> Under MIA s 30(2), each agreement with each co-insurer is regarded as a separate contract.

6.3 While there may be an inclination for insureds to use insurers in their country of domicile, Australian insurers insure risks from all over the world. Shipowners may choose to insure here because their ships are Australian-flagged, they commonly use Australian ports, or the head office of the company is located in Australia. Cargo owners importing goods may buy on C&F or FOB terms<sup>178</sup> and then choose to 'import' insurance or buy insurance from an Australian company.

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<sup>177</sup> Insurers *Consultation* Melbourne 6 June 2000.

<sup>178</sup> 'Cost and Freight' (C&F) or 'Free on Board' (FOB) terms under which the risk (but not necessarily the property) in the goods passes to the purchaser at the ship's rail. The term C&F has been replaced with CFR in the Incoterms 1990 and Incoterms 2000. See ch 11 for further discussion of these terms.

Exporters may sell CIF,<sup>179</sup> in effect ‘exporting’ the insurance, or sell C&F or FOB with the cargo insured overseas.

6.4 Australian involvement in the transport of cargo, for example, because a ship carries the Australian flag or because goods are being exported from or imported into Australia, does not mean that insurance will be purchased here or even that the business is notionally ‘Australian’. Insureds generally place insurance with a particular underwriter because the price is competitive. The market is price-sensitive and competitive within Australia and with overseas insurers. Other factors that influence the choice of insurance include whether the insured is the exporter or importer of goods (importers or buyers generally have the most say about where cargo will be insured) as well as national laws and customs. Some nations, for example, Nigeria and the Solomon Islands, impose legal restrictions that require insureds to use their own insurance companies.<sup>180</sup> Japanese customs and market practices favour their own insurance industry and it is difficult for exporters to Japan to use non-Japanese insurers.<sup>181</sup>

6.5 Essentially, the Australian marine insurance market is marine insurance business written by insurance companies located in Australia. Most Australian insurers are divisions of, or are writing insurance for, foreign-owned insurance companies.<sup>182</sup> Australia’s share of the international market in insurance is measured by the insurance written by companies located in Australia and the figures for other countries also represent a mix of local and international business.

### Premium revenue

6.6 The most recent information available to the Commission concerning the international market in marine insurance relates to the 1999 accounting year and was published by the International Union of Marine Insurance (IUMI).

179 ‘Cost, Insurance and Freight’; see ch 11 for further discussion.

180 Insurers and legal practitioner *Consultation* Brisbane 11 May 2000; Insurers and legal practitioners *Consultation* Sydney 15 May 2000; Associated Marine Insurers Agents Pty Ltd *Correspondence* 15 June 2000.

181 Insurers and brokers *Consultation* Sydney 27 March 2000; Insurers and legal practitioner *Consultation* Brisbane 11 May 2000; Insurers and legal practitioners *Consultation* Sydney 15 May 2000; Insurers *Consultation* Melbourne 6 June 2000. It is less difficult for importers bringing goods from Japan to arrange Australian insurance.

182 For example, the parent companies of Associated Marine Insurers Agents Pty Ltd are Swiss (Zurich) and British (CGU). National Marine is owned by Royal and Sun Alliance, a UK company. QBE, HIH and Suncorp are Australian-owned but QBE’s associate company, Mercantile Mutual, is Dutch. ACE, Chubb and St Paul’s Fire and Marine Insurance are all US companies, and Gerling and MMI are German: Insurers *Consultation* Melbourne 6 June 2000.

6.7 In 1999 the gross premium income for all countries for direct marine insurance was nearly US\$11 billion. This comprised hull insurance (25%), transport and cargo insurance (61%), marine liability insurance (8%) and offshore energy insurance (6%).<sup>183</sup> The following table shows the proportion of premium revenue received by marine insurers in 1999 in all countries where figures are collected. The figures below show the top 14 countries in terms of premium revenue for all markets.

**Table 1. Proportion of premium revenue — 1999<sup>184</sup>**

	<b>% hull market</b>	<b>% cargo market</b>	<b>% marine liability market</b>	<b>% offshore, energy market</b>	<b>% total market</b>
<b>Japan</b>	18.2	27.5	4.3	3.3	21.7
<b>UK</b>	18.6	8.7	24.7	62.5	15.5
<b>USA</b>	10.3	10.0	26.4	12.2	11.3
<b>France</b>	12.9	10.1	0.3	10.2	10.0
<b>Germany</b>	2.8	14.7	0	0	9.6
<b>Norway</b>	9.4	0.8	2.9	10.0	5.6
<b>Italy</b>	7.1	5.2	1.7	0.9	5.1
<b>Spain</b>	3.7	2.5	0	0	2.4
<b>Sweden</b>	2.1	1.9	3.6	0.2	2.0
<b>Netherlands</b>	1.2	1.9	3.1	N/A	1.7
<b>Switzerland</b>	0.1	2.5	1.5	0	1.6
<b>China</b>	1.8	1.8	0	0	1.6
<b>Australia</b>	1.7	1.4	1.8	0.3	1.5
<b>Hong Kong</b>	1.1	1.5	0	0	1.2
<b>Total</b>	91.0	90.5	70.3	99.6	90.8

6.8 The figures demonstrate the importance of the UK in the marine insurance industry though in terms of primary insurance premium revenue its position is by no means dominant. These figures belie London's prominence and influence for historical, cultural and economic reasons; its position would probably be more dominant if reinsurance premiums were included, for example. Furthermore, the widespread use and influence of English law, practice and standard wordings demonstrates an influence far beyond mere premium revenue.

183 IUMI *Report on Marine Insurance Premiums 1998 and 1999: Update per 12th October 2000* IUMI and the Norwegian Central Union of Marine Underwriters (CEFOR) <http://www.cefor.no> (12 October 2000). The figures do not include UK-based P & I clubs or reinsurance (facultative or treaty).

184 Ibid.

### Australia's position

6.9 On the IUMI figures the amounts written in Australia are modest compared to the insurance written in the major jurisdictions. Nevertheless, Australia earned a greater proportion of international marine insurance premium revenue than insurers in Belgium (1.0%) and Canada (0.9%),<sup>185</sup> and Australia's 1999 position as 13th in the world in terms of marine insurance indicates a significant industry, particularly considering the relative sizes of the economies of the other major insuring nations.

6.10 While Australia is fifth in the world in terms of the frequency and volume of shipping,<sup>186</sup> 95% of its trade volume is carried by foreign shipping services. The Australian-flagged fleet is small.<sup>187</sup> This is reflected in the break-up of the Australian insurance market in which cargo insurance dominates, as it does in the global market.

6.11 According to IUMI figures Australia's 1999 marine cargo insurance premium revenue was US\$93 million, followed by hull insurance at US\$46.8 million. The hull figure would include a significant proportion of pleasure craft insurance, which is categorised as marine by insurers even though it no longer comes under the MIA. The following table shows the break-up of this premium revenue and the percentage of Australia's revenue compared with the global market.

**Table 2. Australia — Premium revenue 1999**<sup>188</sup>

	<b>Cargo</b>	<b>Hull</b>	<b>Marine liability</b>	<b>Offshore energy</b>	<b>Total</b>
<b>Premium revenue (US\$ million)</b>	93.0	46.8	15.0	2	156.8
<b>% of Australian premium revenue</b>	59.3	29.8	9.6	1.3	100
<b>% of world premium revenue</b>	1.4	1.7	1.8	0.3	1.5

6.12 The Insurance Council of Australia has estimated that marine insurance premium revenue in Australia totals about A\$400 million (US\$192 million),<sup>189</sup> compared to the IUMI figure of US\$156.8 million.

185 Ibid.

186 P Leary 'The "Maritimeness" of Australia — But How Maritime is Australia?' (Jan/Feb 2000) 140 *Australian Defence Force Journal* 41, 41 citing the government's *State of the Marine Environment Report*.

187 Commonwealth of Australia *Australia's Oceans Policy — Specific Sectoral Measures* Environment Australia 1998, 16.

188 IUMI *Report on Marine Insurance Premiums 1998 and 1999: Update per 12th October 2000* IUMI and CEFOR <http://www.cefor.no> (12 October 2000).

189 Insurance Council of Australia *Submission 11*. Converted at US\$0.48=A\$1.00.

## The place of marine insurance in Australia

6.13 According to the Australian Prudential Regulatory Authority (APRA), in 1999, the Australian marine and aviation insurance market received annual premium revenue of around A\$507 million<sup>190</sup> and claims expenses were around A\$358 million.<sup>191</sup> Premium revenue by state was highest in New South Wales (A\$305 million) followed by Victoria (A\$85 million).<sup>192</sup>

6.14 Marine and aviation insurance in Australia comprises less than 3% of the total general insurance market.<sup>193</sup> Those sectors with the largest share of the market are domestic motor vehicle (22%), house owners/householders (15%) and CTP motor vehicle (14%).<sup>194</sup>

### Market expansion or contraction?

6.15 Whether the marine insurance market is expanding is uncertain. The Australian market is considered by some to be contracting,<sup>195</sup> with companies increasingly using overseas or captive insurers.<sup>196</sup> Globally, the marine insurance market has sustained trading losses for several years. In London, Lloyd's reported in 1998 that there had been deterioration in trading conditions in the market for marine insurance.<sup>197</sup>

6.16 In Norway, the Norwegian Central Union of Marine Underwriters (CEFOR) warned in 1998 that severe losses were a reality for all marine insurance markets.<sup>198</sup> It predicted that, as a consequence, insurers would have to pull out of the market or increase premiums to reflect accurately the risks underwritten.<sup>199</sup> In its 1998 annual

190 APRA 'General Insurance Market Statistics' [http://www.apra.gov.au/iands/Marketstats/gen\\_stats.htm](http://www.apra.gov.au/iands/Marketstats/gen_stats.htm) (14 November 2000); APRA *Selected Statistics on the General Insurance Industry — Year Ending December 1999* APRA 2000, table 6. Figures for the marine and aviation industry are aggregated. More detailed statistics are not collected.

191 APRA *Selected Statistics on the General Insurance Industry — Year Ending December 1999* APRA 2000, table 8.

192 Ibid, table 10.

193 'General insurance' in this context is all insurance apart from life and health. This figure is for the marine and aviation markets for the 12 months ending 31 December 1999: APRA 'General Insurance Market Statistics' [http://www.apra.gov.au/iands/Marketstats/gen\\_stats.htm](http://www.apra.gov.au/iands/Marketstats/gen_stats.htm) (14 November 2000).

194 APRA *Selected Statistics on the General Insurance Industry — Year Ending December 1999* APRA 2000, table 6.

195 Insurers and legal practitioners *Consultation* Sydney 15 May 2000.

196 Insurers and brokers *Consultation* Sydney 27 March 2000. A captive insurer is a company within a group of related companies performing the function of insurer to that group: APRA *Selected Statistics on the General Insurance Industry — Year Ending December 1998* APRA 1999, 49.

197 Lloyd's of London *Global Results 1998* Lloyd's of London 1998, 12.

198 CEFOR 'Marine Underwriters on their Way to the Wizard of Oz?' *News release* CEFOR 11 November 1998 [http://www.cefor.no/nyheter/nyheter\\_index.htm](http://www.cefor.no/nyheter/nyheter_index.htm) (17 February 2000).

199 Ibid.

report, CEFOR attributed these losses to the positive drive by the shipping industry to improve safety and reduce claims, which had been overcompensated for by insurers in reducing the premiums charged.<sup>200</sup> The predicted losses were reported as a reality in 2000 for the Norwegian hull markets with projected global industry losses of US\$3 billion reported.<sup>201</sup> In its 1999 annual report CEFOR attributed losses in 1998 to an overall increase in claims frequency compounded by a number of large claims. However, it also noted that the average cost of claims decreased.<sup>202</sup> CEFOR predicted that premiums would rise for some accounts coming up for renewal in 2001 and, on average, marine hull and machinery insurance would not be profitable in the near future.<sup>203</sup>

6.17 The world fleet is expanding and has steadily increased from 423 million gt in 1990 to 532 million gt in 1998.<sup>204</sup> Global losses have also been declining.<sup>205</sup> In the competitive Australian market the response to this has been to push premiums to a level below profitability<sup>206</sup> and this is the experience in other countries, including the American and London markets.<sup>207</sup>

6.18 The IUMI figures show that, in Australia, premium revenues increased from 1996 to 1997 but fell dramatically in 1998 before settling.<sup>208</sup> This fall was much greater than that experienced by the world market generally. It is not clear whether this fall in premiums is a result of world market conditions, is due to a real contraction in the Australian market or is a function of changes in data collection or

200 CEFOR *Annual report 1998* CEFOR Oslo 1998, 13 <http://www.storebrand.no> (28 March 2000).

201 CEFOR 'Global Marine Insurance Markets Loses US\$3 billion in 1999' *News release* CEFOR 30 March 2000 <http://www.cefor.no> (16 June 2000).

202 CEFOR *Annual report 1999* CEFOR Oslo 1999, 21 <http://www.cefor.no/news/pdf/cefor1999.pdf> (30 November 2000).

203 Ibid.

204 For ships over 100 gt: The world fleet 1990–98 by ship type, International Underwriters Association (IUA) *Marine and Casualty Statistics* IUMI Conference Berlin 1999.

205 Figures from the IUA and IUMI show that global losses have been declining: 0.56% of the tonnage afloat for vessels over 500 gt was totally lost in 1979, steadily declining to 0.2% in 1988. The figure has remained low, down to 0.16% in 1998: World loss ratios 1977-1989, IUA *Hull Casualty Statistics* IUMI Conference London 1990; Total losses in proportion to shipping afloat, IUA *Marine and Casualty Statistics* IUMI Conference Berlin 1999.

206 Insurers and brokers *Consultation* Sydney 27 March 2000.

207 CEFOR 'Marine Underwriters on their Way to the Wizard of Oz?' *News release* CEFOR 11 November 1998 [http://www.cefor.no/nyheter/nyheter\\_index.htm](http://www.cefor.no/nyheter/nyheter_index.htm) (17 February 2000), although Norway claims that its losses are primarily due to an increase in claims, as well as insufficient premium revenue. Germany has also recorded a decline in premium revenues and a decline in claims: H Fromme 'German marine insurers suffer' *Lloyd's List* 26 June 2000.

208 Australian hull premiums: 1996 US\$88 million; 1997 US\$92 million; 1998 US\$48 million; 1999 US\$46.8 million. Australian cargo premiums: 1996 US\$158 million; 1997 US\$171 million; 1998 US\$85 million; 1999 US\$ 93 million. Global premiums also fell, but not as dramatically: Hull: 1996 US\$4 375 million; 1997 US\$3 581 million; 1998 US\$3 072 million; 1999 US\$2 692 million; cargo: 1996 US\$8 205 million; 1997 US\$7 746 million; 1998 US\$7 346 million; 1999 US\$6 520 million: International Union of Marine Insurance *Report on Marine Insurance Premiums 1997* IUMI and CEFOR <http://www.cefor.no> (16 June 2000) and International Union of Marine Insurance *Report on Marine Insurance Premiums 1998 and 1999* IUMI and CEFOR <http://www.cefor.no> (12 October 2000).



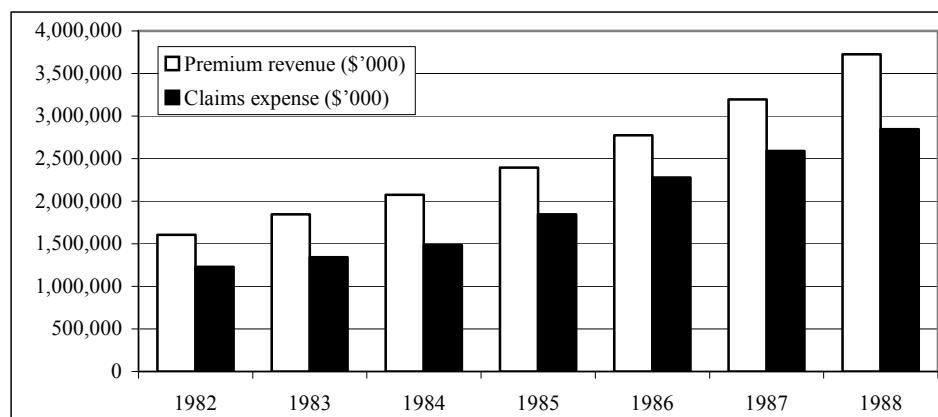
interpretation by IUMI. The Commission has been unable to obtain relevant statistics in relation to the level of marine insurance claims that might clarify the state of the market.

6.19 Overall, the available statistics are not particularly instructive. The bases of the figures collected by IUMI and APRA are unknown; they apparently aggregate different market sectors, for example. The lack of information explaining the assumptions and method behind these figures makes it impossible to assess, for example, whether or not any part of the fall in premium revenue from 1998 to 1999 is attributable to the shift of pleasure craft insurance from the MIA to the ICA and, if so, to what extent.

6.20 Although the Commission has been told anecdotally that premiums rose and then fell after the introduction of the ICA on 1 January 1986, there are no statistics specifically monitoring the effect of the ICA on premium rates and revenue during that period. The following table shows statistics collected by the Insurance and Superannuation Commission<sup>209</sup> of annual premium revenue and payouts in general insurance. There appears to have been a steady increase of both premium revenue and claims expense, with no dramatic change around 1986.

6.21 However, nothing in the information available to the Commission suggests that any fluctuations related to the introduction of the ICA or the amendments relating to pleasure craft insurance had any significant or lasting impact on the Australian non-marine insurance market.

**Table 3. Premium revenue and claims expense for general insurance 1982-1988**<sup>210</sup>



209 APRA took over from the Insurance and Superannuation Commission on 1 July 1998.

210 Insurance and Superannuation Commission *Selected Statistics on the General Insurance Industry — Years Ending 31 December 1982–1988* AGPS Canberra, tables 1.6, 1.8. These statistics cover: fire, house owners and householders, contractors, motor vehicle, public liability, other non-marine general insurance.

## Economic importance

6.22 The Department of Transport and Regional Services has suggested that, consistently with Australia's position as primarily a cargo owning (and not a ship owning) nation, any amendments to the MIA should be made with the interests of Australian shippers, including exporters, importers and coastal cargo interests, foremost in mind.

It is important that Australian shippers can access adequate marine cargo insurance cover at internationally competitive rates. It is especially important in the case of shippers whose goods fall into the category of hazardous or noxious cargoes.

...

Economic studies of supply and demand elasticities suggest that on average around about two-thirds of the costs of transporting Australian export and import is borne finally by Australian exporters and importers rather than by the overseas exporters and importers. The costs borne by the insurance industry in meeting claims in the event of loss or damage to sea cargoes are, for the main part, likely to be passed forward to Australian shippers as a component of subsequent insurance charges.<sup>211</sup>

6.23 There are important economic reasons to encourage Australian importers and exporters to arrange insurance with Australian insurers. Although most insurers located in Australia are not Australian-owned, insurance placed with these businesses is beneficial in providing Australians with jobs in the insurance industry and has positive economic benefits for associated businesses such as ship repairers, lawyers and surveyors, and for Australia's terms of trade.

6.24 Where Australian importers import on CIF terms they are in effect importing the marine insurance as well as the goods. Importing goods on C&F or FOB terms reduces the foreign currency cost of imports and helps to improve the national balance of trade. Similarly, exporters who sell goods on CIF terms help Australia's balance of trade by exporting insurance services as well as goods. The exporter usually recovers the full cost of the insurance from the overseas buyer in the CIF invoice price.<sup>212</sup>

6.25 It has been suggested that, as most Australian insurers are foreign-owned (see paragraph 6.5 above), reform of the MIA should favour the interests of Australia cargo shippers and shipowners. However, any increased exposure to risk resulting from reform could be reflected in increased premiums or more limited access to insurance.<sup>213</sup>

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211 Department of Transport and Regional Services *Submission 2*.

212 M Hill 'The Implications for Marine Insurers of the Carriage of Goods by Sea in the 1980's' *Paper* MLAAANZ Annual Conference Wellington 13–15 September 1979, 5; M Hill 'How to Profit from Australian Marine Insurance' (July–August 1993) *Maritime Studies* 21.

213 *Marine insurance seminar* Phillips Fox Sydney 20 February 2001.

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6.26 Much as the Commission accepts that the outcome of any reform of the MIA must ensure that Australian insureds have access to fair insurance on fair terms and at a fair price, it rejects a unilateral approach in that regard as a driving principle for reform. The objective must be a system that is fair overall, where appropriate consistent with and different from other insurance regimes within Australia, and accessible to (though not necessarily identical to) similar regimes overseas. The following chapter examines overseas marine insurance regimes in some detail.



## 7. International marine insurance law

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### Introduction

7.1 This chapter examines the influence of United Kingdom marine insurance law and practice on the law and practice in Australia and other common law countries. The commonalities and differences between Australian law and the law in the United Kingdom and other common law countries are described. The legal regimes applicable to marine insurance in civil code countries and some important differences between common law and civil code jurisdictions are briefly summarised. The chapter concludes with discussion of initiatives to consider the prospect of the harmonisation of national marine insurance laws and other relevant international reforms.

### The influence of United Kingdom law

7.2 Australia's association with marine insurance law and practice in the United Kingdom is derived from shared legislative provisions and case law. It is influenced by London's leading role in the world marine insurance market<sup>214</sup> and by the industry practice of using standard contracts developed in the United Kingdom. One view is that

[i]t remains crucial to the Australian industry that it is able to assure those in other countries who obtain policies of insurance from Australian organizations that their terms, and their interpretation by Australian courts, will be consistent with the Marine Insurance Act 1906 (UK).<sup>215</sup>

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214 However, it has been noted that the emergence of strong national markets in such regions as Australasia and Asia, the loss of the separate trade association for the company marine insurance market in London in the form of the Institute of London Underwriters, and the disarray of Lloyd's have all contributed to the shrinking in the size and importance of the London market. This trend is said to be likely to continue: M Hill *Correspondence* 21 March 2000.

215 S Hetherington 'Reform Meets Resistance in Australia' (2000) 11 *The Maritime Advocate* 36, 37.

7.3 In the Commission’s view, ‘consistent with’ in this context does not have to mean ‘identical to’. Indeed, current Australian statute and case law in marine insurance already demonstrate major differences from their English counterparts though there are, of course, major areas in which they coincide.

7.4 When first enacted the *Marine Insurance Act 1909* (MIA) was virtually identical to the Marine Insurance Act 1906 (UK) (MIA (UK)), which, as discussed above, codified the English common law in 1906. Some divergence has crept in over the years. Other common law jurisdictions that also have legislation in most or all significant respects based on the MIA (UK) (some with important variations) include

- New Zealand — Marine Insurance Act 1908
- Canada — Marine Insurance Act 1993
- Singapore — the MIA (UK) has force and effect under the Application of English Law Act 1993
- Malaysia — the MIA (UK) has force and effect under the Civil Law Act 1956<sup>216</sup>
- Hong Kong — Marine Insurance Ordinance of 1964<sup>217</sup>
- India — Marine Insurance Act 1963.<sup>218</sup>

7.5 There have been minor amendments to the United Kingdom legislation that have not been followed in Australia. In 1959, the provision rendering invalid time policies made for periods over 12 months was repealed.<sup>219</sup> The same amending legislation also removed the statutory requirement for marine policies to specify the subject matter insured and the risk insured, the voyage or period of time covered, the sum insured, and the name or names of the insurers.<sup>220</sup> No equivalent changes have been made to the MIA in Australia.

7.6 There is a difference of some importance between s 28 of the MIA and its cognate in the MIA (UK), s 22. This relates to the use in court of a contract of marine insurance not embodied in a policy document. This difference arose when the MIA was being drafted though was not commented on at the time in parliament. The effect of this difference is discussed elsewhere in this report at paragraph 15.10–15.24.

216 English law as at 7 April 1956 applies in West Malaysia (with the exception of Penang and Malacca). In Penang, Malacca, Sabah and Sarawak, the law to be applied will be the English law in its current form from time to time at the time the cause of action arose. There has been no deviation from the English position and courts have applied English law: Shearn Delamore & Co *Correspondence* 27 June 2000.

217 The Hong Kong legislation contains an additional clause prohibiting gambling on loss by maritime perils.

218 The Indian legislation contains an additional clause 89, which gives the government power to direct that MIA applies to ships exclusively used in inland navigation.

219 Finance Act 1959 (UK), repealing MIA (UK) 25(2) cf MIA s 31(2).

220 Finance Act 1959 (UK), repealing MIA (UK) 23(2)–(5) cf MIA s 29(b)–(e). See also para 15.33.

7.7 In New Zealand, the law of insurance generally, including marine insurance as codified by the Marine Insurance Act 1908 (NZ), was extensively modified by the Insurance Law Reform Act 1977 (NZ). This legislation reformed the law relating to, among other things, misrepresentations in contracts of insurance and breach of insurance warranties.<sup>221</sup>

7.8 The 1993 Canadian legislation was enacted in response to a decision of the Supreme Court of Canada in the *Triglav* case,<sup>222</sup> which held that a contract of marine insurance is a contract of maritime law clearly within the jurisdiction of the federal parliament as part of navigation and shipping. Marine insurance had previously been governed by provincial marine insurance Acts modelled on the MIA (UK)<sup>223</sup> or left to the common law. As a result of the *Triglav* case, it appeared that provincial legislation governing contracts of marine insurance would be, at least in part, inoperative. Industry groups urged the government to enact a federal marine insurance Act to resolve this uncertainty as to the scope and application of provincial marine insurance Acts and to use the MIA (UK) as the model. The intention of the Canadian legislation was to preserve ‘the substance of the provisions of the British act while modifying the form in which they are expressed to meet the current drafting standards’.<sup>224</sup>

7.9 Accordingly, the Canadian legislation does not differ in substance to any great degree from the MIA (UK). However, its drafting changes may offer some guidance in reforming the MIA. For example, it has been suggested that adopting the Canadian definition of ‘marine insurance’ might help address some uncertainties about the coverage of the MIA and the ICA in relation to insurance of mixed marine and non-marine transit risks.<sup>225</sup>

7.10 By contrast, Canadian case law diverges from Anglo-Australian law in several relevant areas, especially in relation to warranties,<sup>226</sup> perils of the sea,<sup>227</sup> and insurable interests.<sup>228</sup>

7.11 The USA does not have federal marine insurance legislation<sup>229</sup> but its case law has been in close accord with United Kingdom legislation and case law.

221 Insurance Law Reform Act 1977 (NZ) s 5, 6, 11, 14. See also para 9.53–9.57.

222 *Zavarovalna Skupnost Triglav v Terrasses Jewellers Inc and Bank of Montreal* [1983] 1 RCS 283.

223 eg Insurance (Marine) Act 1979 (BC); Marine Insurance Act 1973 (NB).

224 Parliament of Canada *Commons Debates* 23 March 1993, 1025.

225 MIA (Can) s 6 and see para 8.53–8.56.

226 See para 9.3–9.41.

227 See *Great China Metal Ind Co Ltd v Malaysian International Shipping Ltd Bhd (The Bunga Seroja)* (1998) 196 CLR 161.

228 See para 11.11.

229 Alone among the states, California has a chapter of its Insurance Code devoted to marine insurance. Many of its provisions are similar to those in the MIA (UK): G Staring ‘Is the Doctrine of Utmost Good Faith Out of Date?’ *Paper Marine Insurance Seminar CMI 35th International Conference*, Sydney October 1994.

Federal admiralty law in the USA, including that related to marine insurance, has been greatly influenced by the English common law and federal courts in the USA have explicitly sought to keep federal marine insurance law in harmony with English law. However, the law in the USA has been complicated by the decision in *Wilburn Boat v Fireman's Fund Insurance Co*,<sup>230</sup> which resulted in state rather than federal law (including laws relating to general insurance) being applied to policies of marine insurance. As a consequence American law increasingly diverges from the law in the United Kingdom. These differences include variations with respect to misrepresentation, non-disclosure, and express and implied warranties.<sup>231</sup> This is discussed in detail at paragraph 9.41. Differences among the States have the potential of further fracturing the law of marine insurance in the USA.

7.12 In order to address concerns about uncertainty in American law and to address issues of harmonisation with the laws of other jurisdictions, it has been suggested that the USA enact a federal marine insurance Act or that the American Law Institute undertake to produce a Restatement of the law of marine insurance.<sup>232</sup> Professor Thomas Schoenbaum has argued that any new federal law of marine insurance should be based on the MIA (UK) but that the subjects of good faith and warranties should be 'addressed afresh' to remedy the divergence that exists in these areas between United Kingdom and American law.<sup>233</sup>

7.13 The Maritime Law Association of the United States is currently embarked on a project 'to collect, study and synthesize the case law and applicable state statutory law into a ... plain statement of the maritime law ... and settle those issues which are presently deemed unsettled and subject to interpretation and construction under the law of the several states'.<sup>234</sup> It has been suggested that courts in the USA appear to treat the owners of yachts and fishing vessels as 'consumers' rather than as business people, and provide a greater degree of protection against the impact of a strict application of marine insurance rules, such as those in relation to the doctrine of utmost good faith and breach of warranty.<sup>235</sup> At the conference of the Comité Maritime International (CMI) in February 2001

230 348 US 310, 1955 AMC 467 (1955).

231 See M Clarke 'The Marine Insurance System in Common Law Countries: Status and Problems' *Paper Marine Insurance Symposium Oslo 4-6 June 1998*; R Bocko et al 'Marine Insurance Survey: A Comparison of United States Law to the Marine Insurance Act of 1906' (1995) 20 *Tulane Maritime Law Journal* 5; T Schoenbaum 'The Duty of Utmost Good Faith in Marine Insurance Law: A Comparative Analysis of American and English Law' (1998) 29(1) *Journal of Maritime Law and Commerce* 1; T Schoenbaum 'Warranties in the Law of Marine Insurance: Some Suggestions for Reform of English and American Law' (1999) 23 *Tulane Maritime Law Journal* 1.

232 E Cattell 'An American Marine Insurance Act: An Idea Whose Time Has Come' (1995) 20 *Tulane Maritime Law Journal* 1; M Sturley 'Restating the Law of Marine Insurance: A Workable Solution to the Wilburn Boat Problem' (1998) 29(1) *Journal of Maritime Law and Commerce* 41.

233 T Schoenbaum 'Marine Insurance' (2000) 31 (2) *Journal of Maritime Law and Commerce* 281, 291.

234 E Cattell 'Some Thoughts on Disclosure, Good Faith and Warranties in Current American Maritime Law' *Paper Tulane/BMLA London Seminar May 9-10 2000*.

235 Ibid.



Graydon Staring said that the issue of reform of the US law of marine insurance had been raised by individuals and interested groups rather than with the endorsement of the US Maritime Law Association.<sup>236</sup> He noted that it was unlikely that formal legislative reform would be undertaken at a federal level and warned against the enactment of state legislation that varied from one state to the next. He added that the US Maritime Law Association held the view that formal international marine insurance reform by means of any type of international instrument was not appropriate at this stage.

7.14 Other countries which do not have legislation based on the MIA (UK) have nevertheless been influenced by English law. For example, in Japan standard contractual clauses in marine insurance contracts are based on Institute clauses and hence are influenced by English law.

This is not because English law is perceived as anything like perfect but because it is recognised that marine insurance law is international and English law is widely applied at least in substance.<sup>237</sup>

7.15 It must also be borne in mind that United Kingdom and Australian common law vary in important respects that affect the application and interpretation of marine and non-marine policies alike. One important example is the doctrine developed in *Trident General Insurance Co Ltd v McNiece Bros Pty Ltd*,<sup>238</sup> which has no equivalent in the United Kingdom. Other differences relating to the inability of insurers to proceed by way of subrogation against one co-insured for damage caused to another co-insured were discussed in *Woodside Petroleum Development Pty Ltd v H & R-E & W Pty Ltd*.<sup>239</sup>

7.16 It is clear, therefore, that, influential as it is, English law is only the original core of the law of marine insurance from which there has been divergence that in particular cases will produce different outcomes in different jurisdictions. Nevertheless, the interest in maintaining a continuing link with UK law and overseas norms generally does act as a constraint on reform of the MIA.

## Civil code countries

7.17 While the common law countries have broadly similar marine insurance law and practice, the public and private legislation relating to marine insurance in civil

236 G Staring, US representative, International Working Group on Marine Insurance *Report to Plenary Session of the CMI* Singapore 16 February 2001.

237 M Clarke 'The Marine Insurance System in Common Law Countries: Status and Problems' *Paper* Marine Insurance Symposium Oslo 4–6 June 1998.

238 (1987) 4 ANZ Ins Cas ¶74–674; (1987) 8 NSWLR 270 (NSWCA); (1988) 165 CLR 107 (HC). The principle originally enunciated in *Trident* is that a person who, though not a party to a public liability insurance policy and not paying premium, falls within the class of persons expressed to be insured by it, may enforce the indemnity for which the policy provides. It has been subsequently expanded to cover other forms of insurance: *Barroora Pty Ltd v Provincial Insurance (Aust) Ltd* (1992) 26 NSWLR 170.

239 (1997) 10 ANZ Ins Cas ¶61–395 (Anderson J); (1999) 20 WAR 380 (WA Full Court).

code countries produces quite different regimes.<sup>240</sup> The marine insurance legislation in civil code countries is usually contained in general insurance contracts legislation or in commercial codes rather than in legislation applying specifically to marine insurance. Marine insurance legislation tends to be directory only and to preserve freedom to contract, subject to general contract principles relating to illegal and unfair contracts.

7.18 For example, Norway has legislation which regulates contracts of insurance generally, but there are exceptions concerning the insurance of commercial activity involving ships under 15 metres in length and the international carriage of goods, where complete contractual freedom is preserved.<sup>241</sup> Germany has a general insurance law which deals with non-marine insurance, including land transport insurance. One of the main aims of that legislation was ‘to protect the individual insured’ but marine insurance is subject only to the general laws of contract.<sup>242</sup>

7.19 Sweden, Denmark and France all have general insurance contracts legislation which contains provisions applicable both to insurance generally and to marine insurance in particular. However, most of the provisions relating to marine insurance are directory only.<sup>243</sup>

7.20 The law of marine insurance in many civil code jurisdictions must be understood by reference to standard contractual terms as well as to any relevant legislation. These standard terms include those provided in the Norwegian Marine Insurance Plan and the German General Rules of Marine Insurance (known as the ‘ADS’).<sup>244</sup>

7.21 There are many significant differences in the law of marine insurance between civil and common law jurisdictions. These include the following.

240 This summary of civil code regimes is not intended to be comprehensive, but is presented simply to illustrate some of the differences both between civil code and common law jurisdictions and among the laws in European civil code countries. This summary is drawn in large part from T-L Wilhelmsen ‘The Marine Insurance System in Civil Law Countries — Status and Problems’ *Paper Marine Insurance Symposium Oslo 4–6 June 1998* and T-L Wilhelmsen ‘Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire’ in *CMI Yearbook 2000 Comité Maritime International, Antwerp 2000*, 332.

241 Insurance Contracts Act 1989 (Norway): see S Derrington ‘The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform’ *Ph D thesis University of Queensland November 1998*, 69-70; T-L Wilhelmsen ‘Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire’ in *CMI Yearbook 2000 Comité Maritime International, Antwerp 2000*, 332, 333.

242 T Remé ‘Duty of Disclosure: Scope of the Duty and Sanctions for Breach’ *Paper Marine Insurance Symposium: Oslo 4–6 June 1998*.

243 Insurance Contracts Act 1927 (Sweden); Insurance Contracts Act 1930 (Denmark); Insurance Contracts Act 1967 (France) (Code des Assurances). However, some significant provisions of these Acts are mandatory, including those concerning the duties of disclosure and alteration of risk: T-L Wilhelmsen ‘Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire’ in *CMI Yearbook 2000 Comité Maritime International, Antwerp 2000*, 332, 334.

244 *Allgemeine Deutsche See-versicherungsbedingungen*.

- The laws of civil code countries do not recognise the special status of warranties as contractual terms requiring strict compliance.<sup>245</sup> For example, under Scandinavian laws, a breach by an insured of any term of a contract of marine insurance entitles the insurer to avoid liability if and only to the extent that the breach is both material to and causative of the loss.
- The laws of civil code countries have no equivalent to the duty of good faith in relation to insurance contracts, although some manifestations of the common law duties, notably the duty of disclosure, are commonly regulated.<sup>246</sup>
- The laws of civil code countries provide remedies for breach of the duty of disclosure, but these are generally more lenient towards the insured than those at common law.<sup>247</sup>
- The laws of civil code countries recognise a general concept of alteration of risk that has no direct equivalent at common law although elements that are covered under the concept of alteration of risk in the civil code countries are found in provisions of the MIA dealing with the duty of disclosure and the concept of warranties.<sup>248</sup>

7.22 The law relating to marine insurance contracts also differs significantly among civil code jurisdictions. These include differences in laws defining the scope of the duty of disclosure and sanctions for breach of duties of disclosure,<sup>249</sup> the scope of the concept of alteration of risk and related sanctions.<sup>250</sup>

## International reforms and harmonisation of national laws

7.23 This review occurs at a time when the question of reform to or harmonisation of marine insurance law and practice and insurance law generally is being considered overseas and at an international level in various forums.

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245 J Hare 'The Omnipotent Warranty: England v The World' *Paper International Marine Insurance Conference University of Antwerp November 1999*. See also para 9.44–9.48 below.

246 T-L Wilhelmsen 'Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire' in *CMI Yearbook 2000* Comité Maritime International, Antwerp 2000, 332, 347, 373. See also para 10.66–10.68.

247 While the remedies available differ between civil code jurisdictions, in none of these jurisdictions is rescission invariably available as a remedy as it is in the common law jurisdictions. See *ibid* 332, 357–69. See also para 10.109–10.112.

248 T-L Wilhelmsen 'Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire' in *CMI Yearbook 2000* Comité Maritime International, Antwerp 2000, 332, 382–83. See also para 9.44–9.48.

249 See para 10.66–10.68 and 10.109–10.112.

250 T-L Wilhelmsen 'Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire' in *CMI Yearbook 2000* Comité Maritime International, Antwerp 2000, 332.

### The Comité Maritime International

7.24 At present, the Comité Maritime International (CMI) is the most relevant forum in which the international harmonisation of marine insurance law is being examined. The CMI is a non-governmental international organisation, the object of which is to contribute to the 'unification of maritime law in all its aspects'.<sup>251</sup> Its members include the maritime law associations of over 50 countries, such as the Maritime Law Association of Australia and New Zealand (MLAANZ).

7.25 In June 1998 the CMI, the Norwegian Maritime Law Association and the Scandinavian Institute of Maritime Law convened a symposium on marine insurance law in Oslo. This symposium considered whether the CMI should support the development of an international convention or a model law on the subject of marine insurance. In his summary of the conference proceedings, the President of the CMI, Mr Patrick Griggs, concluded that neither an international convention nor a model law was achievable or desirable.<sup>252</sup> The conference resolved instead that the CMI's contribution to harmonisation would be to undertake a detailed survey of various aspects of marine insurance law so that the results of this study could or should be taken into account by countries reviewing marine insurance law.<sup>253</sup>

7.26 A conference summary stated that the aspects of marine insurance law to be examined included insurable interests; insured value and the time at which the subject of insurance is to be valued; ordinary wear and tear (inherent vice); inadequate maintenance and fault in design, construction or material; duty of disclosure before and during the currency of cover; consequences of loss of class, unseaworthiness and breach of safety regulations; warranties: express and implied, consequences of breach and alteration of risk; change of flag, ownership or management; misconduct of assured during the period of cover; responsibility of the insured for the conduct of others; the scope of the duty of good faith; and management issues, including the International Ship Management Code.<sup>254</sup> Many, though not all, of these areas have been examined by the Commission in preparing this report.

7.27 The CMI established an international working group on harmonisation of marine insurance chaired by Dr Thomas Remé of Germany. The working group prepared a questionnaire to obtain input from national maritime law associations. An important focus of the questionnaire was to establish, in relation to each

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251 <http://www.comitemaritime.org> (4 May 2000).

252 P Griggs 'Summing Up: Towards Harmonisation of Marine Insurance Conditions' *Paper Marine Insurance Symposium Oslo June 1998*.

253 R Salter *Correspondence* 9 March 2000.

254 P Griggs 'Summing Up: Towards Harmonisation of Marine Insurance Conditions' *Paper Marine Insurance Symposium Oslo June 1998*.

jurisdiction, what, if any, mandatory or directory rules constrain freedom to contract to allow consideration of whether public or private legislation would be needed to promote harmonisation.<sup>255</sup> Analysis of the questionnaire responses was to form the basis for CMI recommendations on steps towards harmonisation of marine insurance law and practice.

7.28 As part of this work, a paper was presented by Professor Trine-Lise Wilhelmsen of the Scandinavian Institute of Maritime Law at a CMI/Spanish Maritime Law Association colloquium held in Toledo, Spain in September 2000.<sup>256</sup> This paper considered the legislation and standard marine insurance clauses of 26 countries in relation to duties of disclosure, the duty of good faith, alteration of risk and warranties. A report on these issues was published in the materials for the CMI conference in Singapore in February 2001.<sup>257</sup> The International Working Group also prepared a discussion paper identifying a list of the problem areas to be addressed in any comprehensive move towards harmonisation of marine insurance law.<sup>258</sup>

7.29 The Singapore conference resolved to continue the CMI's evaluation of the national laws of marine insurance with the aim of identifying issues of marine insurance that are worthy and capable of harmonisation and those that ought best to be left to national interpretation. However, the ultimate product of the CMI's work remains unclear. In his report to the plenary session of the CMI, the Chairman of the Singapore sessions, Professor John Hare, concluded that the end result

may take the form of a set of CMI approved guidelines which could help countries engaged in their own initiatives to rewrite their laws of marine insurance; or a set of Rules on Certain Issues of Marine Insurance such as may be incorporated into marine insurance contracts in a way which will provide more certainty about the law to which those contracts may be subject; or even contractual terms devised in consultation with the industry which may address some of the problems identified. At this stage, the only end result which is not considered feasible or desirable is a formal convention.<sup>259</sup>

7.30 The Commission has been greatly assisted by the work of the CMI. This work has produced a wealth of comparative law material and given the Commission a broader view of international marine insurance law than may have otherwise been possible. The Commission understands that it is hoped that CMI

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255 T Remé 'The CMI Working Group on Marine Insurance/Challenges for the Future' in M Huybrechts, E Van Hooydonk and C Dieryck (eds) *Marine Insurance at the Turn of the Millennium* vol I Intersentia Antwerp 1999, 399.

256 T-L Wilhelmsen 'Issues of Marine Insurance: Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties' *Unpublished paper* for CMI, September 2000.

257 T-L Wilhelmsen 'Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire' in *CMI Yearbook 2000* Comité Maritime International, Antwerp 2000, 332.

258 International Working Group on Marine Insurance *Discussion Paper* CMI Singapore February 2001.

259 J Hare 'Marine Insurance: The CMI Review Initiative' in *CMI Yearbook 2000* Comité Maritime International, Antwerp 2000, 325, 328.

guidelines or other end product will be circulated to national maritime law associations and other interested parties for comment before being taken forward for consideration and possible adoption by the Assembly of the CMI at its next conference in 2004.<sup>260</sup>

### **Review of Institute Clauses**

7.31 The UK Joint Hull Committee is currently reviewing the wording of the Institute hull clauses with a view to completely rewriting them from scratch rather than simply working with the existing versions.<sup>261</sup>

### **Review of insurance law**

7.32 This review occurs at a time when the question of possible reform to insurance law generally is being considered in a number of other jurisdictions, including the United Kingdom and within the European Union.

7.33 Apart from the MIA (UK) and various compulsory insurance acts covering areas such as motor vehicles and employers liability, insurance law in the United Kingdom has not been codified. Changes to insurance law in the United Kingdom are thought by many organisations and individuals to be well overdue.

It really is time to ask the question whether legal decisions made some 250 years ago are really suitable to determine the rights and obligations of parties to insurance contracts in 2001?<sup>262</sup>

It must be time for a change and a new Insurance Contracts Act that will clearly define the duties of all parties to insurance contracts.<sup>263</sup>

There are numerous areas where reform would be useful and some where it is essential.<sup>264</sup>

7.34 The UK Law Commission published a report in 1980 entitled *Insurance Law: Non-disclosure and Breach of Warranty*. This report stated that the law of non-disclosure and breach of warranty was undoubtedly in need of reform and that such reform had been too long delayed. However, the recommendations for reform in that report have never been implemented.<sup>265</sup>

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260 Ibid.

261 Ibid.

262 J Hanson 'Is There a Need for Legislative Reform of Insurance Contracts?' *Insurance Day* 21 February 2001, 9.

263 D Cole 'Old Law Unfit for a New Century' *Legal Week* 7 September 2000.

264 A Longmore 'An Insurance Contracts Act for a New Century?' *Speech* Pat Saxton Memorial Lecture Trustees of the British Insurance Law Association Trust London 5 March 2001.

265 Ibid.

7.35 The feeling prevails in some quarters that the courts are hamstrung by centuries of precedent or, conversely, are engaged in constant re-interpretation of the law, leading to uncertainty which could be remedied by some legislative reform.

7.36 The City of London Solicitors' Company published a paper on 12 December 2000 which supported reform to the test of materiality and the consequences of non-disclosure and misrepresentation.<sup>266</sup>

7.37 The British Insurance Law Association (BILA) has established a committee on Reform of Insurance Contract Law. The committee's inaugural meeting was in January 2001. A number of sub-committees have been established to address specific areas of reform, one of which is marine insurance. It is thought that the BILA initiative seeks primarily to address areas of perceived harshness within the law such as utmost good faith and breach of warranty.<sup>267</sup> In addition to this the UK Department of Trade and Industry will address insurance contract law as part of a wider consideration and possible codification of UK commercial law.

7.38 European Union initiatives include the following.

- The 'Alpine professors' initiative, which is a reform group consisting of professors from various European academic institutes. The group is attempting to establish common principles of European insurance contract law through studies of national legislation of EU members, Switzerland and relevant EEA members.<sup>268</sup> The aim is to create a Model Law which may be of use to legislators both at a national and EU level.
- A research group at the Max Planck Institute in Hamburg which is considering European insurance law as part of a larger project: the drafting of a European Civil Code.

7.39 There are also a number of current initiatives addressing the possible reform of reinsurance at a European level.

7.40 All of these reform or harmonisation initiatives are matters that the Australian government and marine insurance industry should continue to monitor to consider whether and to what extent any further reform of the MIA or marine insurance law generally should be entertained in the light of the conclusions of these exercises and any consequent reforms to marine insurance law and practice.

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266 The City of London Solicitors' Company *Proposals for Reform of the Doctrine of Utmost Good Faith in Insurance Contract Law* 12 December 2000 <http://www.citysolicitors.org.uk> (27 March 2001).

267 International Underwriting Association of London *Correspondence* 6 March 2001.

268 Ibid. The Project Group's website, 'Restatement of European Contract Law' is at <http://zivilrecht2.uibk.ac.at/restatement/portal/html>.





## 8. The coverage of the *Marine Insurance Act*

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### Introduction

8.1 Australia has several insurance law regimes. Contracts of marine insurance are governed by the *Marine Insurance Act 1909* (MIA) and may cover mixed sea and land risks. Most non-marine insurance is governed by the *Insurance Contracts Act 1984* (Cth) (ICA). Contracts of insurance governed by the ICA include those covering risks in respect of commercial aircraft and all forms of land transport. Specific statutory regimes govern workers compensation, seamen's rehabilitation, motor vehicle accidents, health insurance and so on.

8.2 This chapter compares the characteristics of contracts of insurance to which the MIA applies with those to which the ICA applies, and examines some uncertainties in the respective application of these Acts.

8.3 The question whether the MIA or the ICA applies to a particular contract of insurance, while not often arising in practice, is crucial. There are many significant differences between the MIA and the ICA, especially those examined in the following chapters.<sup>269</sup> They relate not only to the content of the contracts of insurance and the interpretation and effect of contractual terms but also the way in which business is conducted. These differences may lead to very different results for the parties where indemnity is claimed under contracts of insurance.

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<sup>269</sup> eg in relation to the nature of insurance warranties, the scope of the duty of disclosure and the requirement for an insurable interest.

## **What contracts of insurance does the MIA apply to?**

8.4 Generally, the provisions of the MIA apply to ‘contracts of marine insurance’. Section 7 of the MIA defines a contract of marine insurance as follows.

7. A contract of marine insurance is a contract whereby the insurer undertakes to indemnify the assured, in manner and to the extent thereby agreed, against marine losses, that is to say, the losses incident to marine adventure.

8.5 Only losses incident to marine adventures are covered in marine insurance contracts. There is a marine adventure where loss, damage or liability may be incurred by reason of maritime perils.<sup>270</sup> The MIA defines maritime perils as follows.

‘Maritime perils’ means the perils consequent on, or incidental to, the navigation of the sea, that is to say, perils of the seas, fire, war perils, pirates, rovers, thieves, captures, seizures, restraints, and detentions of princes and peoples, jettisons, barratry, and any other perils, either of the like kind, or which may be designated by the policy.<sup>271</sup>

8.6 This definition is not exhaustive. It permits other similar perils to be covered. Quite different perils may also be covered if designated by the policy (though this must be read subject to the rest of the Act).

8.7 Section 9 of the MIA defines the subject matter of marine insurance.

9(1) Subject to the provisions of this Act, every lawful marine adventure may be the subject of a contract of marine insurance.

(2) In particular there is a marine adventure where:

- (a) any ship, goods, or other movables are exposed to maritime perils. Such property is in this Act referred to as ‘insurable property’;
- (b) the earning or acquisition of any freight, passage money, commission, profit, or other pecuniary benefit, or the security for any advances, loan, or disbursements, is endangered by the exposure of insurable property to maritime perils;
- (c) any liability to a third party may be incurred by the owner of, or other person interested in or responsible for, insurable property, by reason of maritime perils.

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270 MIA s 9 (2).

271 MIA s 9. ‘Perils of the sea’ are also mentioned in other sections of the MIA: MIA s 55 (deviation and delay), MIA s 61 (included and excluded losses), MIA s 65 (effect of transshipment), MIA s 66 (constructive total loss), MIA s 70 (particular average loss), MIA s 71 (salvage charges), MIA s 72 (general average loss) and MIA sch 2.

8.8 The MIA requires the subject matter of a contract of marine insurance to be ‘designated in a marine policy with reasonable certainty’.<sup>272</sup> At least the following subject matter is insurable under a marine policy: ships; goods; movables; freight; profits; commissions; disbursements; wages; ventures undertaken by a company; and third party liability.<sup>273</sup>

8.9 Contracts of marine insurance may cover some non-marine risks and subject matter. Section 8 of the MIA provides for contracts of marine insurance to cover mixed sea and land risks. It states that

8(1) A contract of marine insurance may, by its express terms, or by usage of trade, be extended so as to protect the assured against losses on inland waters or on any land risk which may be incidental to any sea voyage.

(2) Where a ship in course of building, or the launch of a ship, or any adventure analogous to a marine adventure, is covered by a policy in the form of a marine policy, the provisions of this Act, in so far as applicable, shall apply thereto; but, except as by this section provided, nothing in this Act shall alter or affect any rule of law applicable to any contract of insurance other than a contract of marine insurance as by this Act defined.

8.10 It is clear that the non-marine risks which s 8(1) permits to be covered by a policy of marine insurance are incidental to the sea voyage and that the maritime risks therefore remain the primary focus of contracts of marine insurance.

### **What contracts of insurance does the ICA apply to?**

8.11 The ICA applies to all contracts of insurance and proposed contracts of insurance, the proper law of which is the law of an Australian state or territory<sup>274</sup> unless excluded by the Act.

8.12 Section 9 provides a number of exceptions to the application of the Act. The ICA does not apply to contracts to or in relation to which the MIA applies.<sup>275</sup> However, the ICA does apply to the insurance of pleasure craft, which in 1998 was excluded from the MIA and brought within the ICA (see paragraph 8.14–8.16).<sup>276</sup>

8.13 The ICA specifically excludes contracts of health insurance, insurance relating to workers’ compensation and third party injury motor vehicle insurance from its application.<sup>277</sup> Some of these forms of insurance, such as workers’ compensation and third party injury motor vehicle insurance, are governed by other

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272 MIA s 32(1).

273 S Hodges *Cases and Materials on Marine Insurance Law* Cavendish London 1999, 83.

274 ICA s 8(1).

275 ICA s 9(1)(d).

276 ICA s 9A inserted by the *Insurance Laws Amendment Act 1998* (Cth).

277 ICA s 9.

comprehensive state or federal legislative schemes.<sup>278</sup> Reinsurance is also specifically excluded by the ICA and is governed by the common law.

### **Pleasure craft and the 1998 amendments**

8.14 In 1998, the ICA was amended by the *Insurance Laws Amendment Act 1998* (Cth) to exclude pleasure craft insurance from the operation of the MIA. A ‘pleasure craft’ is defined in the ICA to mean a ship which is owned by individuals and used wholly for recreational or sporting activities otherwise than for reward. For these purposes, any minor, infrequent or irregular use for other activities is ignored.<sup>279</sup>

8.15 As stated, the explanatory memorandum to the amending legislation noted that the MIA was ‘primarily designed to cover insurance contracts relating to the international carriage of goods’ and the intention was that individuals who owned pleasure craft should receive the consumer protection benefits of the ICA.<sup>280</sup>

8.16 This reform essentially removed from the MIA those insurance contracts that most needed consumer protection. Insurers and others have told the Commission that in practice prior to this reform ICA principles were already being applied by the market to pleasure craft insurance.<sup>281</sup> It would appear that the only area of non-commercial insurance now covered by the MIA is the insurance of personal effects or non-commercial goods carried by sea. This is discussed in detail in paragraph 8.24–8.29.

### **Small fishing and other commercial vessels**

8.17 In the Discussion Paper, the Commission observed that while most marine insurance transactions are ‘business-to-business’ and many insureds have the professional services of a broker, there might be sectors of the marine insurance market which could benefit from the consumer protection provisions of the ICA. In any event, the law should not rely on assumptions about the professional skills of insurance intermediaries (which must be taken to be variable) to remedy faults in the statute.

278 eg third party motor vehicle: *Motor Accidents Act 1988* (NSW); *Transport Accident Act 1986* (Vic); workers compensation: *Workers Compensation Act 1987* (NSW); *Accident Compensation Act 1985* (Vic); *Safety Rehabilitation and Compensation Act 1988* (Cth); *Seafarers Rehabilitation and Compensation Act 1992* (Cth). The insurance of commercial aircraft between 1986 and 1997 came under the common law as it was outside the ICA: *Statute Law (Miscellaneous Provisions) No 1 Act 1986* (Cth). The insurance of commercial aircraft is now once more covered by the ICA: *Financial Laws Amendment Act 1997* (Cth).

279 ICA s 9A.

280 Explanatory memorandum: Insurance Laws Amendment Bill 1997. The memorandum also noted that the MIA had not been amended since its enactment due to ‘international constraints’.

281 Legal practitioners *Consultation* Sydney 1 May 2000; Insurers and legal practitioners *Consultation* Sydney 15 May 2000.

8.18 In particular, the Commission asked whether the insurance of small fishing and other commercial vessels, perhaps defined by reference to usage or a tonnage or other size limit, should be excluded from the MIA and made subject to the ICA.

8.19 Fishing vessels insured under the MIA range from large offshore trawlers and long liners, which may be part of major national or international fishing fleets, to oyster punts and small harbour or coastal fishing vessels. Including the insurance of fishing vessels (or other small commercial vessels) under the ICA could require reference to a tonnage or other size limit, below which the insurance of the vessel would be subject to the ICA, not the MIA. Alternatively, the distinction might be based on the usage of vessels.

8.20 There was little support in submissions or consultations for small fishing and other commercial vessels to be made subject to the ICA. It was noted that shipowners, even of small vessels, are commonly advised by brokers and, like other small businesses, have access to advice and assistance from trade organisations.<sup>282</sup> While some in the fishing industry could see benefit in ICA coverage,<sup>283</sup> others consulted by the Commission considered that with ICA coverage fishing vessel operators would find it even more difficult to obtain affordable insurance cover than they do at present.<sup>284</sup>

8.21 There may be some features of the MIA that, as compared to the ICA, favour the interests of fishing and small commercial vessel owners. For example, the MIA provisions on total constructive loss and abandonment expressly allow the insured to elect to treat a constructive total loss as a partial loss.<sup>285</sup> The Commission understands that shipowners often prefer to repair vessels rather than abandon them to the insurer even though the cost of repair is more than the cost of replacement because 'good second hand tonnage is hard to come by'.<sup>286</sup>

8.22 The Commission considers that the main reason for including the insurance of fishing vessels under the ICA would be to address any perceived unfair treatment of fishing vessel operators by insurers relying on breaches of warranty to deny liability for claims where the breach is trivial or not causally connected to the loss.<sup>287</sup> However, whether actual or perceived, any such unfairness may be avoided by reform of the law relating to marine insurance warranties as recommended in this report.<sup>288</sup>

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282 Insurers *Consultation* Melbourne 6 June 2000; Insurers and broker *Consultation* Sydney 27 March 2000.

283 Queensland Commercial Fishermen's Organisation *Consultation* Brisbane 12 May 2000.

284 MLAANZ *Submission 12*; Broker *Consultation* Perth 23 November 2000.

285 MIA s 67.

286 Broker *Consultation* Perth 23 November 2000.

287 See para 9.18–9.21.

288 See ch 9.

8.23 The Commission considers that the relevant point of distinction is the use of the vessels, not their size. Any demarcation based on dimensions would inevitably be arbitrary, not supported by any argument of principle, and is difficult, if not impossible, to state without causing problems in relation to vessels that fall just one side of the line or the other. Accordingly, the Commission does not recommend any amendment to move the insurance of fishing or small commercial vessels from the MIA to the ICA. In any event, as is discussed elsewhere in this report, the most important criterion is the function of the insured vessel, which is easy to determine, is not arbitrary and goes to the heart of the insured adventure.

### **Carriage of domestic and household goods**

8.24 In the Discussion Paper the Commission noted that insurance of the household contents of people moving home is one area of MIA coverage that may involve insured parties who lack relevant market experience or expertise.

8.25 In its submission the Insurance Council of Australia suggested that carriage of household goods should be excluded from the MIA and placed within the ambit of the ICA. The Council noted that some member insurance companies already write contracts relating to sea carriage of household goods as if covered by the ICA.<sup>289</sup>

8.26 The majority of people moving house do so by road or rail and already receive the consumer protections of the ICA. In addition, those relocating overseas often have their transit insurance paid by their employer, again viewed as a business-to-business deal by the industry.<sup>290</sup> Nevertheless, the Commission considers that the distinction between the MIA and the ICA based on the nature of the transactions governed would be usefully enhanced by the exclusion of all carriage of domestic or household goods from the ambit of the MIA and recommends such a change. Such an amendment would echo the changes in 1998 in relation to pleasure craft. For that reason, the Commission recommends that the amendment be to the ICA by the insertion of a new s 9B rather than by amendment to the MIA itself (see recommendation 2 below).

8.27 One logical starting point for the drafting of such an exclusion is s 74(3)(a) of the *Trade Practices Act 1974* (Cth). This provision excludes certain implied warranties in relation to the supply of services from contracts for ‘the transportation or storage of goods for the purposes of a business, trade, profession or occupation carried on or engaged in by the person for whom the goods are transported or stored’.

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289 Insurance Council of Australia *Submission 11*.

290 Insurers *Consultation* Melbourne 6 June 2000; Insurers and broker *Consultation* Sydney 27 March 2000.

8.28 The point of selecting s 74(3) lies not in the purpose of that provision but because it furnishes an example of statutory drafting of the relevant concept. However, the adoption of a particular form of wording from an existing statutory provision will bring with it judicial consideration of that wording that is applicable in the new circumstances. It is therefore important to note that the High Court considered the scope of s 74(3)(a) in *Wallis v Downard-Pickford (North Queensland) Pty Ltd*.<sup>291</sup> It held that a contract for the transportation of household goods made by the Queensland Commissioner of Police on behalf of a transferred policeman was not covered by s 74(3) because the transportation of the goods was not an ordinary incident of the Commissioner's occupation<sup>292</sup> and the purpose of the transportation was not a private or domestic one.<sup>293</sup>

8.29 As a consequential drafting matter, the Commission suggests that MIA s 7, which defines contracts of marine insurance, be made expressly subject to ICA s 9A and the proposed s 9B. This is probably not strictly necessary but it provides an express indication within the MIA of important restrictions on its scope found in other legislation.

### **The consequences of uncertainty**

8.30 Situations may arise where one or both parties assume that an insurance contract is one of marine insurance, and therefore subject to the MIA, when in fact the contract is governed by the ICA. Alternatively, they may not turn their minds to the question, particularly if they are not expert in insurance law. Uncertainty in relation to the respective coverage of the MIA and ICA may have significant legal and practical consequences. As many of the provisions of the ICA extensively modify the common law principles on which the MIA is based in favour of insured parties, these legal and practical consequences are most likely to prejudice the insurer.

8.31 Where the ICA rather than the MIA governs a contract, the consequences for an insurer may include the following.

- The insurer may be unable to avoid liability under a contract where the insured has failed to disclose, or has misrepresented, a material circumstance, unless the non-disclosure is fraudulent.

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291 (1994) 179 CLR 388.

292 Ibid 400 (per Toohey and Gaudron JJ).

293 Ibid 393 (per Deane and Dawson JJ), 401 (McHugh J).

- The insurer may be unable to rely on an insured's breach of a warranty or other contractual term to discharge it from all liability for subsequent loss, unless the breach caused the loss.
- The insurer may be liable under the contract where the insured has suffered economic loss notwithstanding that the insured did not have a strict insurable interest in the insured property.

8.32 These and other consequences flow directly from differences between the treatment of these legal issues in the ICA and the MIA, as discussed in later chapters of this report.

8.33 There are many other provisions of the ICA that, if breached, may leave the insurer unable to rely on or enforce the provisions of a contract written as if it were subject to the MIA.<sup>294</sup> The ICA provides that certain types of provisions in contracts of insurance are void.<sup>295</sup> Some provisions may not be relied on where the insurer has not clearly informed the insured in writing of the nature and effect of those provisions.<sup>296</sup> In some circumstances, non-compliance with the ICA may result in fines.<sup>297</sup> Contracting out of the ICA to the prejudice of a person other than the insurer is prohibited.<sup>298</sup>

8.34 Except where the contract provides for the application of foreign law (where this is permissible), it seems that either the MIA or the ICA must apply to the whole of any contract of general insurance not covered by another statutory scheme. Neither Act appears to contemplate the splitting of a contract or policy between them<sup>299</sup> although the MIA was, of course, drafted long before the ICA, or anything like it, was thought of. The ICA, however, was drafted with clear knowledge of the MIA but s 9 and 9A, for example, refer to 'contracts' and 'proposed contracts'. These provisions do not anticipate that the ICA or MIA might apply to severable portions of contracts.<sup>300</sup>

294 eg ICA s 39 (Instalment contracts of general insurance); s 46 (Pre-existing defect or imperfection); ICA s 65 (Subrogation to rights against family etc); s 66 (Subrogation to rights against employees).

295 eg ICA s 38 (Interim contracts of insurance); s 43 (Arbitration provisions); s 45 ('Other insurance' provisions).

296 eg ICA s 37 (Notification of unusual terms); s 44 (Average provisions).

297 ICA s 40 (Certain contracts of liability insurance); s 73 (Insurance arranged in connection with supply of goods and services); s 74 (Policy documents to be supplied on request); s 75 (Reasons for cancellation etc to be given).

298 ICA s 52.

299 The Commission has heard anecdotally that others may take a different view but has not seen any legal advice, or received any submission, to this effect.

300 Alexander Street SC suggested that the potential for both the MIA and ICA to apply to a contract should be expressly removed by statute: A Street *Submission 15*.



8.35 Therefore, in some circumstances it may be uncertain whether a contract of insurance is one to which the MIA applies. This uncertainty is most apparent in relation to contracts of insurance which cover both marine and non-marine activities such as multimodal transit and activities located on the foreshore.

8.36 As noted above, the MIA allows a marine policy to cover losses on inland waters or on land which are incidental to any sea voyage. However, in some cases it may be unclear whether a non-marine risk covered by a contract is simply 'incidental' to the marine risks covered or is such a significant component of the cover that the subject matter insured is not 'substantially' a marine adventure. If the latter situation applies, the ICA rather than the MIA will govern the contract. The ICA is in effect the default regime as it will apply unless the contract covers risks which are substantially marine. Parties to insurance contracts where this is in doubt (especially insurers), acting prudently, should assume that the ICA applies.

8.37 This complication does not arise to the same extent in other jurisdictions without legislation equivalent to the ICA. The relevant provisions of the MIA (UK), for example, are expressed no differently from the Australian Act. The MIA (UK) can, therefore, have no greater scope of operation. However, contracts of general insurance governed by UK law but not covered by the MIA (UK) are covered by the common law. As the differences between the MIA (UK) and the UK common law are in most situations negligible, this threshold question is largely immaterial. Furthermore, contracts covered by UK law can contractually incorporate or apply the MIA (UK), thus removing uncertainty about coverage. In Australia this mechanism is not available as ICA s 45 prevents parties to contracts governed by the ICA from contracting out of that Act on terms more favourable to insurers (such as are found in the MIA).

## **Cargo insurance**

8.38 One focus of this uncertainty arises in the context of cargo insurance. More than one form of carriage is often involved in the transit of goods. While some carriage on inland waterways and mixed land and sea risks are contemplated by the MIA, the use of containerisation and travel by air have increased the incidence of transporting cargo by several different modes of transport. Many cargo insurance contracts cover risks relating to several forms of transport either expressly, by implication or because of the breadth of their terms. This can create uncertainty about which legislative regime applies to the contract of insurance. Depending on its construction, the contract may be subject to either the MIA or the ICA. Only one regime will apply to the contract of insurance but different regimes could apply (with different claims outcomes) if separate policies had been taken out.

8.39 The decisive question in determining whether a policy covering mixed sea and land risks is a contract of marine insurance is whether the subject matter insured is ‘substantially’ a marine adventure.<sup>301</sup> For example, in *Leon v Casey*<sup>302</sup> the insurance of cargo warehouse-to-warehouse carried by land from Cairo to Alexandria and then by sea to Jaffa was held to be a marine policy. Francis Marks and Audrey Balla state that ‘the permitted extension to land risks incidental to a sea voyage will only apply where the sea voyage is the dominant activity’.<sup>303</sup>

8.40 The question has not arisen frequently in the courts. The only reported Australian case in which mixed risks were at issue was *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur (Australia) Ltd*.<sup>304</sup> This case involved the insurance of stock in trade from a variety of risks including ‘transit risk — road, rail, sea, air, parcel, post’. This case is of limited assistance as no evidence was led to illustrate the importance of carriage of goods by sea in the context of the whole policy and the terms of the policy indicated that it was but one part of one section of the cover afforded. The High Court held that it could not be said that the policy, viewed in its entirety, indemnified the insured against losses that were substantially incidental to a marine adventure. This case indicates that a policy covering various modes of transport will be governed by the ICA if there is no evidence that sea transport predominates.

8.41 However, all that can be said with real certainty is that the marine component of the cover must be more important than the non-marine component in order for a policy to constitute a contract of marine insurance. How much more important that component needs to be in order for the policy to be ‘substantially’ one of marine insurance has not been established and is a question of fact in each case.

8.42 The Commission has been advised that one policy of insurance will sometimes cover all of an insured’s transport risks, including land transport within Australia (assumed by the parties to be governed by the ICA) and exports and imports (assumed by the parties to be governed by the MIA). In these circumstances, where land transport within Australia is in fact the most important component of the cover, a court may not be able to conclude that the contract is substantially one of marine insurance and the marine risks covered may therefore be governed by the ICA. It could be argued that, depending on how the policy is drafted, a court could split such a policy, in effect finding that there are two

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301 H Bennett *The Law of Marine Insurance* Clarendon Oxford 1996, 323.

302 [1932] 2 KB 576. In England, where there is no equivalent of the ICA, cases dealing with whether policies involving mixed land and sea transit are policies of marine insurance tend to arise where an order for ‘ship’s papers’ is being sought. An order for ship’s papers is an exceptional discovery procedure available only in actions on marine insurance policies: See *ibid* 320.

303 F Marks and A Balla *Guidebook to Insurance Law in Australia* 3rd ed CCH Sydney 1998, 561  
304 (1986) 160 CLR 226.

contracts. For the reasons discussed above (paragraph 8.34) the Commission doubts that this is possible but, even if it is, it is not an attractive solution to uncertainty about the governing law.

8.43 The coverage question in relation to cargo insurance becomes even more difficult where there is open or annual cargo cover.<sup>305</sup> As discussed in chapter 15, open or annual cover may not amount to a contract of marine insurance until each separate declaration of cargo is made. The cargo subject to each declaration may be governed by either the MIA or the ICA, depending on whether the cargo is being sent by air, land or sea. It may not be possible to determine whether the MIA or ICA should apply to the overall contract<sup>306</sup> until the end of the policy period when it will be apparent whether the risks covered predominantly related to sea, or air and land carriage. This uncertainty is most undesirable, not least because, as the ICA governs the way in which insurance business is done (such as notices to the insured), the legal regime governing the contract ought to be known before the business is commenced.

### Coverage problems in practice

8.44 In consultations, the Commission sought to establish the extent to which uncertainty about the coverage of the MIA has a practical effect on the conduct of insurance business in Australia.

8.45 While some insurers have agreed that uncertainty about the respective coverage of the MIA and the ICA may cause problems,<sup>307</sup> the Commission found it difficult to clearly establish how insurers and brokers in practice arrange insurance for mixed marine and non-marine risks. For example, it is unclear whether mixed cover requested by a prospective insured is commonly split into separate policies covering the marine and non-marine components or whether an assessment is made by the insurer and broker as to whether the policy as a whole is ‘substantially’ one of marine insurance and therefore should be written as MIA or ICA insurance.

8.46 One insurer advised that, where insurance of inland transit risks is included in a cargo policy also covering imports and exports by sea, the view is generally taken that marine risks are dominant and that the policy will therefore be subject to the MIA. However, because the inland cover might be construed as governed by

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305 Cargo open cover involves an agreement to provide insurance for all shipments of goods as agreed, subject to declaration by the insured at or about the time of shipment. An annual policy provides cover for all shipments of goods, as agreed, which commence during the annual period specified in the policy: see para 15.49.

306 This assumes that the open or annual cover itself can be regarded as a contract as opposed to an arrangement under which individual contracts are made at the time of each declaration under them.

307 Legal practitioners *Consultation* Sydney 1 May 2000; Insurers and legal practitioner *Consultation* Brisbane 11 May 2000.

the ICA, marine terminology (such as references to warranties) is avoided in that part of the policy wording. This insurer also advised that liability policies are seen as a ‘particularly grey area’ and are entered on the basis that either the MIA or ICA may apply to them.<sup>308</sup>

8.47 Whatever the practical effect of the apparent uncertainty, it does not seem that the issue has resulted in large numbers of disputes. There have been no reported cases on this issue since *Con-Stan*.<sup>309</sup> The dearth of case law is not surprising as only a small number of marine insurance cases ever reach the Australian courts. As Australia is the only common law jurisdiction with marine insurance legislation based on the MIA (UK) and legislation applying to non-marine insurance which extensively modifies common law principles, the question will rarely arise in other jurisdictions and, if it does, it would not have the same ramifications.

8.48 Different interpretations may be placed on the lack of evidence of dispute about the respective coverage of the MIA and ICA. One interpretation is that where insurers are in doubt about the legislative regime applicable, they are writing insurance as subject to the ICA and avoiding claims that terms contained in the contract are rendered void or overridden by the ICA. The legal problem may not be well appreciated by all insurers, brokers and insureds.

8.49 Whether insurance for mixed marine and non-marine risks is written as marine insurance or not may be a function of the type of insurance in which the insurer or broker specialises. In particular, in the area of cargo insurance there may be a tendency for parties to treat the insurance of all cargo in transit as marine insurance whether the cargo is carried by sea, air or land.<sup>310</sup> For this reason it is quite likely that situations may arise where an open or annual cargo cover is issued as if governed by the MIA, but under which all or most cargo is sent by air.<sup>311</sup>

### Reform options

8.50 The easiest solution might seem to be the fusion of the two regimes of insurance into one. In that case, the threshold question would not arise. However, to be effective, this fusion would have to remove all substantive distinctions between the two forms of insurance. If a dichotomy remains for any purpose, parties will still have to decide which category a given contract (or, possibly, part of a contract) falls into, though the frequency with which this issue arises might be reduced. There could be some advantage in characterising a contract as of one type

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308 P Grieve *Correspondence* 19 December 2000.

309 *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur (Australia) Ltd* (1986) 160 CLR 226.

310 D Luxford *Correspondence to AG's Dept* 4 September 1997.

311 *Advisory Committee meeting* 18 December 2000.

or the other for reasons unrelated to the risks covered. For example, at present policies of marine insurance are not subject to stamp duty in any Australian state or territory but other insurance policies are.<sup>312</sup>

8.51 The Commission has rejected the repeal of the MIA and the abolition of the distinction between marine and non-marine insurance as an overall solution (see paragraphs 3.12–3.23 and recommendation 1).

8.52 In the Discussion Paper, the Commission proposed that the MIA and the ICA should be amended to address uncertainties about their respective coverage in relation to insurance of mixed marine and non-marine transit risks, for example multimodal cargo transport, and ship repair and marina operations.<sup>313</sup>

8.53 The idea that uncertainties about coverage need to be addressed received support in submissions<sup>314</sup> but there was no consensus on the steps that should be taken. Some submissions agreed with the suggestion that s 6(1) of the Marine Insurance Act 1993 (Can) should be one starting point for reform.<sup>315</sup> This provision states

- 6(1) A contract of marine insurance is a contract whereby the insurer undertakes to indemnify the insured, in the manner and to the extent agreed in the contract, against
- (a) losses that are incidental to a marine adventure or an adventure analogous to a marine adventure, including losses arising from a land or air peril incidental to such an adventure if they are provided for in the contract or by usage of the trade; or
  - (b) losses that are incidental to the building, repair or launch of a ship.
- (2) Subject to this Act, any lawful marine adventure may be the subject of a contract.

8.54 Apart from the differences relating to inland waters discussed below (paragraph 8.85), the significant differences between s 6(1) of the Canadian legislation and MIA s 8(1) appear to be as follows.

- The Canadian provision states that a contract of marine insurance is a contract which covers losses incidental or analogous to a marine adventure, telescoping a number of provisions in the Australian MIA.
- The section expressly permits an ‘air peril’ incidental to a marine adventure to be insured against in a contract of marine insurance.

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312 See generally ch 3.

313 ALRC DP 63 draft proposal 13.

314 K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*; MLAANZ *Submission 12*.

315 K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*.

- The Canadian provision refers to repairs, which are discussed in paragraph 8.64 below.

8.55 The Commission recommends that, as with the Canadian Act, the MIA s 8(1) should be amended to include air risks incidental to a sea voyage (see recommendation 3 below).

8.56 While it provides some additional clarity and makes express reference to air perils, the Canadian provision does not remove the central uncertainty about when a non-marine risk ceases to be merely incidental to a marine adventure. A more radical solution to questions relating to the coverage of mixed risks by the MIA would be to create a comprehensive transport insurance regime outside the ICA that covers marine, aviation and other transport insurance (an MAT Act). There was significant support in submissions and consultations for amending the MIA to allow most or all international cargo insurance to be governed by the same regime (the MIA).<sup>316</sup> As discussed in more detail in chapter 3, the Commission concluded that, while such reform may be a goal for the longer term, it could not realistically be dealt with by this inquiry. There is no MAT legislation in any other common law country and no move towards any such legislation.

### **Conclusion on coverage of cargo insurance**

8.57 Clearly, a contract of marine insurance should be able to cover incidental non-marine risks. However, as discussed above, case law has established that these risks must not be such a significant component of the cover that the subject matter insured is not ‘substantially’ a marine adventure.

8.58 There are arguments for leaving this aspect of the MIA untouched. It may be too difficult to define in the legislation the dividing line between the MIA and the ICA with any greater degree of certainty. Insurers’ interests rather than those of the insured are likely to be adversely affected when parties mistakenly assume that the ICA does not apply to a contract. For some, this may make the case for reform less compelling. Further, policies written as marine policies but in fact covered by the ICA could be regarded as misleading or deceptive and have ramifications under trade practices or fair trading legislation.

8.59 There could be advantages in allowing cargo transit insurance which includes any, or alternatively any significant or non-trivial, component of carriage by water to be covered by the MIA. The Commission recognises that this would not remove all uncertainty about cargo insurance coverage. The substitution of ‘any significant’ for ‘substantial’ would do little except to replace one formula of words with another. Questions would still arise about whether the sea carriage component

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316 P Grieve *Submission 6; Advisory Committee meeting* 18 December 2000.

was ‘significant’ enough to justify MIA coverage, just as it is currently necessary to ask whether a contract is ‘substantially’ one of marine cargo insurance. Nevertheless, by moving the threshold in favour of MIA coverage, the practical effect might be that the question would arise less often.

8.60 The reform would bring Australian market practice (if not the law) closer to that in the United Kingdom. Contracts that include an element of marine cargo but which are not substantially contracts of marine insurance would be covered under the amended Australian MIA and in the United Kingdom by the common law, on which the MIA (UK) is based.<sup>317</sup>

8.61 However, on balance the only solution that provides real certainty under the current dual regime is to put all insurance with any marine element under the MIA. This, however, has the unacceptable effect of widening the scope of the MIA to cover many contracts that are clearly intended by relatively recent legislation to be covered by the ICA. The construction of a new form of words to attempt to define a median point detracts from certainty and, accordingly, the Commission declines to recommend any modification of the MIA in this respect.

## **Other insurance**

8.62 Leaving aside cargo insurance, the application of the MIA to other kinds of insurance involving marine and non-marine risks may likewise be uncertain. Ship repairers, marina operators and port authorities, amongst others, must cover risks which involve marine and non-marine risks — for example, liabilities related to the operation of marina car parks.

8.63 While shipbuilding and launching are specifically covered by the MIA,<sup>318</sup> it may be unclear in other situations whether the MIA or ICA applies. For example, if a marina includes a large retail or commercial development, does the policy remain substantially one of marine insurance?

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317 Therefore, some significant differences would still exist in the law applying to Australian and UK cargo insurance policies that cover some marine risk but are not contracts of marine insurance in terms of the MIA, as it now stands. For example, in the UK it would not necessarily be the case that the broker is directly responsible to the insurer for the premium, unless otherwise agreed, as MIA (UK) s 53(1) would not apply. The distinction between the common law and equivalent provision of the MIA (MIA s 59(1)) made necessary the High Court’s ruling about the coverage of the MIA in *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur (Australia) Ltd* (1986) 160 CLR 226.

318 MIA s 8(2).

8.64 It appears illogical for the MIA to cover shipbuilding and launching but not ship repair, and there is support for an amendment to remedy this position.<sup>319</sup> The Commission notes that s 6(1)(b) of the Marine Insurance Act 1993 (Can) expressly refers to losses incidental to the repair of a ship and recommends that the MIA s 8(2) be amended in similar fashion (see recommendation 4 below).

8.65 Liability insurance has been identified as another area of uncertainty in relation to the respective coverage of the MIA and ICA.<sup>320</sup> It can be difficult to discern whether a particular policy of liability insurance is a contract of marine insurance. Where cargo or other property is insured, the policy can be characterised by reference to the location, movement or activity of the insured property (and the extent that loss is likely to result from exposure to maritime perils). Liability, such as the liability of a freight forwarder, can arise from many causes depending on the operations of the insured, making it potentially more difficult to establish that a contract of public liability insurance is ‘substantially’ one of marine insurance.

8.66 In *Hansen Development P/L v MMI Ltd & Anor*,<sup>321</sup> the New South Wales Court of Appeal found that a public liability insurance policy was governed by the ICA not the MIA. The claim involved a wave sled accident on Cugden Lake. Meagher JA referred to *Arnould’s Law of Marine Insurance and Average*<sup>322</sup> and to the Lloyd’s SG Policy<sup>323</sup> and stated that

[i]n the whole of Arnould’s work I have not located a single example of a public liability risk being treated as a marine insurance risk, let alone a policy dealing with nothing but public liability being treated as a marine policy. Particularly must this be so when no “sea” is involved: Cugden Lake can hardly be said to be a sea.<sup>324</sup>

8.67 This statement suggests that public liability insurance cannot be marine insurance, or at least that it is very rare. However, the MIA specifically refers to marine adventures as including situations where

any liability to a third party may be incurred by the owner of, or other person interested in or responsible for, insurable property, by reason of maritime perils.<sup>325</sup>

319 A Street *Submission 15*; Queensland Commercial Fishermen’s Organisation *Consultation* Brisbane 12 May 2000.

320 MLAANZ members *Consultation* Perth 22 November 2000; Broker *Consultation* Perth 23 November 2000.

321 [1999] NSWCA 186.

322 M Mustill and J Gilman *Arnould’s Law of Marine Insurance and Average* 16th ed vol I Stevens & Sons London 1981.

323 The wording of the Lloyd’s SG Policy can be found in the second schedule to the MIA.

324 *Hansen Development P/L v MMI Ltd & Anor* [1999] NSWCA 186 para 11.

325 MIA s 9(2)(c). MIA s 80 also deals expressly with the measure of indemnity under policies that insure against liabilities to third parties.



8.68 P & I insurance is liability insurance and covers liability incurred by the insured to third parties as a result of a very wide range of maritime causes. In principle there is no reason that public liability cannot be covered by a contract of marine insurance, even though property is not insured by the same policy, as long as the insured is responsible for property that is insurable under the MIA, or if the exposure to liability arises due to a maritime peril.

8.69 One reform option would be to extend the MIA generally to any non-marine risk where there is a real, or alternatively any, connection between the non-marine risks and the marine risk or marine subject matter.<sup>326</sup> This would for example, make it clearer that the MIA applies to marina operations or to public liability insurance related to marine subject matter.

8.70 However, the Commission is concerned that, because there are incentives for insurers to write MIA rather than ICA insurance, some of which are unrelated to the contract itself (such as stamp duty),<sup>327</sup> there is a real risk that too many ICA risks would come under the MIA as a result of such a reform. Such a reform might also risk introducing significant new uncertainty about MIA and ICA coverage.

8.71 It does not make sense to expand the scope of the MIA so that risks that are essentially non-marine are covered by that Act simply because they are coincidentally associated with some marine risks. Why should the risks associated with, for example, a marina car park or a yacht club restaurant be covered by the MIA while similar risks away from the waterfront are covered by the ICA? Furthermore, as a matter of overall policy, the Commission does not see any justification for increasing the scope of the MIA significantly where that encroaches on insurance covered by the ICA except where small refinements to its scope (such as those dealt with in recommendations 2–4) serve to clarify or update the MIA.

8.72 On balance, therefore, the Commission concludes that no statutory reformulation of the demarcation between marine and non-marine insurance in this regard will satisfactorily remove the uncertainty surrounding the location of that demarcation. Accordingly, its recommendation is that the MIA remain unaltered in this respect, subject to the topics covered in the remainder of this chapter.

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326 A Street *Submission 15*.

327 *Advisory Committee meeting* 18 December 2000. The incentives include differences in stamp duty liability and industry levies, avoiding the requirement to give various notices and other consumer protection provisions of the ICA, and differences in the substantive law applying to MIA and ICA insurance, that generally favour insurers.

## The sea and inland waters

8.73 The concept of the ‘sea’ is fundamental to the coverage of the MIA. As noted above, a contract of marine insurance is defined by reference to losses incident to marine adventure,<sup>328</sup> in turn defined by reference to maritime perils which are perils ‘consequent on, or incidental to, the navigation of the sea, that is to say, perils of the seas’.<sup>329</sup> The MIA also allows a contract of marine insurance to extend to protect the insured ‘against losses on inland waters ... which may be incidental to any sea voyage’<sup>330</sup> and to ‘any adventure analogous to a marine adventure’.

8.74 It seems to follow from the definition of maritime perils that to constitute a marine adventure the vessel must either be on a sea voyage or at least be waterborne on the sea. Professor Sutton observes

Admittedly, the definition refers to perils *of* the seas, not perils *on* the seas and such dangers as collision, fire, grounding and foundering, are met with on inland waters as well as the sea, but they are not perils *consequent on or incidental* to the navigation of the sea.<sup>331</sup>

8.75 The distinction between inland waters and the sea can be important in determining the respective coverage of the MIA and the ICA. In practice, the need to make this distinction is limited. Australia’s navigable rivers and other inland waterways are no longer regularly used for cargo transport. Most vessels on Australian rivers and lakes are pleasure craft, insurance of which is expressly covered by the ICA. Further, in many instances commercial navigation on inland waters will be incidental to a sea voyage.

8.76 However, it is possible to hypothesise situations involving commercial vessels where it may be necessary to consider where the sea ends and inland waters start to determine whether the inland waters element of the cover is incidental to a sea voyage or is itself the more significant component. This issue may arise where commercial vessels, such as tour boats, are engaged in voyages from the coast up any one of Australia’s rivers such as the Murray, Swan, Alligator, Daintree, Manning, Yarra, or Gordon rivers.

8.77 At common law the difficulty in distinguishing ‘sea’ from ‘inland waters’ was adverted to by Stephen J in *Raptis & Son v South Australia*,<sup>332</sup> a fisheries case.

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328 MIA s 7.

329 MIA s 9(2).

330 MIA s 8(1).

331 K Sutton *Insurance Law in Australia* 3rd ed LBC Information Services Sydney 1999, 30.

332 *Raptis & Son v South Australia* (1977) 138 CLR 356.

The common law has always recognized that coastal waters in the form of bays enclosed within the jaws of the land form part of the inland waters of the littoral State. However, difficulty has always been experienced in defining with any precision what must be the attributes of such waters before they may be regarded as sufficiently landlocked to qualify as inland waters.<sup>333</sup>

8.78 The MIA does not define ‘inland waters’ or ‘sea’. The Commission’s research has not identified any Australian or other common law marine insurance cases dealing with this issue.<sup>334</sup>

8.79 Definitions of the ‘sea’ found in federal legislation vary considerably. Some legislation, including the *Navigation Act 1912* (Cth), defines the sea as ‘any waters within the ebb and flow of the tide’.<sup>335</sup> Other definitions found in federal legislation include ‘all marine waters other than the internal waters of States’,<sup>336</sup> and ‘marine and tidal waters within the limits of a State or an internal Territory, but [not including] waters enclosed by means of a mariculture installation’.<sup>337</sup> This suggests that ‘marine’ and ‘tidal’ waters are different, at least for the purposes of some legislation.

8.80 The *Seas and Submerged Lands Act 1973* (Cth), which defines Australia’s territorial waters, describes the baseline from which the territorial sea is measured as the low-water line along the coast. The Act provides a lengthy formula for drawing straight baselines in localities where the coastline is deeply indented or if there is a fringe of islands.<sup>338</sup> Waters on the landward side of the baseline are internal waters.<sup>339</sup>

8.81 The *Admiralty Act 1988* (Cth) defines ‘inland waters’ as ‘waters within Australia other than waters of the sea’ and defines the sea as ‘any waters within the ebb and flow of the tide’.<sup>340</sup> Various other definitions are found in state legislation including ‘waters not subject to tidal influence’,<sup>341</sup> specified lakes and geographical features,<sup>342</sup> or waters declared to be inland waters.<sup>343</sup>

333 (1977) 138 CLR 356, 376.

334 As noted in para 8.66, in *Hansen Development P/L v MMI Ltd & Anor* [1999] NSWCA 186 para 11, Meagher JA in the New South Wales Court of Appeal found that Cugden Lake was not the sea. There was, however, no discussion of the indicia of either inland waters or the sea.

335 *Navigation Act 1912* (Cth) s 6; *Historic Shipwrecks Act 1975* (Cth) s 3; *Environment Protection (Alligator Rivers Region) Act 1978* (Cth) s 3.

336 *Environment Protection (Sea Dumping) Act 1981* (Cth).

337 *Prawn Export Promotion Act 1995* (Cth) s 3.

338 *Seas and Submerged Lands Act 1973* (Cth) s 3(1) states that ‘territorial sea’ has the same meaning as Articles 3 and 4 of the Convention on the Territorial Sea and the Contiguous Zone. The definition is further complicated by a provision which allows the positioning of straight baselines to take into account economic interests peculiar to the region concerned, as evidenced by usage.

339 *Seas and Submerged Lands Act 1973* (Cth) s 10.

340 *Admiralty Act 1988* (Cth) s 3(1).

341 Fisheries Management (General) Regulation 1995 (NSW) Reg 3(1).

342 eg *Fisheries Act 1995* (Vic) s 4.

343 eg *Fisheries Act 1995* (Vic) s 4(e), *Inland Fisheries Act 1995* (Tas) s 5.

8.82 It has been suggested that the MIA should be amended to define the ‘sea’ and ‘inland waters’.<sup>344</sup> However, the Commission considers that a simpler and more satisfactory solution would be to amend the MIA so that it clearly covers risks on inland waters. As noted above, the MIA applies to any ‘adventure analogous to a marine adventure’ that is ‘covered by a policy in the form of a marine policy’.<sup>345</sup> Francis Marks and Audrey Balla argue that the existing wording of the MIA might be sufficiently broad to allow the MIA to apply to hull insurance covering inland waters only.

As it applies to ships, the definition of marine adventure in sec 9(2) refers to a ship being exposed to maritime perils, being perils consequent on or incidental to the navigation of the sea. The analogy which most readily springs to mind is the exposure of a ship to perils consequent on or incidental to the navigation of water not being the sea. On this basis the Act will apply to any contract of insurance which covers a ship whilst on inland waters provided that the contract is in the form of a marine policy. Accordingly, the *Marine Insurance Act* will apply to hull insurance covering inland waters only.<sup>346</sup>

8.83 The *Hansen* case (see paragraph 8.66) was the subject of a special leave application to the High Court in *Anchorage Marine Underwriting v Hansen Development*.<sup>347</sup> In the District Court of New South Wales, the trial judge had found that navigation on a lake was analogous to a marine adventure in terms of MIA s 8(2) and therefore covered by the MIA. One of the grounds for the application for special leave in the High Court was that the Meagher JA in the New South Wales Court of Appeal had failed to address this issue. The application for special leave was refused as not appropriate for the determination of the questions of statutory construction raised by the applicant.<sup>348</sup>

8.84 The Commission does not consider that there is any justification for the insurance of commercial vessels on inland waters to be governed by a different legal regime from that governing the insurance of commercial vessels on the sea. The important distinction is the nature of the enterprise to be insured, not the arbitrary, invisible, varying and often irrelevant distinction between the waters of the sea and other waters. The Commission recommends that the MIA should be amended so that a contract of marine insurance may include a contract to indemnify the insured against losses on inland waters regardless of whether or not the risks are an incidental or substantial part of the cover provided. Such a reform would have no international trade implications. It would be consistent with the exclusion of the insurance of pleasure craft and the carriage of personal goods from

344 MLAANZ members *Consultation* Perth 22 November 2000; *Advisory Committee meeting* 18 December 2000.

345 MIA s 8 (2).

346 F Marks and A Balla *Guidebook to Insurance Law in Australia* 3rd ed CCH Sydney 1998, 561.

347 See *Anchorage Marine Underwriting v Hansen Development* [1999] HC Transcript S118/1999.

348 In discussion Gummow J referred to the fact that the Commission had been given a reference to review the MIA.

the MIA.<sup>349</sup> Determining whether a hull insurance contract is covered by the MIA or ICA would depend solely on the use of the insured property<sup>350</sup> (see recommendation 5 below).

8.85 The Commission understands that the Canadian Marine Insurance Act is intended to cover the insurance of risks on inland waters (whether or not incidental to sea risks). To achieve this result, the provisions of the Canadian legislation contain no reference to inland waters or sea voyage<sup>351</sup> and the definition of maritime peril refers to perils consequent on or incidental to 'navigation' rather than to 'navigation of the sea'.<sup>352</sup> The Indian Marine Insurance Act 1963 also appears to apply to inland risks. That Act states that an adventure analogous to a marine adventure 'includes an adventure where any ship, goods or other moveables are exposed to perils incidental to local or inland transit'.<sup>353</sup>

8.86 An amendment of this sort is best placed within MIA s 8 in new subsections that expressly extend the scope of contracts of marine insurance to cover risks on inland waters and provide that where appropriate the 'sea' and expressions using that word should be read as including inland waters, subject to the terms of the contract itself. That would appear to remove the need to re-word the Act where those expressions appear. A small change is also required in s 8(1) to remove the unnecessary and possibly confusing reference to inland waters and the heading to s 8 should also be amended appropriately.

## **Other coverage problems**

### **Usage of trade**

8.87 The wording of MIA s 8 raises a number of other problems that should be resolved. A contract of marine insurance may be given extended coverage over incidental non-marine risks by 'usage of trade'.<sup>354</sup> Consultations have demonstrated that there is little common understanding about the usage of trade in this or other contexts. Although certain common usages might be proved by appropriate evidence in court, there must be some doubt that insureds and others outside the marine insurance industry would have any common understanding about many marine insurance usages. For example, cargo owners could not necessarily be

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349 *Advisory Committee meeting* 18 December 2000.

350 That is, whether the vessel is used or intended to be used for recreational activities or sporting activities and otherwise than for reward, in terms of the ICA definition of a 'pleasure craft': ICA s 9A.

351 MIA (Can) s 6(1).

352 MIA (Can) s 2(1) cf MIA s 9.

353 Marine Insurance Act 1963 (India) s 4(2). Further, s 89 empowers the Indian Central Government to direct that the provisions of the Act shall 'in their application to contracts of marine insurance relating to any class of ships exclusively used in inland navigation, be subject to such conditions, exceptions and modifications as it may specify'.

354 MIA s 8(1).

expected to have much understanding of common usages in the sea-carriage of goods.

8.88 The lack of common understanding on the part of one side of the marine insurance contract means that there is in fact no such common usage, but that question is untested. There remains the possibility that relatively obscure practices could influence the interpretation and operation of marine insurance contracts in ways that are not anticipated on the face of the contractual documents.

8.89 Furthermore, the reference to usage of trade may both clarify the uncertainty surrounding the demarcation between the ICA and the MIA or provide a means of circumventing the statutory policy found in the ICA. Consultations have revealed that cargo insurance is often written as marine insurance irrespective of the modes of transport used or their relative importance or frequency. Does this mean that insurers can determine that all cargo insurance will be covered by the MIA simply by developing a usage of writing such insurance as if it were?

8.90 On balance, the Commission does not consider that MIA s 8(1) warrants reform in this regard. Even if usage might be regarded as too vague to be a reliable indicator of the scope of a contract of marine insurance, there may be cases where it can usefully determine the scope of a contract. Consistently with its general approach not to restrict the flexibility of the MIA, the Commission recommends that the section remain unchanged in this regard. In any event, the only effect that usage can have under s 8(1) is to extend a policy to cover incidental non-marine risks and its application is constrained without further amendment.

### **‘Form of a marine policy’**

8.91 A similar concern arises out of the wording of s 8(2) under which ship building and launching risks,<sup>355</sup> and adventures ‘analogous to’ marine adventures, are covered by the MIA if written on a policy in the ‘form of a marine policy’. This provision invites the conclusion that such risks can be written on other forms and, if they are, that other laws will govern them. The Commission’s concern is that the form of the documents may determine the nature of the cover and the applicable statutory regime and that it is unacceptable that these issues are determined by the style of the documentation.

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355 This would extend to ship repair risks if the Commission’s recommendation in this regard is adopted. See para 8.64 and rec 4.

8.92 The Commission recommends that s 8(2) be amended to delete the reference to ‘a policy in the form of a marine policy’ and to insert a simple statement that these risks are covered by the MIA unless the contract provides otherwise. There is no constraint on the parties contractually applying the ICA (see recommendation 6 below).

### Offshore platforms

8.93 One specific uncertainty that arises in determining what is an ‘adventure analogous to a marine adventure’<sup>356</sup> concerns the insurance of offshore platforms. Is the insurance of a fixed oil platform analogous to a marine adventure, notwithstanding that the platform, unlike a ship, is permanently stationary and secured to the seabed?

8.94 It has been suggested that the MIA should be amended to expressly apply to insurance of fixed or floating navigational aids and equipment and all floating structures or structures affixed to the seabed.<sup>357</sup> The Commission understands that some litigation in England involving fixed and movable platforms has been conducted on the basis that both are covered by the MIA (UK).<sup>358</sup> This may indicate that the London market practice assumes that the MIA governs the insurance of such platforms.

8.95 On the other hand, some Australian insurers have advised that fixed platforms are not, and should not, be covered by the MIA as they may not easily be distinguished from wharves or waterfront houses (in terms of location or exposure to maritime perils) neither of which are covered by contracts of marine insurance.<sup>359</sup>

8.96 The Commission considers that the insurance of oil platforms and similar structures should not as a matter of general principle be covered by the MIA rather than the ICA. Offshore platform policies will cover risks that should clearly remain governed by the ICA. There was no support for the idea that offshore platform insurance should be brought within the MIA from insurers and the Commission makes no recommendation that offshore installations be covered by the MIA.

8.97 This leaves the coverage of such risks, as well as many other risks associated with foreshore activities, to be determined by the current test in MIA s 7 and 8(1). These require a conclusion as to whether a risk is ‘incident’ to a marine adventure or incidental to a sea voyage. Although this issue is still somewhat unsatisfactory,

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356 MIA s 8(2).

357 A Street *Submission 15*.

358 eg *Promet Engineering (Singapore) Pty Ltd v Sturge (The Nukila)* [1997] 2 Lloyd’s Rep 146. This case involved damage to a moveable platform and the interpretation of an Inchmaree clause.

359 *Advisory Committee meeting* 18 December 2000.

the Commission is concerned that attempting to impose a statutory formula will reduce flexibility and could have unforeseen and undesirable consequences that are not easily fixed other than by further statutory amendment. For as long as Australia has two statutes governing activities that may be underwritten as part of one insurance exercise, issues concerning the demarcation between the two systems will continue to arise. This position currently requires the parties to contracts where the respective coverage of MIA and ICA is unclear to consider their position carefully, especially insurers, who have much more to lose if their initial decision turns out to be incorrect. Regrettably, that position will persist for some time to come.

8.98 The solution lies in careful underwriting practices. The onus in this regard falls on the various insurance professionals on each side of the contract, particularly insurers, as errors are likely to prejudice them rather than insureds. Good practice suggests that separate policies be issued if it is intended that the MIA cover marine risks (and incidental non-marine risks) or that it be assumed that the ICA will cover any contracts that have any greater non-marine component and business done accordingly.

## **Recommendations**

**Recommendation 2. The ICA should be amended to cover contracts of insurance for the transportation by water of goods other than goods being transported for the purposes of a business, trade, profession or occupation carried on or engaged in by the insured. This amendment will have the effect of removing the insurance of the carriage of goods for non-commercial purposes from the MIA. MIA s 7 should be amended to state that it is subject to s 9A and the proposed s 9B of the ICA.**

**Recommendation 3. MIA s 8(1) should be amended to refer expressly to losses arising from any air risk incidental to a sea voyage.**

**Recommendation 4. MIA s 8(2) should be amended to refer expressly to losses arising from the repair of a ship.**

**Recommendation 5. The MIA should be amended so that, subject to the terms of the contract, marine insurance covers risks on inland waters and that where appropriate the 'sea' and the 'seas' should be read as including inland waters.**



**Recommendation 6. MIA s 8(2) should be amended to delete the reference to ‘a policy in the form of a marine policy’ and to state that the risks referred to in it are covered by the MIA unless the contract states otherwise.**



## 9. Warranties

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### **Introduction**

9.1 Maritime risks are covered or excluded by the terms of the contract as stated in the policy document, implied by statute or found elsewhere in the contractual documents and incorporated by reference into the policy. Certain terms material to the insurance contract are known as warranties. Warranties are dealt with in Division 7 of the MIA and are defined as follows.

39(1) A warranty, in the following sections relating to warranties, means a promissory warranty, that is to say a warranty by which the assured undertakes that some

particular thing shall or shall not be done, or that some conditions shall be fulfilled, or whereby he affirms or negatives the existence of a particular state of facts.

(2) A warranty may be express or implied.

9.2 The MIA implies certain warranties, those of seaworthiness (MIA s 45 and s 46(2)) and legality (MIA s 47), into contracts of marine insurance. Express warranties may be created by the parties and, consistently with the discretionary nature of this legislation, can override implied warranties.<sup>360</sup> Express warranties may address, for example, geographical restrictions, sailing dates, crew certification and numbers, towage restrictions and loss minimisation.

### **What is a warranty?**

9.3 A fundamental feature of marine insurance warranties is that they must be exactly complied with; otherwise the insurer is discharged from liability.

39(3) A warranty, as above defined, is a condition which must be exactly complied with, whether it be material to the risk or not. If it be not so complied with, then, subject to any express provision in the policy, the insurer is discharged from liability as from the date of the breach of warranty, but without prejudice to any liability incurred by him before that date.

9.4 If a warranty is breached, even if the subject matter of the warranty is irrelevant to the loss, the insurer is automatically discharged from all future liability.<sup>361</sup> The insurer does not have to elect to avoid further liability although it can waive its rights.<sup>362</sup> Any liability that has already arisen remains on foot. There is no requirement that the breach be connected in any way with any subsequent claim. Trivial or inadvertent breaches are sufficient to trigger the insurer's discharge of liability. The breach cannot be remedied.<sup>363</sup> The rules of strict compliance apply to both express and implied warranties.

### **Warranties and other contractual terms**

9.5 General contract law distinguishes between conditions and warranties. Conditions go to the heart of the contract and a breach may lead to rescission; warranties are terms whose breach may give rise to damages, but not rescission.<sup>364</sup>

360 MIA s 41(3): 'An express warranty does not exclude an implied warranty, unless it be inconsistent therewith.'

361 MIA s 39(3).

362 MIA s 40(3).

363 MIA s 40(2): 'Where a warranty is broken, the assured cannot avail himself of the defence that the breach has been remedied, and the warranty complied with, before loss.'

364 *Hongkong Fir Shipping Co v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 69–70; T Schoenbaum 'Warranties in the Law of Marine Insurance: Some Suggestions for Reform of English and American Law' (1999) 23 *Tulane Maritime Law Journal* 267, 276; *Associated Newspapers Ltd v Banks* (1951) 83 CLR 322; N Seddon and M Ellinghaus *Cheshire and Fifoot's Law of Contract* 7th Australian ed Butterworths 1997, 745.

9.6 In insurance law, the term warranty has been described as a ‘word of uncertain meaning’.

Any attempt to explain the significance of the term is complicated by the often indiscriminate use of the word to denote clauses in policies with widely varying functions, and by variations in legal vocabulary attributable in part to changes in legal terminology over the years and in part simply to judicial idiosyncrasy.<sup>365</sup>

9.7 A series of judgments in the 1770s by Lord Mansfield held that warranties in insurance were equivalent to conditions, requiring strict compliance.<sup>366</sup> These principles were subsequently codified in marine insurance legislation in England, Australia and other countries.

9.8 In *The Good Luck*, the English Court of Appeal stated that a warranty in marine insurance is equivalent to a condition precedent in general contract law.<sup>367</sup> Following *The Good Luck*, Malcolm Clarke stated

The place of the insurance warranty in the ranks of contractual terms is now clearer than before. As regards contracts in general, it is distinguished from the general warranty, in that the latter, if broken, gives rise to damages but not to discharge, whether automatically or by election. The insurance warranty is distinguished from the general condition, in that the latter, if broken, gives rise to both damages and discharge, but the discharge occurs only on the election of the party not in breach. As regards insurance contracts in particular, the insurance warranty is distinguished from the exception, in that the effect of the latter is to suspend the insurer’s undertaking to pay, whereas a breach of warranty discharges the liability of the insurer altogether.<sup>368</sup>

9.9 Within the framework of general contract law, the breach of a marine insurance warranty under the MIA may also be considered to be analogous to the breach of an essential term (breach of condition) or a breach going to the root of the contract (fundamental breach)<sup>369</sup> although termination is automatic rather than by election.

365 K Sutton *Insurance Law in Australia* 3rd ed LBC Information Services Sydney 1999, 625. Professor Sutton states that he uses the term ‘warranty’ as synonymous with ‘condition’ in the sense of a clause in the contract of insurance the breach of which will entitle the insurer to repudiate liability under the contract: 626.

366 T Schoenbaum ‘Warranties in the Law of Marine Insurance: Some Suggestions for Reform of English and American Law’ (1999) 23 *Tulane Maritime Law Journal* 267, 278; W Vance ‘The History of the Development of the Warranty in Insurance Law’ (1911) 20(7) *Yale Law Journal* 521, 525–32.

367 *Bank of Nova Scotia v Hellenic Mutual War Risk Association (Bermuda) Ltd (The Good Luck)* [1992] 1 AC 233, 263.

368 M Clarke ‘Breach of Warranty in the Law of Insurance’ (1991) *Lloyd’s Maritime and Commercial Law Quarterly* 437, 441. This passage highlights the confusing and unsatisfactory nature of the term ‘warranty’ which, in any event, cannot be expected to have any, or any particular, meaning to people unfamiliar with marine insurance law.

369 To adopt the terminology used by N Seddon and M Ellinghaus *Cheshire and Fifoot’s Law of Contract* 7th Australian ed Butterworths 1997, 742.

9.10 The different use of the term ‘warranty’ in marine insurance law as compared with general contract law is well established but potentially confusing. The term is not used in the ICA except to negate the existence of warranties.<sup>370</sup> The peculiar impact of a warranty in marine insurance law would surprise many not familiar with it, and concerns many who are.

### **Creating an express warranty**

9.11 The MIA provides that express warranties must be written in or incorporated into the policy.<sup>371</sup> An early English case found that

[p]rima facie, words qualifying the subject-matter of the insurance will be words of warranty, which in a policy of marine insurance operate as conditions.<sup>372</sup>

9.12 Warranties can be created by the use of the word ‘warranty’ or ‘warranted’. However, whether a term constitutes a promissory warranty depends upon the intention of the parties as revealed by the policy as a whole. No particular form of words is required.<sup>373</sup>

[T]he warranty may be in any form of words so long as there is an intention to warrant, and if this intention exists the warranty has effect as a condition which must be exactly complied with, whether material to the risk or not.<sup>374</sup>

9.13 Given the harsh consequences of a breach of warranty, it is unsatisfactory that the true nature and ramifications of express warranties in the policy can be obscured in this way.

### **Waiver of breach of warranty**

9.14 The Act provides several, though limited, situations where a breach of warranty will be excused.

40(1) Non-compliance with a warranty is excused when, by reason of a change of circumstances, the warranty ceases to be applicable to the circumstances of the contract, or when compliance with the warranty is rendered unlawful by any subsequent law.

9.15 In addition, an insurer may waive a breach of warranty.<sup>375</sup> This concept of waiver has been the subject of legal controversy. One difficulty is that, as the

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370 See ICA s 24 which provides that statements by the insured with respect to the existence of a state of affairs do not have effect as a warranty.

371 MIA s 41(2).

372 *Yorkshire Insurance Company v Campbell* [1917] AC 218.

373 MIA s 41(1).

374 *K Sutton Insurance Law in Australia* 3rd ed LBC Information Services Sydney 1999, 635.

375 MIA s 40(3): ‘A breach of warranty may be waived by the insurer.’

remedy of avoidance of the contract is automatic,<sup>376</sup> ‘there would appear to be nothing for the insurer to waive’.<sup>377</sup> However, in *The Good Luck* Lord Goff held that the effect of a waiver was simply that ‘to the extent of the waiver, the insurer cannot rely upon the breach as having discharged him from liability’.<sup>378</sup> The insurer may, therefore, be held to the contract through either an election to waive his right to rely on the automatic discharge or an equitable estoppel barring him from so relying.<sup>379</sup>

9.16 Waiver was discussed by the Federal Court in *Mowie Fisheries*.<sup>380</sup> The insured argued that waiver was imputed by the conduct of the insurer in its delay in denying the claim. The Court held, following *Commonwealth v Verwayen*,<sup>381</sup> that there is no independent doctrine of waiver as distinct from election, variation of contract or estoppel.<sup>382</sup>

9.17 ‘Held covered’ clauses allow the insured to renegotiate the contract where a breach of warranty would otherwise have occurred. While such provisions are included in the Institute clauses, it has been said that they are not in common use in Australia.<sup>383</sup>

## The requirement of strict compliance

9.18 In its Discussion Paper the Commission noted that criticism focused on the operation of the warranty provisions under which the insurer may, subject to any express contrary provisions in the policy, avoid all liability from the date of the breach of a warranty regardless of whether the breach was material to the loss, the state of mind of the insured or whether there was any causal connection between the breach and the loss.

9.19 Marine insurance case law provides examples of situations where insurers seek to avoid liability on the basis of a breach of a warranty that was immaterial to the loss.<sup>384</sup> Some of these cases are discussed later in relation to specific warranties.

376 That is, without the need for any election by the insurer.

377 See H Bennett *The Law of Marine Insurance* Clarendon Press Oxford 1996, 283.

378 *Bank of Nova Scotia v Hellenic Mutual War Risks Association (Bermuda) Ltd (The Good Luck)* [1992] 1 AC 233, 263.

379 H Bennett *The Law of Marine Insurance* Clarendon Press Oxford 1996, 284.

380 *Mowie Fisheries Pty Ltd v Switzerland Insurance Australia Ltd* (1996) 140 ALR 57.

381 (1990) 170 CLR 394; (1990) 95 ALR 321.

382 *Mowie Fisheries Pty Ltd v Switzerland Insurance Australia Ltd* (1996) 140 ALR 57, 80. See also *Switzerland Insurance Australia Ltd v Mowie Fisheries Pty Ltd* (1997) 74 FCR 205, 243 (Beaumont J); 144 ALR 234, 268 (Beaumont J).

383 ITC Hulls cl 3; Legal practitioner Consultation Brisbane 11 May 2000.

384 eg *Pawson v Watson* (1778) 2 Cowp 785; *Overseas Commodities Ltd v Style* [1958] 1 Lloyd’s Rep 546; *Doak v Weekes* (1986) 82 FLR 334.

9.20 An example is the *Mowie Fisheries* case,<sup>385</sup> where the insurer sought to avoid liability for the sinking of a fishing vessel on the basis of breach by the insured of express warranties and the implied warranty of legality. At issue was whether there had been any breach of State marine safety laws or other regulations, necessitating an exhaustive examination of a plethora of regulations even though there was no indication that any such breach contributed to the sinking. Concerns expressed by the Queensland Commercial Fishermen's Organisation (QCFO) about the operation of warranties in such a way were instrumental in prompting this review.<sup>386</sup>

9.21 While consultations confirmed that particular problems have been experienced in claims relating to commercial fishing vessels, there is broad concern about the potentially unfair operation of the law relating to warranties. Submissions, including those from insurers, have expressed considerable support for reform (see paragraphs 9.114–9.117 below).

### The case for and against reform

9.22 Although there is a wide consensus that the provisions of the MIA dealing with warranties are capable of operating in an unfair manner, and that fair outcomes may require insurers to 'do the right thing' even where they may have no legal obligation to honour a claim, there are some who favour their retention.

9.23 Some insurers favour the retention of strict compliance so they can rely on it where necessary to refuse a claim.<sup>387</sup> Those defending the status quo argue that a requirement that causation be proved before an insurer is entitled to avoid liability for breach of warranty would result in more and longer trials in an attempt to find fault or privity on the part of the insured.<sup>388</sup>

### Market practice

9.24 Some insurers note that market disincentives restrain insurers from relying unfairly on a breach of warranty. Brokers may cease to facilitate insurance

385 *Mowie Fisheries Pty Ltd v Switzerland Insurance Australia Ltd* (1996) 140 ALR 57; *Switzerland Insurance Australia Ltd v Mowie Fisheries Pty Ltd* (1997) 74 FCR 205; (1997) 144 ALR 234.

386 QCFO Submission to AG's Dept — Reform of the Law of Marine Insurance Marine Insurance Act 1909 1997; QCFO Consultation Brisbane 12 May 2000. The submission by the QCFO instigated the initial review of the MIA by the Attorney-General's Department in 1997. The QCFO remained concerned that reform address cases where warranties are relied upon to avoid a claim where the loss is not related to a technical breach: QCFO Consultation Brisbane 12 May 2000. The QCFO is now known as the Queensland Seafood Industry Association.

387 Insurers and brokers Consultation Sydney 27 March 2000; Insurers, brokers and legal practitioners Consultation Perth 29 March 2000; J Hare 'The Omnipotent Warranty: England v The World' Paper International Marine Insurance Conference Antwerp November 1999 <http://www.uct.ac.za/depts/shiplaw/imic99.htm> (24 February 2000).

388 R Cooper 'Australian Perspectives in Marine Insurance' Paper Shipping in the New Millennium Conference MLAANZ Brisbane 19 March 1999.



contracts with insurers who act unfairly in relation to minor or non-causative breaches of warranty and this may act as a brake on insurers' conduct in refusing claims.

9.25 Consultations confirmed that an insurer's decision not to rely on a technical breach may be influenced by reasons unconnected to the circumstance of the loss, such as whether or not the insured has renewed its policy with that insurer<sup>389</sup> or the commercial importance to the insurer of retaining the particular insured as a client.<sup>390</sup>

9.26 In its Discussion Paper, the Commission noted that the QCFO, lawyers and judges had all stated that, in practice, while insurers may be legally entitled to avoid a claim on the basis of breaches of the myriad of shipping regulations, they generally do not do so, particularly where insured parties, their brokers, and insurers have an ongoing relationship.<sup>391</sup>

9.27 Throughout the course of the inquiry, insurers continued to maintain that, while recourse to refusing a claim for a non-causative breach of warranty was a valuable 'ace up the sleeve', it was rarely used. An exception to this restraint was where the insurer strongly suspected, but was unable to prove, that the loss was caused by or contributed to by some breach of the insured's obligations. However, this view of insurers' conduct was strongly contested by lawyers and others in the industry who professed knowledge of many instances in which breach of warranty had been raised by insurers in an attempt to refuse claims where there was clearly no causal effect on the loss.<sup>392</sup> Some brokers and others have stated that recent amalgamations among Australian based insurance companies have led to a 'watering down' in marine insurance expertise and a consequent overzealous recourse to breach of warranty to refuse claims, often in response to legal advice.<sup>393</sup>

9.28 In any case, the fact that insurers may only rarely use unfair provisions is not a convincing argument for their retention. In fact, if this is the case, reforming the law relating to warranties by requiring that breaches of warranties be causative of loss in order for the insurer to avoid liability would simply reflect what is said to be common industry practice.<sup>394</sup> If the statute is unfair, it is inappropriate to rely on the

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389 F Hunt Correspondence 24 May 2000.

390 Insured interests Consultation Perth 24 November 2000.

391 ALRC DP 63 para 5.26.

392 eg MLAANZ members Consultation Perth 22 November 2000; Broker Consultation Perth 23 November 2000.

393 Ibid.

394 In a similar way, it has been said that the inclusion of pleasure craft within the ICA in 1998 reflected the pre-change market practice of treating contracts of insurance for pleasure craft as they if they came under the ICA rather than as under the MIA: Legal practitioners Consultation Sydney 1 May 2000.

sense of fair play of the party which benefits as the basis for retaining one-sided provisions.

### **Knowledge in the market**

9.29 One role of the broker in the formation of marine insurance contracts is to negotiate appropriate warranty provisions on behalf of the insured. The severity of the consequences of a breach of warranty may be tempered by the terms of the contract.

9.30 For example, the Institute Time Clause Hulls contract terms contain a ‘held covered’ clause that holds the insured covered for a breach of warranty as to cargo, trade, locality, towage, salvage services or date of sailing if notice is given to the insurer and any amended terms of cover and additional premiums are agreed.<sup>395</sup> Such clauses allow the contract to be renegotiated following a breach by the insured; insurance coverage continues even where a breach has occurred, provided that the insurer is informed of the breach and further contractual arrangements, if required, are made.<sup>396</sup> Professor John Hare has stated

In the marine context, London cover is often extended specifically for breach of warranty upon payment of an additional premium. This ... is an attempt by a hopefully somewhat embarrassed industry to take the edge off the otherwise draconian effects of the Marine Insurance Act. But self-regulation should not relieve the legislature of its responsibility to ensure that its laws are fair.<sup>397</sup>

9.31 In consultations, some Australian importers and exporters observed that the complexities of marine insurance law and the harsh consequences of breaching legal obligations mean that parties seeking to be covered by marine insurance are much more reliant on the advice of brokers compared with those entering contracts governed by the ICA. Concerns were also expressed about the availability of specialist marine broking expertise within Australia.<sup>398</sup>

9.32 It is a fact that levels of expertise vary and that the understanding of even experienced insurance professionals of the existence, meaning and effect of provisions of marine insurance law and contracts vary considerably. Some unpalatable aspects of warranties are that they do not have to be couched in any particular words, that the word ‘warranty’ does not necessarily convey any, or any accurate, meaning to the parties and that the consequences of a breach are not customarily stated in the policy or other contractual documents.

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395 ITC Hulls cl 3. Similar provisions are contained in the ITC Freight Contract, cl 4.

396 Legal practitioner Consultation Brisbane 11 May 2000.

397 J Hare ‘The Omnipotent Warranty: England v The World’ Paper International Marine Insurance Conference Antwerp November 1999 <http://www.uct.ac.za/depts/shiplaw/imic99.htm> (24 February 2000).

398 Insured interests Consultation Perth 24 November 2000.

9.33 Problems with the harsh operation of warranties are exacerbated by a lack of understanding about what ‘warranty’ means, at least outside the legal profession and insurance industry. Rather than changing the substantive law relating to warranties, reform could also require the effect of a breach of warranty to be expressly stated on proposal forms and in policies.<sup>399</sup>

### Industry dispute resolution

9.34 It has been suggested that the harsh operation of the existing law of marine insurance could be addressed through the introduction of an industry dispute resolution scheme rather than by amending the MIA itself.<sup>400</sup> The Discussion Paper noted that the insurance industry already operates such a scheme in relation to most domestic insurance and some small business insurance.<sup>401</sup> The suggestion that such a scheme could be an appropriate substitute for law reform was rejected in submissions.<sup>402</sup>

### Safety

9.35 Strict compliance with warranties is considered important by some as warranties may promote compliance with safety, anti-pollution and other standards. As the Law Society of Western Australia noted

The rigours of insisting on strict compliance with warranties may actually encourage and promote greater care on the part of insureds and encourage greater safety standards and vigilance of the insured at all times. This can only be in the interest of the maritime industry generally.<sup>403</sup>

9.36 The importance of safety of life at sea cannot be overemphasised. This is reflected in the many international conventions and national and state laws relating to shipping. The imposition of warranties addressing seaworthiness and the legality of operations provide financial incentives for compliance with these legal regimes. There is concern that this inducement will be removed if strict compliance with

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399 Advisory Committee meeting 18 December 2000. cf ICA s 37, under which an insurer may not rely on unusual provisions unless the insurer clearly informed the insured about the effect of the provision, and ICA Part IX.

400 Insurers, brokers and legal practitioners Consultation Perth 29 March 2000; Insurers and legal practitioner Consultation Brisbane 11 May 2000; Insurers and legal practitioners Consultation Sydney 15 May 2000.

401 The Insurance Enquiries and Complaints Scheme is a national scheme aimed at resolving disputes between insurance companies and insureds. See ALRC DP 63 para 5.31.

402 K Carruthers Submission 9.

403 The Society was nevertheless supportive of reform to introduce an element of causation as a prerequisite to the insurer’s discharge from liability and to make breach of warranty remediable: Law Society of WA Submission 7.

warranties is relaxed, and personal safety and the environment may be more at risk.<sup>404</sup>

9.37 Another view is that it is not appropriate to make any direct link between public policy issues, such as those related to safety at sea, and the contents of private marine insurance contracts. Such public policy issues may be better left to legislative regulation and supervision by bodies such as the Australian Maritime Safety Authority (AMSA).<sup>405</sup>

## The law in other jurisdictions

### Developments in other common law countries

9.38 Canada's Marine Insurance Act 1993 is also based on the MIA (UK). However, a review of recent Canadian cases by Christopher Giaschi illustrates how Canadian courts may be increasingly disinclined to hold that terms of the contract of marine insurance are promissory warranties, even when the language of the contract expresses them to be warranties.

Recent developments in the law in relation to warranties in policies of marine insurance indicate that there has been a judicial amendment of, if not complete revocation of the Marine Insurance Acts. It is only in very rare circumstances that a Canadian court will find a policy to contain a true warranty. These circumstances will essentially be limited to situations where the warranty is material to the risk and the breach has a bearing on the loss.<sup>406</sup>

9.39 For example, in *Century Insurance Company of Canada v Case Existological Laboratories Ltd (The Bamcell II)*<sup>407</sup> the contract contained the following clause: 'Warranted that a watchman is stationed on board the Bamcell II each night from 2200 hours to 0600 hours.' In fact, from the time the insurance commenced, no watchman had been stationed on the ship. The fact that there was no watchman on board during the prescribed hours had no bearing on the loss of the vessel, which occurred in mid-afternoon.<sup>408</sup> The Supreme Court of Canada found that the provision was not a warranty. Giaschi states that the Court

404 See para 9.188.

405 Marine insurance seminar Phillips Fox Sydney 20 February 2001, referring to comments made by participants at CMI conference, Singapore, February 2001. In this context, Mr David Taylor stated that governments consider marine insurers to be a part of the 'chain of maritime responsibility' and look to insurers to accept a level of responsibility for ensuring maritime safety: Marine insurance seminar Phillips Fox Sydney 20 February 2001.

406 C Giaschi 'Warranties in Marine Insurance' Paper Association of Marine Underwriters of British Columbia Vancouver 10 April 1997.

407 [1984] 1 WWR 97.

408 Ibid 104.

‘disregarded the plain words of the policy of insurance and the statute to do what it perceived as fair’.<sup>409</sup>

9.40 *The Bamcell II* was applied by the British Columbia Supreme Court in *Federal Business Development Bank v Commonwealth Insurance*,<sup>410</sup> where it found that the clause ‘Warranted vessel to be laid up at the north foot of Columbia Street’ was not a warranty because the parties did not intend it to be strictly complied with. In *Federal Business Development Bank v Reinsurance and Excess Managers Ltd*<sup>411</sup> the Court held that the clause ‘warranted that the vessel shall not otherwise tow or be towed’ was not a true warranty because vessels of the same type as that insured were commonly used for towing. The insured tugboat had sunk while towing a jetboat.

9.41 In *Shearwater Marine Ltd v Guardian Insurance Co*<sup>412</sup> a warranty that the vessel be inspected daily and pumped as necessary was found to be a suspensive condition; that is, one that suspends the policy following a breach until the breach is rectified. This approach is similar to that in some courts in the USA, which have held that a breach of warranty in a marine insurance contract suspends operation of the policy. According to American case law, an insurer cannot avoid the policy if the breach is rectified prior to a loss.<sup>413</sup>

9.42 This reasoning is also used in some cases in United Kingdom courts. In *Kler Knitwear Ltd v Lombard General Insurance Co Ltd*<sup>414</sup> the English High Court found a warranty to be a ‘suspensory condition’ which, rather than cancelling the policy automatically on its breach, suspended the policy until the breach was rectified. This case is the latest in a line of cases where courts have been ‘reluctant to construe a clause as a warranty, even when so described, unless breach of the clause has serious consequences for the insurer’.<sup>415</sup> The court relied on the decision of the English Court of Appeal in *Hussain v Brown*<sup>416</sup> in which Saville LJ said

409 C Giaschi ‘Warranties in Marine Insurance’ Paper Association of Marine Underwriters of British Columbia Vancouver 10 April 1997.

410 (1983) 2 CCLI 200.

411 (1979) 13 BCLR 376.

412 (1997) 29 BCLR (3d) 13.

413 *Employer’s Ins v Trotter Towing Co* 834 F 2d 1206, 1212 (5th Cir 1988); *Graham v Milky Way Bargo Inc* 824 F 2d 276, 383 (5th Cir 1987); P Griggs ‘Coverage, Warranties, Concealment, Disclosure, Exclusions, Misrepresentations, and Bad Faith’ (1991) 66 *Tulane Law Review* 423, 343; T Schoenbaum ‘Warranties in the Law of Marine Insurance: Some Suggestions for Reform of English and American Law’ (1999) 23 *Tulane Maritime Law Journal* 267, 289.

414 *Kler Knitwear Ltd v Lombard General Insurance Co Ltd* [2000] 1 *Lloyd’s Law Reports Insurance and Reinsurance* 47, discussed in J Miller ‘Continuing Warranties — Court Reviews Nature of Contract Terms’ 18 May 2000 *Insurance Day* 6.

415 J Miller ‘Continuing Warranties — Court Reviews Nature of Contract Terms’ 18 May 2000 *Insurance Day* 6.

416 [1996] 1 *Lloyd’s Rep* 627.

It must be remembered that a continuing warranty is a draconian term. The breach of such a warranty produces an automatic cancellation of cover, and the fact that a loss may have no connection with that breach is irrelevant. If underwriters want such protection, it is up to them to stipulate for it in clear terms.<sup>417</sup>

9.43 This last remark suggests one possible avenue of reform. As noted below,<sup>418</sup> repealing or amending MIA s 40(2), which prevents an insured using the defence that the breach has been remedied and the warranty complied with before loss, would leave it open for insureds to argue that warranties should be treated as suspensive in nature.

### **Civil code countries**

9.44 The law in civil code countries does not generally elevate contractual terms in marine insurance contracts to the status of promissory warranties. Breaches of contractual terms, which would be considered as warranties under the MIA, do not necessarily entitle an insurer to avoid liability from the time of the breach. Liability is determined by reference to various principles relating to fault or knowledge on the part of the insured, the materiality of the breach, and causation.

9.45 The civil code concept of alteration of risk covers many matters which, in common law countries, might be the subject of a promissory warranty. Alteration of risk provisions may be used to cover ‘almost anything the insurer did not bargain for at the time the policy was drawn up’.<sup>419</sup>

9.46 Under the Norwegian Marine Insurance Plan where an alteration of risk<sup>420</sup> occurs the liability of the insurer for subsequent loss depends on whether

- the alteration of risk was caused or agreed to by the insured
- the insurer would have accepted the insurance at the time the contract was concluded if the insurer had known that the alteration of risk would take place
- the alteration of risk was notified to the insurer, and

417 Ibid 630.

418 See para 9.50–9.52.

419 It can include such things as navigating outside the geographical area contemplated by the policy, sailing outside specified time periods, a loss of ship classification and so on: S Derrington ‘The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform’ Ph D thesis University of Queensland November 1998, 275.

420 The Norwegian Marine Insurance Plan states ‘An alteration of the risk occurs when there is a change in the circumstances which, according to the contract, are to form the basis of the insurance, and which alter the risk contrary to the implied conditions of the contract’: Norwegian Marine Insurance Plan cl 3-8 <http://exchange.dnv.com/nmip/books/plan> (28 March 2000). The commentary states that two general conditions must be met: ‘there must have been a change in the factual circumstances which affect the nature of the risk and this must amount to a breach of the implied conditions upon which the contract was based’. Commentary to Norwegian Marine Insurance Plan cl 3-8 <http://exchange.dnv.com/nmip/books/comm> (28 March 2000).

- the loss is attributable to the alteration of risk.<sup>421</sup>

9.47 The insurer may avoid liability for loss if the insured has intentionally caused or agreed to the alteration of risk and the insurer would not have accepted the insurance knowing about the alteration of risk. If the insurer would have accepted the insurance, or accepted it on other conditions, the insurer is liable only to the extent that loss is not attributable to the alteration of risk. Failure to notify the insurer about an alteration of risk may allow the insurer to avoid liability even where the insured is not responsible for the alteration of risk. In all cases, if an alteration of risk occurs, the insurer may terminate the insurance on 14 days' notice.<sup>422</sup>

9.48 Loss of class appears to be one area of contractual obligation where breach may allow an insurer to avoid liability for loss, regardless of materiality or causation.<sup>423</sup> In many civil code countries, breach of contractual obligations for ships to be entered with a classification society approved by the insurer automatically results in termination of the policy.<sup>424</sup> This echoes some of the concerns that lie behind an approach that treats warranties relating to safety, pollution and similar matters differently from other concerns.

## Options for reform

9.49 There are many options for reform of the law relating to marine insurance warranties. Generally, these approaches provide for the introduction of elements of causation or materiality so that, for example, an insurer may only avoid liability for breach of warranty where the warranty was not remedied before the loss occurred or where the breach caused or contributed to the loss. In some cases, a distinction is drawn between express warranties in the policy and the warranties implied by statute. Some of these options for reform are discussed below.

421 Norwegian Marine Insurance Plan cl 3-9; cl 3-10; cl 3-11. Dr Sarah Derrington notes that Norwegian law uses the same type of rule to deal with both the problems of disclosure and misrepresentation and the problems relating to alteration of risk: S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' Ph D thesis University of Queensland November 1998, 274-5 and eg see Norwegian Marine Insurance Plan cl 3-3.

422 Ibid. These general rules on alteration of the risk are not frequently invoked as specific provisions deal with specific types of breaches, such as seaworthiness and safety regulations.

423 Classification societies and loss of class are discussed in more detail in para 9.203-9.207.

424 This position applies in Norway, Sweden, Finland, Denmark, Belgium and China. Trine-Lise Wilhelmsen states that loss of class seems to be the only example of a civil law contractual provision which may be compared to a common law affirmative warranty: T-L Wilhelmsen 'Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire' in CMI Yearbook 2000 Comité Maritime International, Antwerp 2000, 332, 404-5. In Norway, cover nevertheless continues until the ship reaches the nearest safe port in accordance with the insurer's instructions: Norwegian Marine Insurance Plan cl 3-14.

## **Breach of warranty remedied prior to loss**

9.50 The effect of MIA s 40(2) is that once a warranty is breached the insurer is discharged from all future liability; the fact that the insured remedied the breach before any loss occurred has no effect. A minimal reform of the law could alter this position so that a breach of warranty suspends the insurer's liability under the contract either generally or for losses to which the breach relates, but reinstates that liability once the breach is remedied.<sup>425</sup> Most other reform options, including those discussed below, introduce requirements of causation or actual prejudice to the insured before the insurer's liability is discharged or limited. If reform along these lines is adopted, the suspension should be of the insurer's liability for particular loss and not of the contract itself.

9.51 It might be thought that simply making breaches of warranty remediable would achieve the same effect as introducing causation because a breach of warranty that is remedied before loss cannot have caused or contributed to the loss. Conversely, if a breach did not cause or contribute to the loss, it is immaterial whether it is ever remedied.

9.52 However, it is incorrect to regard remediability and causation as merely reverse aspects of the same concept.<sup>426</sup> In determining how reform might be accomplished it must be borne in mind that during the life of a policy multiple breaches may arise, and be remedied, at different times, each playing some or no role in any loss that may occur. For example, assume that while the insurer's liability under the contract is suspended due to a breach of warranty, loss results from a cause entirely unrelated to that breach. If breaches were remediable but causation were not an element of the insurer's right to relief, the insurer would be able to avoid liability for this loss even if the breach were subsequently remedied. Therefore, depending on the way a reformed MIA is drafted, the remediability of breaches of warranty may not be sufficient to address concerns about the inequitable consequences of non-causative breaches of warranty.

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425 This is the approach to breach of warranty taken in some US and Canadian cases: see para 9.38–9.41.

426 Marine insurance seminar Phillips Fox Sydney 20 February 2001.



## Legislative models for reform

### Insurance Law Reform Act 1977 (NZ)

9.53 In New Zealand, the Insurance Law Reform Act 1977 (NZ) provides as follows.

11. Where —

- (a) By the provisions of a contract of insurance the circumstances in which the insurer is bound to indemnify the insured against loss are so defined as to exclude or limit the liability of the insurer to indemnify the insured on the happening of certain events or on the existence of certain circumstances; and
- (b) In the view of the Court or arbitrator determining the claim of the insured the liability of the insurer has been so defined because the happening of such events or the existence of such circumstances was in the view of the insurer likely to increase the risk of such loss occurring, —

the insured shall not be disentitled to be indemnified by the insurer by reason only of such provisions of the contract of insurance 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.

9.54 In the event of a breach of a warranty (including a warranty in a contract of marine insurance),<sup>427</sup> the section provides that the insured remains entitled to be indemnified if he or she proves on the balance of probabilities that the loss was not caused or contributed to by the breach of warranty.

9.55 There have been suggestions that the section was intended to deal with exclusions from cover rather than warranties, but the section has been taken to apply more widely.<sup>428</sup> However, obiter statements in case law suggest that while it applies to express warranties, warranties implied by statute, such as the implied warranty of legality in MIA s 47, are not affected.<sup>429</sup> In *Harbour Inn Seafood Ltd v Switzerland General Insurance Ltd*, Fisher J stated that

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427 Insurance Law Reform Act 1977 (NZ) s 14 states that nothing in the Marine Insurance Act 1908 (NZ) shall limit any provision of the Insurance Law Reform Act.

428 ALRC 20 para 223; *Sampson v Goldstar Insurance Company Ltd* [1980] 2 NZLR 742, 745. On introducing this legislation, the New Zealand Minister of Justice stated 'Clause 11 deals with what are called non-causative exemptions. Insurance policies commonly exclude liability in certain instances. For example, a motor vehicle policy may exclude liability while the vehicle is being driven in an unsafe condition. If the vehicle is hit while stopped at traffic lights the insurer would be able to avoid liability even though the unsafe condition had nothing to do with the accident. The clause confines the right to avoid the policy to those instances where the circumstances specified in the exemption contributed to the accident': House of Representatives Parliamentary debates 6 July 1977, 1207.

429 *Harbour Inn Seafoods Ltd v Switzerland General Insurance Ltd* (1991) 6 ANZ Ins Cases ¶61-048; *Womersley v Peacock* (unreported, High Court of NZ, Christchurch Registry CP 24/98, 8 September 1999).

whatever the relevance of s 11 to promissory warranties in the defendant's standard policy, the provisions could certainly not overcome the independent difficulty the plaintiff faces under s 42 of the Marine Insurance Act. Section 11 of the Insurance Law Reform Act in its use of the words 'in the view of the insurer' is, in my view, inconsistent with promises which become part of the contract not because of any view of the insurer but because of the intentions of the legislature'.<sup>430</sup>

9.56 Similarly, in *Womersley v Peacock* Panckhurst J said

Exemptions, or warranties, implied by statute were not seemingly considered when s 11 was drafted with reference to the circumstances in "a contract of insurance" (s 11(a)) and "the view of the insurer" as to increased risk (s 11(b)). As a result ... I think it is doubtful whether s 11 can override a statutory warranty.<sup>431</sup>

9.57 The Insurance Council of Australia has suggested that the provisions of the Insurance Law Reform Act 1977 may be a suitable starting point for reform.<sup>432</sup> One advantage would be that it would also harmonise the law in the Trans-Tasman shipping market.

### ***Insurance Act 1902 (NSW)***

9.58 Section 18 of the *Insurance Act 1902* (NSW) permits a court to excuse a breach of a term or condition of the contract of insurance by an insured which does not prejudice the insurer.<sup>433</sup> Section 18 states

18(1) In any proceedings taken in a court in respect of a difference or dispute arising out of a contract of insurance, if it appears to the court that a failure by the insured to observe or perform a term or condition of the contract of insurance may reasonably be excused on the ground that the insurer was not prejudiced by the failure, the court may order that the failure be excused.

(2) Where an order of the nature referred to in subsection (1) has been made, the rights and liabilities of all persons in respect of the contract of insurance concerned shall be determined as if the failure the subject of the order had not occurred.

9.59 The section applies to policy terms which impose a positive obligation on the insured, such as a requirement to give notice of a loss,<sup>434</sup> and to policy terms which exclude the insurer's liability.<sup>435</sup> The effect is to provide relief where

430 *Harbour Inn Seafoods Ltd v Switzerland General Insurance Ltd* (1991) 6 ANZ Ins Cases ¶61-048, 77,065. The Australian equivalent of MIA (NZ) s 42 is MIA s 47.

431 *Womersley v Peacock* (unreported), High Court of NZ, Christchurch Registry CP 24/98, 8 September 1999.

432 Insurance Council of Australia Submission to AG's Dept 29 May 1997.

433 The section was based on provisions contained in state and territory legislation dealing with the purchase of goods on credit: See ALRC 20 para 221. As inconsistent state law, under s 109 of the Constitution these provisions of the NSW legislation do not apply to contracts subject to the ICA or the MIA and, therefore, have almost no operation as the NSW government no longer operates a state insurer.

434 F Marks and A Balla *Guidebook to Insurance Law in Australia* 3rd ed CCH 1998, 396.

435 *Accident Insurance Mutual Ltd v Sullivan* (1986) 4 ANZ Ins Cases ¶60-748.

insurers rely on non-compliance with a term of the contract even though the insurer was not prejudiced by that non-compliance.<sup>436</sup>

9.60 Some have expressed a preference for the form of the New South Wales provision over that of ICA s 54 for its simplicity and apparent flexibility,<sup>437</sup> features in keeping with the style of the MIA.

9.61 The New South Wales provision is narrower than ICA s 54 in that it is limited to providing relief in the event of a failure by the insured to ‘observe or perform a term or condition’ of the contract and not, for example, breaches of the common law. In contrast, the ICA provisions operate whenever some act of the insured or some other person could lead the insurer to refuse to pay a claim.<sup>438</sup> This aspect of the New South Wales provision could be altered if adapted for the purposes of an amended MIA.

### ***Insurance Contracts Act 1984 (Cth)***

9.62 The common law of general insurance also recognised warranties as terms requiring strict compliance. Reform of the law relating to warranties in contracts of insurance was one of the aims of the ICA.

9.63 The Commission’s 1982 report *Insurance Contracts* (ALRC 20) considered a range of possibilities for reform of the law of general insurance relating to breaches of warranties and conditions in insurance contracts.<sup>439</sup> It was recognised that the law, which still applies in relation to contracts of marine insurance, could operate inequitably in that a breach of a term may lead to the termination of the contract regardless of whether the insurer was prejudiced by the breach.<sup>440</sup>

9.64 The options canvassed by the Commission included two approaches which preserved the insurer’s right to terminate the contract but restricted the circumstances in which that right might be exercised, and two others that involved

436 Ibid.

437 K Carruthers Submission 9.

438 *East End Real Estate Pty Ltd v CE Heath Casualty & General Insurance Ltd* (1991) 25 NSWLR 400, 403. The effect of s 18 of the Insurance Act 1902 (NSW) was considered by the New South Wales Law Reform Commission in its 1983 report on insurance contracts. The NSWLRC referred to cases which had the effect of ‘exposing possible areas where liability might be avoided by insurers upon technical grounds that are beyond the reach of s 18’, notably because s 18 did not apply to breaches of the common law duty of disclosure: New South Wales Law Reform Commission Community Law Reform Program – First Report Insurance Contracts — Non-disclosure and Misrepresentation (LRC 3) 1983. *Kolokythas v The Federation Insurance Ltd* [1980] 2 NSWLR 663; *Bazouni v Sun Alliance Insurance Ltd* (Unreported) 17 March 1981 Supreme Court of New South Wales.

439 ALRC 20 ch 8.

440 Explanatory memorandum to the ICA; *East End Real Estate Pty Ltd v CE Heath Casualty & General Insurance Ltd* (1991) 25 NSWLR 400, 404.

abolition of the right to terminate, the insurer being left with a right to damages.<sup>441</sup> The options in the first category were the following.<sup>442</sup>

- The right to termination might be limited to cases where the insured's conduct caused or contributed to the relevant loss. This approach is adopted by the Insurance Law Reform Act 1977 (NZ) s 11, discussed above.
- An insurer could be prima facie entitled to reject a claim for breach of warranty, but the insured entitled to recover the loss on proof either (i) that the warranty was intended to reduce the risk of a particular type of loss, different from the type of loss that actually occurred, or (ii) that the insured's breach could not have increased the risk that the loss would occur in the way in which it did occur. This approach was recommended by the UK Law Commission in its 1980 report.<sup>443</sup>

9.65 The second category involved abolishing the right to terminate and substituting a right to damages, assessed in accordance either with the principle of proportionality<sup>444</sup> or by reference to whether the insured's breach caused or contributed to the loss.

9.66 The Commission concluded that a test based on causation, whether formulated as a limitation on the right to termination or as the criterion for the award of damages, is clearly preferable where the insured's conduct is of a type that may cause or contribute to a loss.<sup>445</sup> However, the Commission noted that such an approach would deprive the insurer of all remedy where there is merely a statistical correlation between the conduct and an increase in the risk. In such circumstances, therefore, acceptable underwriting practices would be seriously inhibited.<sup>446</sup>

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441 ALRC 20 para 224.

442 Ibid para 225.

443 UK Law Commission Insurance law — Non-disclosure and Breach of Warranty Law Comm No 104 1980 para 10.36.

444 In this context, the 'principle of proportionality' is taken to refer to the approach to remedies for non-disclosure found in the law of France and some other European countries. Briefly, an insurer is obliged to pay the proportion of the claim which the actual premium paid bears to the premium which would have been payable if the material facts had been disclosed: see para 10.109; ALRC 20 para 188, 226. Adopting this principle to remedies for breach of warranty would mean that an insurer would be obliged to pay the proportion of the claim which the actual premium paid bears to the premium which would have been payable if the insurer had known that the breach of warranty would occur. However, the term 'proportionality' is also commonly used by those interested in reform of insurance law, including in consultations and in submissions to this inquiry, to refer to where the insured may recover only that part of the loss that was not caused by the insured's breach of warranty ie ICA s 54(4).

445 ALRC 20 para 228.

446 Ibid.

9.67 In this context, the Commission referred to warranties concerning unlicensed motor vehicle drivers, named drivers, and drivers under a particular age. This observation could be applied to marine insurance warranties relating to, for example, manning or other requirements. While the UK Law Commission's test would overcome the problem, the Commission concluded that it would do so at the price of doing serious injustice to some insureds where the remedy of termination would be seriously disproportionate to the harm caused by the insured's breach.

9.68 The Commission concluded that the only satisfactory solution was a combination of two tests: a test based on potential causation (to determine whether the insurer may terminate the contract) and, where termination is not available, an insurer's right to damages, exercisable by way of reduction of the amount payable in response to a claim. This position was reflected in ICA s 54.

Where the conduct of the insured might, in principle, have caused or contributed to the loss, a causal connection test should be adopted. As between termination and damages in these cases, there may not be a great deal to choose. But damages provide a more flexible remedy in those rare cases where the insured's conduct caused or contributed to only a part of the loss. Given the insured's superior knowledge concerning the circumstances of most losses, he should bear the burden of proof. Where the insured's conduct could not, in principle, have caused or contributed to the loss, the insurer should also be limited to a right to damages. Those damages should be assessed by reference to ordinary contractual principles. That would, presumably, involve an application of the principle of proportionality ... The actual test should be stated in terms of prejudice to the insurer.<sup>447</sup>

9.69 Section 54 reads 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 the insurer's 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.

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447 Ibid.

(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 not to do the act;

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.

9.70 An insurer cannot rely simply on a breach of a warranty or some other term of a contract of insurance to avoid liability. Section 54 allows an insurer to refuse to pay where the conduct caused or contributed to the loss but an insurer cannot refuse to pay a claim where the insured proves that the loss was not caused by the breach. Furthermore, the insurer may not refuse the claim where the insured's conduct was necessary to protect a person's safety, preserve property or it was not reasonably possible for the insured to not act in that way.<sup>448</sup> However, the insurer may have a statutory right to cancel the policy under ICA s 60.

## **The *Insurance Contracts Act* as a model for reform**

### **Warranties and other contractual terms**

9.71 Contractual terms in insurance contracts can be characterised in many ways. For example, to adopt the terminology of Kelly and Ball's *Principles of Insurance Law*, it is possible to distinguish the following types of terms in insurance contracts

- Terms that define the limits of the insurer's liability. These include terms describing the risk that is covered and exclusions from cover.
- Terms that impose obligations on the insured and conditions precedent to liability. These terms include warranties and collateral obligations.<sup>449</sup>

9.72 Whether a term imposing an obligation is an insurance warranty or a collateral obligation is a question of the construction of the contract and whether the parties intend the term to be fundamental to the contract.

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448 ICA s 54(5) cf MIA s 40.

449 D Kelly and M Ball *Principles of Insurance Law in Australia and New Zealand* Butterworths 1991, 244.

9.73 In ALRC 20, the Commission noted that, apart from imposing warranties or collateral obligations, another means for insurers to avoid an increase in risk is by careful definition of the risks in the policy. For example, cover may be suspended during the existence of specified facts or circumstances which increase the risk. Terms affecting this result were referred to as ‘temporal exclusions’.<sup>450</sup>

9.74 As was the position prior to the enactment of the ICA,<sup>451</sup> the precise remedy available to an insurer in the event of breach of a marine policy may depend on matters of form rather than of substance. The wording of the particular clause is crucial. Warranties can easily be drafted as exclusions from cover. For example, a hull insurance policy may state that the insured ‘warrants’ that a fishing vessel will not be let out on hire or charter or, alternatively, may include an exclusion stating that the cover does not apply if the vessel is let out on hire or charter. If the insured does let the vessel out on hire and loss does not occur on that occasion but on a subsequent occasion when the insured is in charge of the vessel, the insurer is able to avoid liability for loss if the policy contains a warranty but not if the provision is construed as an exclusion.<sup>452</sup>

9.75 In other circumstances where the insured’s conduct is not covered by a warranty but by an exclusion, the consequences for the insured may be just as harsh. If the fishing vessel is let out for hire and suffers a loss not connected to the hire — for example, because of fire caused by a mechanical defect covered by a clause in the policy — while there may be no question of breach of warranty or of termination of the contract, the loss may not be recoverable.

9.76 In ALRC 20, the Commission concluded that

Simplification of terminology and of the rules governing the effect of the insured’s conduct prior to a loss is obviously necessary. The effect of a term should not depend on whether it is in the form of a warranty or a condition. Similarly, the difference in effect between breach of warranty and the occurrence of an excluded loss is not justified. The rights of the parties should depend on matters of substance, not on subtle differences in form.<sup>453</sup>

9.77 Accordingly, s 54 of the ICA was drafted in such a way that it applies to any term of a contract the effect of which is to allow the insurer to refuse to pay a claim by reason of an act occurring after the contract was entered into.<sup>454</sup> A similar approach must also be an essential part of the drafting of the proposed reforms to the law relating to marine insurance warranties.

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450 See ALRC 20 para 217.

451 Ibid para 218.

452 See ALRC 20 para 220 discussing *Azevedo v Australian & International Insurances Ltd* unreported Northern Territory Supreme Court 18 August 1976.

453 Ibid para 224.

454 See ICA s 54, para 9.69 above.

### The ambit of s 54

9.78 The question concerning the categories of act or omission covered by s 54 has been a matter of some legal controversy. For example, it has been suggested that the protection that s 54 provides should extend only to an insured's breach of terms which are conditions to be satisfied by the insured but not to terms that might extend the scope of the cover itself.<sup>455</sup>

9.79 To date, most of the cases in which this issue has arisen have involved 'claims made' or 'claims made and notified' policies of liability insurance and situations where the insured has failed to notify the insurer of circumstances that might give rise to a claim against the insured.

9.80 However, the issue has broad implications for marine insurance, if a provision similar to s 54 were to be enacted in the MIA. These implications arise not just because marine insurance includes marine liability insurance, but also because of the possible effects on the operation of 'held covered' clauses and other terms that allow for the extension of the cover provided by a policy on the giving of notice by the insured.

### Claims made policies

9.81 Some forms of liability insurance<sup>456</sup> apply to claims made against the insured within the period of cover ('claims made' policies), rather than to events which occurred within that period ('occurrence based' policies). Claims made policies recognise that claims are often not made until many years after the event giving rise to liability takes place.

9.82 Many such policies provide coverage only for claims which are both made and notified to the insured within the period of cover ('claims made and notified' policies). Claims made and notified policies usually extend to cover claims made and notified *after* the period of insurance expires provided that such claims arise out of an occurrence notified to the insurer within the period of insurance. A common drafting mechanism to achieve this contractual extension in cover is a deeming clause under which a claim arising from facts notified to the insurer within the period of insurance is deemed to be a claim made during the policy period, even if actually made after that period.<sup>457</sup>

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455 Greentree v FAI General Insurance Co Ltd (1998) 158 ALR 592.

456 The reported cases have most often involved forms of professional indemnity insurance.

457 eg Condition 3 of the contract at issue in FAI General Insurance Co Ltd v Perry (1993) 30 NSWLR 89, 99.



9.83 Claims made and notified policies address a dilemma that would otherwise be faced by the insured under a professional indemnity or other liability policy.

If at the end of a policy period the insured was aware of facts that might give rise to a claim and disclosed those facts in the proposal for renewal, the insurer might exclude any claims rising out of those circumstances in the renewal cover. The insured's only alternative would be to encourage the client who might make a claim to do so during the policy period. Such a course of action was obviously not desired by either the insured professional or the insurer and would probably be a breach of the duty of utmost good faith.<sup>458</sup>

9.84 There are also advantages for insurers in offering claims made and notified cover. Insurers can close their books with certainty at a specific date and calculate reserves for further liabilities and premium. The risk of disputes between an insurer on risk at the time of the circumstances of the claim and the insurer on risk at the time the claim was actually made is also reduced.<sup>459</sup>

9.85 In ALRC 20, the Commission concluded that additional cover of the type provided by claims made and notified policies should be made mandatory by legislation. This recommendation was subsequently reflected in s 40 of the ICA, which states as follows.<sup>460</sup>

(1) This section applies in relation to a contract of liability insurance the effect of which is that the insurer's liability is excluded or limited by reason that notice of a claim against the insured in respect of a loss suffered by some other person is not given to the insurer before the expiration of the period of the insurance cover provided by the contract.

...

(3) Where the insured gave notice in writing to the insurer of facts that might give rise to a claim against the insured as soon as was reasonably practicable after the insured became aware of those facts but before the insurance cover provided by the contract expired, the insurer is not relieved of liability under the contract in respect of the claim, when made, by reason only that it was made after the expiration of the period of the insurance cover provided by the contract.

9.86 The effect of s 40 of the ICA is to allow an insured to notify the insurer of its knowledge of facts that might lead to a claim and thereby ensure that any claim arising from those facts will be covered, whenever it is made, provided that notification of facts is made as soon as reasonably practicable and before the insurance cover expired.

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458 G Masel 'Taking Liberties with Claims Made Policies' (2000) 11(2) Insurance Law Journal 104, 105. Failure to disclose would also be a breach of the duty of disclosure and lead to the insurer avoiding liability for the claim under the renewed policy.

459 Ibid.

460 ALRC 20, Summary of recommendations para 40; Appendix A Draft Insurance Contracts Bill 1982 cl 41.

9.87 A literal construction of ICA s 40(1) would tend to suggest that the section does not apply to a claims made policy because, under such a policy, the exclusion from liability does not arise because notice of a claim was not given to the insurer but because no claim was made during the period of the insurance. However, in *Newcastle City Council v GIO*<sup>461</sup> the High Court considered the legislative history of s 40, including its origins in ALRC 20,<sup>462</sup> and confirmed that the operation of s 40 extends to claims made as well as claims made and notified policies.<sup>463</sup> In this case, the Council was insured under a claims made policy. Following the Newcastle earthquake in 1989, and within the period of cover, the Council had notified the insurer about potential claims against the Council for damage to the Newcastle Workers Club. The High Court found that the insurer was obliged to indemnify the Council. Professor Sutton has concluded that, as result of this decision

[p]rotection in respect of a claim made after expiry of the cover will be mandatory where notice of an occurrence giving rise to a potential claim has been given to the insurer as soon as reasonably practicable, once the assured has been apprised of the claim, provided that it is given while the policy is still current.<sup>464</sup>

9.88 Where notification of facts does not take place within the required period or there are other reasons the insured may not rely on ICA s 40, the insured party under a contract of liability insurance may seek to invoke the broader provisions of ICA s 54.

### The case law

9.89 The following discussion briefly summarises relevant case law on ICA s 54. The decision of the High Court in *FAI General Insurance Co Ltd v Australian Hospital Care Pty Ltd*<sup>465</sup> was not available when this report was prepared and the Commission anticipates that it may change or clarify the law in this area.

461 (1997) 191 CLR 85; (1997) 149 ALR 623.

462 (1997) 191 CLR 85, 89–101 (Toohey, Gaudron, Gummow JJ), 110–112 (McHugh J); (1997) 149 ALR 623, 631–3 (Toohey, Gaudron, Gummow JJ), 640–1 (McHugh J).

463 McHugh J stated that when extrinsic material, which included the Commission’s discussion paper (ALRC DP 7), report (ALRC DP 20) and the explanatory memorandum to the Insurance Contracts Bill 1984, was properly taken into account, it could be concluded that had parliament had the defects in the drafting of s 40 drawn to its attention it would have overcome it by adding at the end of s 40(1) the words ‘because no claim was made against the insured before that period expired’.

464 K Sutton ‘The High Court Widens the “Reach” of the Insurance Contracts Act’ (1998) 26 Australian Business Law Review 57, 60. Sutton observes ‘It is possible that in future insurers will cease to include extension of cover (or “occurrence notification”) clauses in their policies of liability insurance (unless their retention will be useful as a marketing exercise) and will instead leave the assured to invoke s 40(3) in an appropriate case’: 59–60.

465 On an appeal, heard on 17 November 2000, from the decision of the Queensland Court of Appeal in *FAI General Insurance Co Ltd v Australian Hospital Care Pty Ltd* (1999) 153 FLR 44.

9.90 In *East End Real Estate Pty Ltd v CE Heath Casualty & General Insurance Ltd*<sup>466</sup> the New South Wales Court of Appeal found that ICA s 54 applied to a claims made and notified policy where the insured failed to give notification of a claim during the period of cover.<sup>467</sup> The Court of Appeal rejected an argument that s 54 does not apply to acts or omissions which form part of the definition of the risks insured, referring to the legislative intention that the parties' rights be determined not by the form in which the contract is drafted but by reference to the harm caused.<sup>468</sup> However, Gleeson CJ noted that there might be a valid distinction between omissions and simple 'non-events' such as where no claim was made on the insured by a third party during the period of cover.<sup>469</sup>

9.91 In *FAI General Insurance Co Ltd v Perry*<sup>470</sup> the New South Wales Court of Appeal by majority<sup>471</sup> decided that the section did not apply to a claims made and notified policy where the failure was to give notification of facts that might give rise to a claim when the facts were known to the insured during the period of insurance but the claim itself was not made until after the insurance had expired. In *Perry*, the Court of Appeal held that the insured's failure to notify the insurer of the facts giving rise to a claim was not an 'omission' within the meaning of s 54 because the insured had a choice whether or not to notify the insurer and thereby expand the scope of cover of the policy<sup>472</sup> and because the insured lost no previously existing right by reason of the failure to notify.<sup>473</sup>

9.92 The broader implications of the issue dealt with in *Perry* are illustrated by the fact that its reasoning has been applied outside the liability insurance context, for example in the Supreme Court of Western Australia's decision in *Kelly v New Zealand Insurance Co.*<sup>474</sup> This case involved a home and contents policy under the terms of which the insured could have extended its cover by providing the insurer with a list of specific items, but chose not to. The Court referred to the distinction between an 'omission' entitling the insurer to refuse to pay a claim, which is covered by the ambit of s 54, and the exercise by the insured of a right not to expand the scope of cover, which in this case was not.<sup>475</sup>

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466 (1991) 25 NSWLR 400.

467 And, therefore the insured could not rely on ICA s 40.

468 (1991) 25 NSWLR 400, 404.

469 Ibid 405. This reasoning was later adopted by Spigelman CJ in *Greentree v FAI General Insurance Co Ltd* (1998) 158 ALR 592, 595.

470 (1993) 30 NSWLR 89.

471 Gleeson CJ and Clarke JA, Kirby P (dissenting).

472 (1993) 30 NSWLR 89, 93.

473 Ibid 107.

474 (1996) 130 FLR 97.

475 Ibid 110 (Owen J).

9.93 The correctness of the decision in *Perry* was thrown into doubt by the subsequent decision of the High Court in *Antico v Heath Fielding Australia Pty Ltd*.<sup>476</sup> *Antico* involved legal expenses indemnity insurance. The policy provided that the insurer would not be liable to indemnify the insured unless the insured obtained the specific consent of the insurer, which the insurer was only obliged to give if the insurer had reasonable grounds for defending the proceedings or for the successful outcome of any matter. The policy contained detailed provisions concerning how the existence of reasonable grounds was to be established. The insured had failed to obtain the insurer's consent to incur legal costs in defending proceedings against him.

9.94 The majority of the High Court<sup>477</sup> found that s 54 could be relied upon by the insured to remedy the failure to obtain consent. The Court referred to the remedial character of s 54 and concluded that it would not be appropriate to deny s 54 operation because the insurer may have denied consent.<sup>478</sup>

The legislation is expressed in broad terms and, on its face, there is no reason why the omission of the insured may not be a failure to exercise a right, choice or liberty which the insured enjoys under the contract of insurance.<sup>479</sup>

9.95 The majority stated that s 54 does not require the act or omission to be the sole or unique cause of the entitlement of the insurer to refuse the claim.<sup>480</sup> The High Court expressly rejected the reasoning in *Perry*, at least to the extent that this reasoning was based on a distinction between an omission, which is a failure to comply with an obligation, and an inaction, such as failure to exercise a choice, which was found not to amount to an omission under s 54.

9.96 In *Greentree v FAI General Insurance Co Ltd*,<sup>481</sup> the New South Wales Court of Appeal held that the failure by a third party<sup>482</sup> to make a claim was not an 'omission ... of some other person' within the terms of ICA s 54(1). The Court returned to the distinction between an omission, in terms of s 54, and a non-event. Spigelman CJ stated that an omission is a non-event in the sense of conduct wholly external to the policy itself.<sup>483</sup> Mason P referred to the words of Brennan CJ in

476 (1997) 188 CLR 652.

477 Dawson, Toohey, Gaudron and Gummow JJ. Brennan CJ dissented on this point, finding that the failure to comply with the condition to seek the insurer's consent would be an omission to which s 54 applied only if, before the expenses were incurred, there were reasonable grounds for defending the proceedings or for the successful outcome of the matter.

478 As the New South Wales Court of Appeal had earlier decided: *Antico v CE Heath Casualty and General Insurance Ltd* (1996) 38 NSWLR 681.

479 *Antico v Heath Fielding Australia Pty Ltd* (1997) 188 CLR 652, 669.

480 *Ibid* 672–73.

481 (1998) 158 ALR 592.

482 In the other cases discussed above, the relevant act or omission invoking the operation of s 54 was clearly on the part of the insured rather than a third party.

483 (1998) 158 ALR 592, 595.

*Antico*<sup>484</sup> where he stated that s 54 does not operate to alter the contractual promise of the insurer to pay a claim and emphasised the difference between a failure to notify an insurer of a notifiable event and a failure to expand the scope of cover,<sup>485</sup> recognised in *Kelly v New Zealand Insurance Co.*<sup>486</sup> While the decision in *Antico* had rejected any rigid dichotomy between an omission and inaction, Mason P stated that ‘*Perry* stands on a wider base than this and its correctness in point of decision has not been undermined by the High Court’s judgment in *Antico*.’

9.97 Supporting the reasoning of Mason P, Professor Sutton explains the distinction between *Antico* and *Perry* as resting on whether there is a sufficient causal connection between the terms of the policy and the insurer’s refusal to pay the particular claim.

In a situation outside the ambit of s 54(1), the effect of the contract is that the assured is not entitled to an indemnity in respect of a claim which is foreshadowed but may not yet have been made, unless and until notice is given by the assured extending the scope of the indemnity to meet that claim if and when made. Such notification is not merely procedural but is a substantive step to take, and there is not a sufficient causal connection between the failure to act and the insurer’s refusal to pay the subsequent claim.<sup>487</sup>

9.98 Other cases since *Antico* have held that *Perry* has been overruled. In *FAI General Insurance Co Ltd v Australian Hospital Care Pty Ltd*<sup>488</sup> the Queensland Court of Appeal held that s 54 applied to a failure by an insured under a professional indemnity claims made policy to give notice of facts during the period of cover that might give rise to a claim. A similar decision was reached in *Einfeld v HIH Casualty & General Insurance Ltd*,<sup>489</sup> by Rolfe J in the New South Wales Supreme Court, notwithstanding that the insured had decided not to give notice to the insurer after considering a possible increase in insurance premiums and receiving legal advice.<sup>490</sup>

9.99 An appeal from the decision in *FAI General Insurance Co Ltd v Australian Hospital Care Pty Ltd*<sup>491</sup> was heard by the High Court in November 2000. As stated, the judgment of the Court may help clarify the law in this area.

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484 *Antico v Heath Fielding Australia Pty Ltd* (1997) 188 CLR 652, 661.

485 (1998) 158 ALR 592, 607.

486 (1996) 130 FLR 97.

487 K Sutton *Insurance Law in Australia* 3rd ed LBC Information Services Sydney 1999, 680–3, 686. See also J Clarke ‘After the dust settles on *Antico*: *FIA v Perry Lives*’ (1997) 9 *Insurance Law Journal* 29, 36–7.

488 *FAI General Insurance Co Ltd v Australian Hospital Care Pty Ltd* (1999) 153 FLR 44.

489 (1999) 166 ALR 714.

490 *Ibid* 716.

491 (1999) 153 FLR 44.

## Commentary

9.100 These decisions have been the subject of considerable critical analysis by legal commentators.<sup>492</sup>

There is now a considerable body of jurisprudence on the subject of s 54 which appears to have taken on a life of its own. Although the courts initially responded to novel fact situations by introducing legal distinctions which could place some rational limit on the operation of s 54, over the years they have tended to become preoccupied with the legal distinctions themselves. In doing so, the courts have lost sight of both the intended scope of reforms intended by the drafters of the ICA and the commercial realities underlying claims made cover.<sup>493</sup>

9.101 Most of this criticism has focussed on the implications for claims made policies. Geoff Masel has stated that recent decisions have delivered a ‘serious blow to the viability of claims made professional indemnity insurance policies’ and have taken s 54 beyond the reforms intended to be achieved by the ICA.<sup>494</sup> Masel observes that s 40 of the ICA was specifically designed to deal with claims made policies and there is nothing in ALRC 20 which suggests that the failure by an insured to exercise rights granted by a deeming clause or by ICA s 40(3) should in any way be subject to s 54.<sup>495</sup> He expresses concern that courts have not understood that the peril insured against under a claims made professional indemnity policy is not legal liability but the making of a claim, a quite different concept. While the deeming clause expands the meaning of the making of a claim it does not convert the policy into an occurrence based policy.<sup>496</sup>

If the courts cannot accommodate a workable distinction exempting acts and omissions which define or extend the scope of cover from the operation of s 54, it appears that a legislative intervention may provide the only solution.<sup>497</sup>

9.102 Others have argued that s 54 now has a much wider application than envisaged by the framers of the legislation and that amendments are required to deal with claims made policies. Patrick Mead has proposed an amendment to s 54 which, as well as confirming the outcome in *Perry*, would also reverse the *East*

492 See eg A Schoombee ‘Antico’s Case and Other Recent Decisions on Notification of Claims and Circumstances: Sections 54 and 40 of the Insurance Contracts Act’ (1997) 8 Insurance Law Journal 167; P Mead ‘The Effect of Section 54 of the Insurance Contracts Act 1984 and Proposals for Reform’ (1997) 9 Insurance Law Journal 1; J Clarke ‘After the Dust Settles on Antico: FIA v Perry Lives’ (1997) 9 Insurance Law Journal 29; G Masel ‘Taking Liberties with Claims Made Policies’ (2000) 11(2) Insurance Law Journal 104.

493 G Masel ‘Taking Liberties with Claims Made Policies’ (2000) 11(2) Insurance Law Journal 104, 104.

494 Ibid.

495 Ibid 107.

496 Ibid 110–11.

497 Ibid 111. Masel suggests providing in the ICA that a failure to give notice of facts or circumstances within the meaning of s 40(3), or a similar clause in the policy, shall not be construed as an omission under s 54.

*End* decision by excluding from the operation of s 54 a failure to notify both a claim or an occurrence which might give rise to a claim.<sup>498</sup>

### Implications for marine insurance

9.103 The case law discussed above has obvious implications for marine liability insurance if an amended MIA were to incorporate the wording of ICA s 54. Some forms of liability insurance covered by the MIA may be written on a claims made and notified basis. However, claims made and notified liability insurance may be less common in marine insurance than in some other areas of insurance practice. For example, the major category of marine liability insurance, P&I insurance, seems to be written on an occurrence basis.<sup>499</sup> It is also common for ship repairers' liability policies to be written on an occurrence basis.<sup>500</sup>

9.104 As noted, the decision of the High Court in *FAI General Insurance Co Ltd v Australian Hospital Care Pty Ltd*<sup>501</sup> may help to clarify whether the decision in *Antico* means that ICA s 54 operates where an insured fails to exercise rights granted by a deeming clause or by ICA s 40(3).

9.105 However, as noted above, there are broader implications for marine insurance, relating among other things to the operation of 'held covered' clauses and other terms that allow for the extension of the cover provided by a policy on the giving of notice by the insured. Whatever position is established by the High Court in relation to notification of claims under liability policies, the reasoning in *Antico* appears capable of applying to such notice clauses so that an omission to give notice to the insurer may be curable by s 54.

9.106 For example, the Institute Time Clause Hulls contract terms contain a 'held covered' clause that holds the insured covered for a breach of warranty as to cargo, trade, locality, towage, salvage services or date of sailing if notice is given to the insurer and any amended terms of cover and additional premiums are agreed.<sup>502</sup> If an equivalent to ICA s 54 was applicable to marine insurance contracts, an insured who failed to give notice to the insurer might be able to invoke such a provision.

498 P Mead 'The Effect of Section 54 of the Insurance Contracts Act 1984 and Proposals for Reform' (1997) 9 Insurance Law Journal 1, 27. See also the comments of David Kelly that any change to s 54 should be the minimum required to deal with the peculiarity of claims made liability insurance, recorded by Kirby J in *FAI General Insurance v Perry* (1993) 30 NSWLR 89, 103. See also J Clarke 'After the Dust Settles on *Antico*: *FIA v Perry Lives*' (1997) 9 Insurance Law Journal 29. Clarke argues that an expansion in the scope of the policy, including by notifying facts or circumstances under a claims based policy, effectively creates a new contract of insurance and so a failure to exercise rights under such a term should not be able to be cured by s 54: 37.

499 eg The Shipowners' Mutual Protection and Indemnity Association (Luxembourg) Class 1 Rules 2000 Rule 1, section 6.

500 The policy will generally exclude damage reported more than 12 months after delivery of the vessel to its owners: Broker Consultation Perth 23 November 2000.

501 (1999) 153 FLR 44.

502 ITC Hulls cl 3.

Following *Antico*, the fact that the insurer might refuse to renegotiate the contract if approached is not a barrier to the operation of s 54.

9.107 Section 54(1) reduces the insurer's liability to the extent of the prejudice it suffers as a result of the act or omission. Therefore, it is open to the insurer to show that the insurer would not have agreed to extend the cover. Patrick Mead has observed that

[i]n emphasising the remedial nature of the legislation and construing the language of s 54 to give the most complete remedy fairly available on the words of that section, the High Court has lowered the "threshold" question of the applicability of s 54(1) to a particular act or omission. By "lowering the bar", as it were, the High Court has evidenced an intention to allow an insured more readily to take the benefit of s 54(1) in appropriate circumstances, adopting the view that an insurer will be provided with adequate protection of its interests by the application of the "prejudice test" within the second limb of s 54(1).<sup>503</sup>

### The prejudice test

9.108 In contrast to the threshold question of the applicability of s 54, the operation of the prejudice test under s 54(1) appears to be well established. The leading authority is the High Court case *Ferrcom Pty Ltd v Commercial Union Assurance Co of Australia Ltd*.<sup>504</sup> In *Ferrcom*, a mobile crane was insured against physical loss, destruction or damage. At the time of issue of the policy the crane was not registered to be driven on public roads. However, it was registered some months later. Notification of this change in circumstance was not passed on to the insurer by the broker, contrary to a clause in the policy which made the insurer's liability conditional on the insured notifying the insurer of any material change in circumstances. When an accident occurred, the insurer denied liability on the basis of this clause.

9.109 *Ferrcom* confirmed that the prejudice to the insurer may consist of both the additional premium that would have been payable to cover any increased risk and loss of the opportunity to cancel the policy.<sup>505</sup>

9.110 In assessing the quantum of the prejudice suffered by the insured, three possible tests have been suggested: a subjective test based on the position of the actual insurer; an objective test based on the position of a reasonable insurer; and an equitable test based on principles of fairness between the insured and the insurer.<sup>506</sup>

503 P Mead 'The Effect of Section 54 of the Insurance Contracts Act 1984 and Proposals for Reform' (1997) 9 Insurance Law Journal 1, 13.

504 (1993) 176 CLR 332.

505 Ibid 342.

506 J Mannolini 'The Uncertain Ambit of Section 54 of the Insurance Contracts Act' (1996) 24 Australian Business Law Review 260, 270.



9.111 In *Ferrcom*, the High Court found in favour of the subjective test<sup>507</sup> and determined on the evidence that, had the insurer received notification of the public road registration, it would have exercised its right to cancel the policy. The prejudice to the insurer was found to be equivalent to the entire liability of the insurer. The High Court subsequently confirmed this approach in *Antico*.<sup>508</sup>

## Reform of express warranties

### Abolition of express warranties

9.112 In her 1998 thesis, Dr Derrington suggested that the concept of a warranty as it exists in Anglo-Australian marine insurance law should be abolished.

The use of warranties ... as a means of delimiting the risks or dealing with alterations to the risk is clumsy, uncertain and, in some respects, unfair. Despite the nine provisions in the *Marine Insurance Act* which deal with warranties only two warranties are in fact provided for in the *Marine Insurance Act*, the implied warranty of seaworthiness in a voyage policy and the implied warranty that the adventure is lawful. Most warranties in Anglo/Australian law are express, and the ones which are contained in policies most frequently relate to classification, trading limits, disbursements, towage and salvage. These matters can quite simply be incorporated into a standard policy form.<sup>509</sup>

9.113 Dr Derrington suggested replacing the concept of express warranties with an obligation on the insured to notify the insurer of any change in the circumstances which forms the basis of the contract of insurance and which alters the risk. Under this proposal, in the case of an alteration of risk, the insurer would escape liability in circumstances where the loss is attributable to the alteration of risk but only where the insurer would not have entered into the contract on any terms had the insured known of the alteration at the time when the contract was concluded and the insured either intentionally caused or agreed to the alteration of risk, or failed to promptly notify the insurer of the alteration.<sup>510</sup>

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507 *Ferrcom Pty Ltd v Commercial Union Assurance Co of Australia Ltd* (1993) 176 CLR 332, 341.

508 *Antico v Heath Fielding Australia Pty Ltd* (1997) 188 CLR 652, 673–4.

509 S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' Ph D thesis University of Queensland November 1998, 336–7.

510 *Ibid* 338, Draft provision A4.

### **Submissions on reform of express warranties**

9.114 The Commission found much support for reform of the law on warranties in submissions to the inquiry.<sup>511</sup> However, many of those in favour of reform emphasised the need for measured reform.

ICA [the Insurance Council of Australia] agrees that warranty provisions are in need of reform. It is difficult to sustain the view that different rights and liabilities can be imposed on the insured in a marine insurance contract than exists in general insurance. [The Insurance Council's] concern is that in seeking a basis of reform, Australia's international competitiveness must not be put at risk by any substantive change to the Act, which place it beyond the boundaries of international acceptance. Rather the solution should be developed, wherever possible, in conformity with international practice.<sup>512</sup>

9.115 Most suggestions for reform focus on introducing requirements that the breach be material to, or causative of, the loss before an insurer may avoid or reduce its liability. Such a reform would be in broad conformity with international practice, certainly in civil code countries and in some common law jurisdictions, whether as a result of statutory reform, as in New Zealand, or judicial interpretation, as in Canada.

9.116 The Commission did not identify any significant opposition to the idea that a breach of warranty that is remedied before loss should not lead to the discharge of the insurer's liability. Most submissions also agreed that an element of causation should be introduced but there was no clear agreement on the mechanism and in particular on whether any form of proportionality should be introduced.

9.117 The Law Society of Western Australia suggested that the extent to which the insurer is discharged should be proportional to the degree to which the breach caused or contributed to the loss.<sup>513</sup> Others disagreed with introducing such a principle.<sup>514</sup>

Section 54 has the benefit now of considered judicial analysis. The point has been well made however that it is more consumer oriented than one would expect in legislation dealing with marine insurance which operates in the vast majority of cases in a wholly commercial context.<sup>515</sup>

511 P Grieve Submission 6; Law Society of WA Submission 7; K Carruthers Submission 9; Insurance Council of Australia Submission 11; Gault Armstrong & Kemble Submission 17. Support for reform of the warranty provisions was also expressed in many consultation meetings.

512 Insurance Council of Australia Submission 11. The Council states that '[a]ny breach of warranty and its result should incorporate the doctrine of causation'.

513 Law Society of WA Submission 7.

514 A Street Submission 15; K Carruthers Submission 9.

515 K Carruthers Submission 9. Others have suggested that ICA s 54 'sounds more useful than it has been' and that, while academically interesting, it has not often been of practical use: Advisory Committee meeting 18 December 2000.

9.118 Dr Derrington provided detailed proposed provisions relating to reform of express warranties, assuming such a concept was to be retained.<sup>516</sup> These provisions would introduce elements of causation and knowledge, and would provide for different remedies depending on a range of factors, including whether

- the insured notifies the insurer about the breach
- the insurer would have entered the contract had it known that the breach of warranty would occur
- the breach of warranty was intentionally caused by the insured, and
- loss is attributable to the breach of warranty.

9.119 The insurer's remedies for breach of warranty vary in scope depending on the circumstances of the breach. These remedies may include complete freedom from liability, termination of the insurance on notice, retention of the premium and rights to demand a proportionate additional premium.<sup>517</sup>

### **Adapting ICA s 54**

9.120 Section 54 has broad operation. Adapting this provision as a model for reform of the MIA would be a sweeping reform. In important respects, the practical effect of the operation of s 54 is to allow the insured to unilaterally alter the bargain made by the parties, arguably to the extent of fundamentally changing the scope of the insurance (see paragraphs 9.100–9.102). While the insurer's liability may be reduced to the extent of the prejudice it suffers, even to zero, the room for dispute over whether or not a particular marine insurance claim is payable, and the extent to which it is payable, would be greatly expanded.

9.121 A related objection to the ICA model relates to the element of proportionality it introduces. Under the ICA, even where a breach of warranty could reasonably be regarded as being capable of causing or contributing to a loss, the insured is still entitled to claim under the policy if the insured proves that either 'no part of the loss that gave rise to the claim was caused by the act' or 'some part of the loss that gave rise to the claim was not caused by the act'.<sup>518</sup> This approach may lead to practical difficulties in quantifying an insurer's liability. Concerns have been expressed about resultant uncertainty and the cost of litigating disputes about quantification of liability under a proportionality principle.<sup>519</sup>

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516 S Derrington Submission 13.

517 Ibid.

518 ICA s 54(3) and (4).

519 MLAAZ member Consultation Queenstown 8 September 2000; Advisory Committee meeting 18 December 2000.

9.122 The ICA model has some advantages. Section 54 addresses warranties and all similar contractual terms that allow an insurer to refuse to pay a claim by reason of some act of the insured and, while there has been some uncertainty over its ambit,<sup>520</sup> case law now exists to guide the interpretation of this provision. In any event, most of the litigated areas of uncertainty would arise in a small minority of policies covered by the MIA.

9.123 However, the Commission has concluded that the ICA reforms do not provide a suitable model for MIA reform. The ICA provisions are broader than necessary to address the deficiencies of the present law of marine insurance. In particular, the Commission's recommended amendments to the MIA relating to the consequences of a breach of an express contractual term by the insured do not include an element of proportionality as found in ICA s 54.

### **Causation**

9.124 In insurance law, as in many other areas of the law, causation can be a difficult issue. In marine insurance, as many losses occur because of a combination of factors, the liability of the insurer may depend on fine distinctions being drawn between proximate, immediate and remote causes.

9.125 During consultations concern was expressed that adopting the ICA s 54 formulation of causation, which refers to acts 'causing or contributing to a loss',<sup>521</sup> would be overly prejudicial to the insured. The insurer might be entitled to avoid liability if there was any connection between the breach of warranty and the loss.<sup>522</sup>

9.126 Alexander Street SC submitted that the insurer should only be entitled to avoid for a breach that was a proximate cause of the loss and that the notion that there may be dual or multiple proximate causes should be expressly recognised. He added that

the proportionate diminution of insurer's liability by a reason of a breach with indirect causal effect or contribution to the loss is a recipe for unmeritorious pressure to be exerted by the insurer on the insured.<sup>523</sup>

9.127 The Commission agrees that an insurer should be able to avoid liability only where the loss in respect to which the insured seeks to be indemnified was proximately caused by the breach of warranty. The phrase 'proximately caused by'

520 See para 9.77.

521 ICA s 54(1)–(2). Kelly and Ball state that there appears to be no significance in the omission of 'contributes' in ICA s 54(3)–(4): D Kelly and M Ball *Principles of Insurance Law in Australia and New Zealand* Butterworths 1991, 272 fn 222.

522 Advisory Committee meeting 18 December 2000.

523 A Street Submission 15.

is used in MIA s 61, is a well understood insurance law concept and is subject to comprehensive and complex case law.<sup>524</sup> For example, it is established that where there are several competing proximate causes and where one of the proximate causes is specifically excluded, the exclusion prevails and the insurer is not liable.<sup>525</sup> Similarly, under the Commission's recommended reforms, where a breach of warranty is one of several proximate causes of loss the insurer would not be liable, notwithstanding that an insured peril is also a proximate cause.

### **Burden of proof**

9.128 It is existing law that the burden of proving the breach of warranty is on the insurer, even where compliance is a condition precedent to recovery under the policy.<sup>526</sup> This should remain the position but, given the insured's superior knowledge concerning the circumstances of most losses, the insured should have the burden of proving that the breach of a contractual term did not cause the loss.<sup>527</sup> To remove any doubt, this should be specified in the amending legislation, as it is under ICA s 54 and Insurance Law Reform Act (1977) (NZ) s 11.<sup>528</sup> This position should apply to breaches of all contractual terms.

### **Conclusions in relation to express warranties**

9.129 The Commission's recommendations relating to express warranties are set out at the end of this chapter together with separate recommendations relating to the implied warranties of seaworthiness and legality and other related matters. The recommendations on express warranties reflect the following conclusions of the Commission.

- The separate concept of express warranties, and the consequences that flow from a breach of express warranties under the existing law, should be abolished.
- In place of express warranties, the amended MIA should permit the parties to include a term that the insurer is discharged from liability to indemnify the insured for loss proximately caused by a breach by the insured of an express term of the contract. An express term providing for the insurer's

524 eg see H Bennett *The Law of Marine Insurance* Clarendon Oxford 1996, ch 6; ALRC DP 63 para 5.110-14.

525 *Wayne Tank & Pump Co Ltd v Employers Liability Assurance Corp Ltd* [1974] QB 57; *HIH Casualty & General Insurance Ltd v Waterwell Shipping Inc (The Alpha Kilimanjaro)* (1998) 43 NSWLR 601.

526 M Mustill and J Gilman Arnould's *Law of Marine Insurance and Average* 16th ed vol III Stevens & Sons London 1997, 528; *Bond Air Services Ltd v Hill* [1955] 2 QB 417; *Australian Associated Motor Insurers Ltd v Wright* (1997) 70 SASR 110; *Vosten v Commonwealth* [1989] 1 Qd R 693.

527 ALRC 20 para 228. In contrast, both MLAANZ and Justice Carruthers stated that the insurer should assume the burden of establishing that the loss was caused or contributed to by a breach of warranty: K Carruthers Submission 9, MLAANZ Submission 12.

528 See para 9.69, 9.53.

discharge from liability could be drafted to apply to the insured's obligations generally or only to particular breaches. In the absence of such a term, breach of the contract will entitle the insurer only to such relief as may be available under the general law of contract, which would generally be the award of damages.

- Accordingly, MIA s 39 should be amended to state that no contractual term is a warranty or has the effect that a breach of it entitles the insurer to be discharged from any liability except as is otherwise permitted by the MIA. Section 41, which specifically provides for express warranties, should be repealed.
- It is not equitable to allow an insurer the right to avoid liability where there is only a minor or immaterial breach of a contractual term by the insured. An insurer should only be automatically discharged from liability to indemnify an insured for loss proximately caused by a breach by the insured of an express contractual term. The familiar formula of proximate cause is the appropriate measure of the required causal link, rather than the more remote formula of loss 'attributable' to the breach.<sup>529</sup>
- The insurer's discharge from liability for a claim should continue to be automatic. Although not raised specifically in submissions or consultations, the Commission would reject the idea that the insurer should be required to elect to avoid liability within a reasonable period. In many cases the circumstances of a loss and the discovery of a breach by the insured will only come to the insurer's attention after the loss has occurred and a claim has been made. It would be nonsense to require the insurer to make an election and notify the insured of that election as a pre-requisite to exercising its remedies. At present the insurer's discharge from liability is automatic and, in many cases, neither party will be aware of the discharge and both will continue to act on the understanding that cover remains on foot until they become aware of the circumstances which gave rise to the discharge. In this regard, no change is proposed except that the discharge in some cases will have a more limited scope (being limited to discharge from liability for loss proximately caused by the breach).
- An insured should be able to remedy a breach of warranty so that the insurer's liability continues or is automatically reinstated once the breach is remedied. However, achieving this does not require express statutory amendment other than repeal of s 40(2) as it is a necessary consequence of the other changes recommended. If the breach is remedied before any loss is

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529 cf the Commission's recommended reforms concerning seaworthiness and legality. See para 9.170–9.175 and 9.183–9.187.

sustained, the breach has no effect on the insurer's liability as the insurer is not discharged from liability unless the breach proximately causes loss. If the breach is not remedied before it causes loss, the insurer is discharged from liability (although only for loss proximately caused by the breach). If the breach is not remedied before loss is sustained by reason of some insured cause unrelated to the breach, the breach can not be said to be a proximate cause of the loss and the insurer is not discharged from liability for the loss.

- If the whole package of changes relating to express warranties is not adopted, the Commission would recommend amending MIA s 40(2) so that the insurer's liability is automatically reinstated once a breach of warranty is remedied.
- If breach by the insured of an express contractual term is a proximate cause of loss, the insurer's discharge from liability for that loss is complete and is not further apportioned. However, the policy remains on foot in all other respects. The insurer can avail itself of the new statutory right of cancellation (see paragraphs 9.225–9.228).
- The MIA should specify that the insurer must prove the breach of a contractual term and that the insured must prove that the breach did not proximately cause the loss.
- Consequential changes should be made in MIA s 24(3)(d), s 40(1) and (3), 82(1)–(3), and 84(1) to remove the term 'warranty' and to replace it with references to contractual terms.

## Reform of implied warranties

9.130 The MIA implies two warranties into contracts of marine insurance where the contract is otherwise silent. These relate to seaworthiness and the legality of the insured adventure. The Commission proposes additional and separate reform in relation to the implied warranties of seaworthiness and legality. The warranties of seaworthiness and legality require separate consideration because of their importance to the risks covered by insurers and their role in promoting maritime safety. This approach received broad support in submissions.<sup>530</sup>

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<sup>530</sup> eg P Grieve Submission 6; K Carruthers Submission 9; Insurance Council of Australia Submission 11. Alexander Street SC expressed the view that the implied warranties should be reformed in the same manner as the express warranties: A Street Submission 15. Gault Armstrong & Kemble submitted that only the implied warranty of legality, so far as lawful purpose is concerned, should be excepted from reforms introducing a causal connection requirement: Gault Armstrong & Kemble Submission 17.

### **Implied warranty, statutory requirement or express contractual term?**

9.131 A threshold question is whether the content of these provisions should continue to be framed as implied warranties. The Insurance Council of Australia and others have suggested that the implied warranties should not ‘be implied’ but ‘stated as provisions in the Act’.<sup>531</sup> The Commission understands the effect of this suggestion to be that instead of providing that there is an implied warranty in the policy, for example that the ship shall be seaworthy, this obligation should simply be expressed as a statutory requirement so that a provision adapting MIA s 45(1) might read<sup>532</sup>

At the commencement of the voyage a ship insured under a voyage policy shall be seaworthy for the purpose of the particular adventure insured.

#### 9.132 Rather than

In a voyage policy there is an implied warranty that at the commencement of the voyage the ship shall be seaworthy for the purpose of the particular adventure insured.

9.133 Removing the language of ‘warranty’ has some attraction. The meaning of the term within marine insurance law varies from its usual meaning in general contract law and causes confusion. The Commission’s recommended reforms to express warranties are intended in part to remove any distinction between breach by the insured of an express warranty or of any other express contractual term. If these reforms were also accompanied by reforms reframing the obligations of legality and seaworthiness, this might allow the term ‘warranty’ to be removed entirely from the MIA.

9.134 Another means to achieve this would be to provide for obligations of legality and seaworthiness to be included in policies as express contractual terms. Such a reform would also be consistent with the reforms recommended in relation to express warranties. Requiring seaworthiness and legality obligations to be stated in the contract would help ensure that the insured is clearly informed about its obligations. Current marine insurance underwriting practice and standard terms incorporate clauses which deal with aspects of seaworthiness (or safety) and legality styled either as affirmative obligations on the insured’s part or as exclusions.

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531 P Grieve Submission 6; Insurance Council of Australia Submission 11.

532 Leaving aside the issue of whether the MIA should continue to distinguish between voyage and time policies: see para 9.141.



## Warranty of seaworthiness

9.135 Section 45(1)–(4) implies a warranty of seaworthiness into voyage policies. The relevant provisions read as follows.

45(1) In a voyage policy there is an implied warranty that at the commencement of the voyage the ship shall be seaworthy for the purpose of the particular adventure insured.

(2) Where the policy attaches while the ship is in port, there is also an implied warranty that she shall, at the commencement of the risk, be reasonably fit to encounter the ordinary perils of the port.

(3) Where the policy relates to a voyage which is performed in different stages, during which the ship requires different kinds of or further preparation or equipment, there is an implied warranty that at the commencement of each stage the ship is seaworthy in respect of such preparation or equipment for the purposes of that stage.

(4) A ship is deemed to be seaworthy when she is reasonably fit in all respects to encounter the ordinary perils of the seas of the adventure insured.

9.136 There is no such warranty implied into time policies but under s 45(5) the insurer is not liable for loss attributable to unseaworthiness in certain circumstances.

45(5) In a time policy there is no implied warranty that the ship shall be seaworthy at any stage of the adventure, but where, with the privity of the assured, the ship is sent to sea in an unseaworthy state, the insurer is not liable for any loss attributable to unseaworthiness.

9.137 The aim of the warranty of seaworthiness is to ensure that those with an insurable interest do not grow careless of the condition of the vessel and the safety of the crew because they have insurance cover.<sup>533</sup>

9.138 Whether a vessel is seaworthy is relative. It is related to the vessel insured and varies with changes in knowledge of, and standards for, ship construction and with the adventure to be undertaken.<sup>534</sup> Section 45(4) states that the test is one of reasonable fitness. Establishing seaworthiness may involve a consideration of the steps that would be taken by an ordinary, careful and prudent shipowner as well as objective standards, which may include the International Safety Management (ISM) Code.<sup>535</sup> Examples of unseaworthiness include a defective hull, sailing with

533 Wilkie v Geddes (1815) 3 Dow 57; Douglas v Scougall (1816) 4 Dow 269; H Bennett *The Law of Marine Insurance* Clarendon Press Oxford 1996, 293.

534 Burges v Wickham (1863) 122 ER 251; T Schoenbaum 'Warranties in the Law of Marine Insurance: Some Suggestions for Reform of English and American Law' (1999) 23 *Tulane Maritime Law Journal* 267, 303; H Bennett *The Law of Marine Insurance* Clarendon Press Oxford 1996, 294.

535 T Schoenbaum 'Warranties in the Law of Marine Insurance: Some Suggestions for Reform of English and American Law' (1999) 23 *Tulane Maritime Law Journal* 267, 303.

an open sea valve, defects in fire-fighting equipment, overloading, incompetence of crew, insufficient numbers of crew and having an unskilled master.<sup>536</sup>

9.139 In a policy on goods or other movables, there is no implied warranty that the insured goods or movables are seaworthy: MIA s 46(1). However, in a voyage policy on goods or movables, there is an implied warranty that at the commencement of the voyage the ship is not only seaworthy but also reasonably fit to carry the goods or movables to their contemplated destination: s 46(2).<sup>537</sup> Although these provisions do not seem to be the subject of much discussion, they appear to have the extraordinary effect of undermining a cargo owner's cover due to defects in the vessel over which it may have little or no control.

9.140 In practice policies for cargo insurance often contain provisions, such as those in the Institute Cargo Clauses (A),<sup>538</sup> that provide that the insurer waives any breach of the implied warranty of seaworthiness of the ship unless the insured or its servants are privy to the defect. This softens the effect of MIA s 46(2). On the other hand, a Cargo ISM Endorsement developed by the London market places the onus on the cargo owner to ensure the cargo is carried with a vessel that is ISM Code<sup>539</sup> certified or whose owners or operators hold an ISM Code Document of Compliance,<sup>540</sup> which may indirectly reinstate the adverse effect of s 46(2) on an insured cargo owner.

## Reform of the warranty of seaworthiness

### Time and voyage policies

9.141 One question is whether the distinction between voyage and time policies should be retained, at least in relation to this implied warranty (or its replacement). Importantly, under a time policy the insurer may not avoid liability on the grounds of unseaworthiness unless there is a causal relationship between the breach and the loss<sup>541</sup> as the insurer is relieved from liability only for loss 'attributable to unseaworthiness'.<sup>542</sup> Conversely, a breach of the warranty of seaworthiness in s 45(1) in a voyage policy entitles the insurer to a discharge from all liability under

536 Ibid 303–4 citing *Tropical Marine Products Inc v Birmingham Fire Insurance Co (The Sea Pak)* 247 F 2d 116, 1957 AMC 1946 (5th Cir 1957); *Commercial Union Insurance Co v Daniels* 343 F Supp 674, 1973 AMC 452 (SD Tex 1972); *Laing v Boreal Pacific* (1999) 163 FTR 226 (FCTD) (Canada); *Forshaw v Chabert* (1821) 3 Brod & B 158; *Manifest Shipping & Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [1997] 1 Lloyd's Rep 360.

537 MIA s 46(2).

538 ICC(A) cl 5.2.

539 The International Safety Management Code (ISM Code) is discussed further at para 9.192–9.202.

540 Cargo ISM Endorsement (JC 98/019, 1 May 1998).

541 MIA s 45(5).

542 The difference between a loss being 'attributable to' and 'proximately caused by' a particular cause is discussed at para 9.151–9.152.

the policy from the time of the breach. The distinction between time and voyage policies in relation to the warranty of seaworthiness<sup>543</sup> arose due to the physical difficulties of inspecting a ship under a time policy that attaches while the vessel is at sea, the ship's condition being beyond the knowledge of the owner. With voyage policies, the policy attaches while the ship is in port or at the time of sailing.<sup>544</sup>

9.142 In *Gibson v Small*<sup>545</sup> the House of Lords found that there was no evidence of custom or usage implying a warranty of seaworthiness in a time policy. A time policy may cover many voyages and it would be impossible to determine to which voyages the warranty applied. If it applied to each separate voyage, 'seaworthiness' would become a guarantee of ability to encounter every possible peril. In addition in relation to a voyage policy

both the contracting parties contemplated the state of the ship when the risk is to begin, that this state must be supposed to be known to the shipowner, that he has it in his power to put the ship into good repair before the voyage begins.<sup>546</sup>

9.143 However, in a time policy

both parties must be assumed to be in the same state of knowledge or ignorance as to the circumstances or condition of the ship.<sup>547</sup>

9.144 Under time policies the insurer must show that the insured was privy to the unseaworthiness.<sup>548</sup> This involves knowledge of the facts constituting the unseaworthiness, knowledge that those facts rendered the ship unseaworthy, and identifying whose knowledge was required.<sup>549</sup>

### **Seaworthiness and the Norwegian Marine Insurance Plan**

9.145 The provisions of the Norwegian Marine Insurance Plan provide a useful comparison with the MIA. The Norwegian Plan does not differentiate between time and voyage policies. Under the Norwegian Plan

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543 Compare MIA s 45(1) and s 45(5). For discussion of the definitions of time and voyage policies see para 15.39–15.41.

544 C Anderson 'The Evolution of the Implied Warranty of Seaworthiness in Comparative Perspective' (1986) 17(1) *Journal of Maritime Law and Commerce* 1, 3.

545 (1853) 10 ER 500.

546 *Ibid* 507.

547 *Ibid* 525.

548 MIA s 45(5).

549 M Clarke 'Good Faith and Good Seamanship: The Star Sea' (1998) 4 *Lloyd's Maritime and Commercial Law Quarterly* 465, 466.

[t]he insurer is not liable for loss that is a consequence of the ship not being in a seaworthy condition, provided that the assured knew or ought to have known of the ship's defects at such a time that it would have been possible for him to intervene.<sup>550</sup>

9.146 Unseaworthiness is not defined in the Norwegian Plan.<sup>551</sup> The commentary acknowledges that unseaworthiness varies according to the age of the ship. A ship found to be seaworthy by inspection authorities will be presumed to be seaworthy, although this is not determinative for the purposes of insurance.<sup>552</sup> In addition

[i]t does not matter whether the unseaworthiness arose before or after the ship left port. With the communication systems now available, it is easy to report defects which have arisen at sea.<sup>553</sup>

9.147 The burden of proving that the ship is unseaworthy rests with the insurer. Where a ship is unseaworthy, the insurer may terminate the insurance with 14 days' notice if the ship, by reason of defects, unsuitable construction or similar circumstances, cannot be considered seaworthy or has become unseaworthy due to a casualty or other similar circumstances, and the assured fails to have this rectified without undue delay.<sup>554</sup> The insured may still be able to recover for loss if the insured can prove that it did not know, nor ought to have known, of the defects and that there was no causal connection between the unseaworthiness and the loss.<sup>555</sup> Under the Norwegian Plan the outcome of a claim based on a loss due to unseaworthiness depends on when the insured acquired knowledge of the unseaworthiness.

Thus there is an emphasis on fault; a causal connection between the knowledge and the loss. This, it is suggested, is a much fairer position than the Anglo/Australian system. The Norwegian position reflects what is seen as the lack of need in modern times for such draconian rules. The vast improvements made in preventing loss at sea, particularly through the agency of official control and classification societies, have led to the introduction of wider rules where the question of the assured's fault is dominant.<sup>556</sup>

550 Norwegian Marine Insurance Plan cl 3-22 <http://exchange.dnv.com/nmip/books/plan> (28 March 2000).

551 The provision serves more as a rule of evidence than as a definition of seaworthiness. Seaworthiness is defined in the Seaworthiness Act of 1903: S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' Ph D thesis University of Queensland November 1998, 284.

552 Commentary to Norwegian Marine Insurance Plan cl 3-22 <http://exchange.dnv.com/nmip/books/comm> (28 March 2000).

553 Ibid cl 3-22.

554 Ibid cl 3-27.

555 Norwegian Marine Insurance Plan cl 3-22. This burden was directed to the insured in the latest version of the Plan in consideration of the increasing age of shipping fleets and the reduction in skill of deck and machine officers.

556 S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' Ph D thesis University of Queensland November 1998, 287.

9.148 Dr Derrington has also proposed that the MIA's distinction between time and voyage policies be abolished, along with the 'seaworthiness by stages' doctrine.<sup>557</sup>

The vessel should be seaworthy when leaving port but an insurer should not be liable if the vessel becomes unseaworthy after leaving port and the assured fails to take remedial steps which were available to him. This accords with the stricter Norwegian approach rather than the Anglo/Australian approach and is appropriate in light of modern concerns with respect to ship safety and marine pollution.<sup>558</sup>

9.149 In her opinion, the insurer should not be liable where the insured knows or ought to have known of the defects in the ship. The insurer should be required to prove that the vessel was unseaworthy and the insured should be required to prove that the insured did not know of the defects and that there was no causal connection between the unseaworthiness and the casualty.<sup>559</sup>

### Loss 'attributable' to unseaworthiness

9.150 At least where time policies are concerned, s 45(5) already contains an element of causation. That is, the insurer is not liable for loss 'attributable to unseaworthiness' where the ship was sent to sea in an unseaworthy state but remains liable to indemnify the insured for all insured losses unconnected with unseaworthiness.

9.151 It is significant that the MIA uses the words 'attributable to' rather than 'proximately caused by' as used in s 61(1).<sup>560</sup> Howard Bennett states that the drafting

reflects the nineteenth century approach to causation according to which the loss of a vessel to a sea peril which a seaworthy vessel could have withstood would be regarded as proximately caused by the sea peril as the cause immediate in time. Consequently, a formula was required to permit the courts to consider an otherwise legally remote if factually significant cause. Thus, if the unseaworthiness necessarily increased the danger which led to the loss, the insurer would have a good defence even if, when the accident overtook the vessel, the accident was the cause of the loss most immediate in time. The position is the same today, except that the unseaworthiness should be classified as the or a proximate cause.<sup>561</sup>

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557 That is, MIA s 45(3).

558 S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' Ph D thesis University of Queensland November 1998, 340, Draft provision S1-S3.

559 Ibid 340-1.

560 MIA s 61(1) provides that 'unless the policy otherwise provides, the insurer is liable for any loss proximately caused by a peril insured against, but, subject as aforesaid, he is not liable for any loss which is not proximately caused by a peril insured against'.

561 H Bennett *The Law of Marine Insurance* Clarendon Press Oxford 1996, 318. See also the discussion of proximate cause in ALRC DP 63 para 5.110-14.

9.152 Despite the modern adoption of ‘proximate cause’ as the link between cause and loss,<sup>562</sup> the use of the words ‘attributable to unseaworthiness’ in s 45(5) is critical in cases where the unseaworthiness is a more remote cause of loss. The MIA effectively dilutes the rule of proximate cause of loss where there is privity of the insured.<sup>563</sup> If unseaworthiness is an excluded peril and is the (or a) proximate cause of the loss, the insurer will be able to deny liability under MIA s 61(1). If unseaworthiness is not a proximate cause of loss but the loss can nonetheless be attributed to it, the insurer can still establish a defence under s 45(5) if it can prove the insured’s privity.<sup>564</sup>

### The privity of the insured

9.153 There is considerable case law concerned with the meaning of the ‘privity of the assured’ in s 45(5), which deals with the obligation of seaworthiness in time policies. These cases focus on two main issues.

- What state of mind must be shown in order to prove privity. For example, is it necessary to prove negligence, knowledge, or deliberate or reckless conduct?
- Where the insured is a corporation, who are the natural persons whose state of mind is to be attributed to the insured?

9.154 In relation to the latter issue, the Discussion Paper noted concerns that the concept of ‘privity of the assured’ may be out of date given that many provisions dealing with corporate liability in shipping law and elsewhere extend obligations not only to the insured but also to employees, agents, contractors and, in some cases, managers.<sup>565</sup> Submissions echoed this concern.<sup>566</sup>

It is difficult to justify the concept of ‘privity of the insured’ bearing in mind the complex ship owning and management arrangements which exist at the present time.<sup>567</sup>

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562 It is now settled beyond doubt that the proximate cause is determined by its effect and not simply by the timing of various factors contributing to a loss. *Leyland Shipping Co v Norwich Union Fire Ins Society* [1918] AC 350 (House of Lords); See H Bennett *The Law of Marine Insurance* Clarendon Oxford 1996, 116; ALRC DP 63 para 5.111.

563 S Hodges *Cases and Materials on Marine Insurance Law* Cavendish London 1999, 324. It is enough if the unseaworthiness to which the assured is privy forms part of the cause of the loss: *George Cohen, Sons and Co v Standard Marine Insurance Co* (1925) 21 LIL Rep 30, 36.

564 H Bennett *The Law of Marine Insurance* Clarendon Oxford 1996, 319.

565 ALRC DP 63 para 5.73 citing D Luxford ‘The Marine Insurance Act: Chronologically Challenged Legislation?’ *MLAANZ Annual Conference Wellington 5–8 November 1995*, 29 referring to The Hague Rules, the limitation of shipowners’ liabilities conventions and the Warsaw Convention.

566 K Carruthers Submission 9.

567 *Ibid.*

9.155 In *The Eurysthenes*,<sup>568</sup> Lord Denning MR stated that, for the purposes of s 39(5) of the MIA (UK) (MIA s 45(5)), where the insured is a corporation, the privity of the corporation is that of the corporation's alter ego.<sup>569</sup> This reasoning is derived from the 'organic theory' of corporate knowledge under which the acts and omissions of senior people in the management and direction of the company are imputed to the company.<sup>570</sup> These persons are more than agents or employees and act not just for the company but as the company itself.

9.156 The classic statement of the alter ego principle refers to the people who are 'really the directing mind or will or the corporation'.<sup>571</sup> In *The Eurysthenes*<sup>572</sup> the test suggested by Lord Denning MR was whether the relevant knowledge was held by the 'head people' of the company.<sup>573</sup> Such people would generally be confined to the controlling shareholders or managing directors. This position has been criticised as too restrictive. *Arnould's Law of Marine Insurance and Average* states

It is submitted that a pragmatic approach to this point is better suited to the conditions of the business of shipowning, where the technical management of the vessel is often delegated to outside managers or to a superintendent who is not on the board of the directors of the owning company, rather than a narrow test which would confine the *alter ego* to the controlling shareholders or the managing directors.<sup>574</sup>

9.157 The decision of the English Court of Appeal in *The Star Sea*<sup>575</sup> may be taken as applying a more expansive approach in the marine insurance context. In that case Leggatt LJ stated that where the insured is a corporation 'the search would be to draw a circle around the natural persons which fairly reflected the equivalent position to that which would prevail where a natural person was the assured'.<sup>576</sup> In doing so, the Court looked towards the persons 'involved in the decision making processes required for sending the *Star Sea* to sea'.<sup>577</sup>

568 *Compania Maritima San Basilio SA v Oceanus Mutual Underwriting Association (Bermuda) Ltd* 'The Eurysthenes' [1976] 2 Lloyd's Rep 171.

569 *Ibid* 179.

570 The origins of the 'organic theory' are found in the reasoning of Haldane LC in *Lennard's Carrying Co. v Asiatic Petroleum Co* [1915] AC 705. See M Mustill and J Gilman Arnould's *Law of Marine Insurance and Average* 16th ed vol III Stevens & Sons London 1997, 559. In Australia, see *Alstergren v Owners of the Ship Territory Pearl* (1992) 36 FCR 186; (1992) 112 ALR 133; *Sanko Steamship Co Ltd & Grandslam Enterprise Corporation v Sumitomo Australia Ltd (No2)* (1995) 63 FCR 227 in which Lennard's and subsequent English and Australian cases are discussed in the context of establishing 'actual fault or privity' for shipowner's liability purposes.

571 *Lennard's Carrying Co v Asiatic Petroleum Co* [1915] AC 705, 713 (Haldane LC).

572 *Compania Maritima San Basilio SA v Oceanus Mutual Underwriting Association (Bermuda) Ltd* (The Eurysthenes) [1976] 2 Lloyd's Rep 171.

573 *Ibid* 179.

574 M Mustill and J Gilman Arnould's *Law of Marine Insurance and Average* 16th ed vol I Stevens & Sons London 1981, 559.

575 *Manifest Shipping & Co Ltd v Uni-Polaris Insurance Co Ltd* (The *Star Sea*) [1997] 1 Lloyd's Rep 360.

576 *Ibid* 375.

577 *Ibid*.

9.158 However, this formulation is not as broad as many modern statutes, which commonly provide that bodies corporate are deemed to have committed the acts and omissions of their directors, employees and agents<sup>578</sup> or that the state of mind of a corporation may be established by reference to the state of mind of their directors, employees and agents.<sup>579</sup> However, similar provisions may not be appropriate in the context of seaworthiness as the risks covered by the insurance are generally intended to include risks arising from the conduct of the master, officers or crew of the ship, such as negligence and barratry, including conduct that might lead to the ship commencing a voyage in an unseaworthy state.

9.159 The cases discussed above also examine the state of mind that must be shown in order to prove ‘privity’. In *The Eurysthenes*<sup>580</sup> the English Court of Appeal ruled that in order to establish privity it must be shown that there has been ‘knowledge and concurrence’ on the part of the insured in sending the ship to sea in an unseaworthy state, but that this does not necessarily have to amount to wilful misconduct and may simply amount to ‘turning a blind eye’.<sup>581</sup>

9.160 In *The Star Sea* the English Court of Appeal ruled that the owners or managers had not turned a blind eye to the unseaworthiness because they neither suspected nor believed that the vessel was unseaworthy.<sup>582</sup> In upholding this ruling, the House of Lords confirmed that the test of privity is subjective.<sup>583</sup> Lord Scott stated.

In summary, blind-eye knowledge requires, in my opinion, a suspicion that the relevant facts do exist and a deliberate decision to avoid confirming that they exist. But a warning should be sounded. Suspicion is a word that can be used to describe a state-of-mind that may, at one extreme, be no more than a vague feeling of unease and, at the other extreme, reflect a firm belief in the existence of the relevant facts. In my opinion, in order for there to be blind-eye knowledge, the suspicion must be firmly grounded and targeted on specific facts. The deliberate decision must be a decision to avoid obtaining confirmation of facts in whose existence the individual has good reason to believe. To allow blind-eye knowledge to be constituted by a decision not to enquire into an untargeted or speculative suspicion would be to allow negligence, albeit gross, to be the basis of a finding of privity. That, in my opinion, is not warranted by section 39(5).<sup>584</sup>

578 eg Corporations Law s 762(4).

579 eg Navigation Act 1912 (Cth) s 395A; Fisheries Management Act 1991 (Cth) s 164.

580 *Compania Maritima San Basilio SA v Oceanus Mutual Underwriting Association (Bermuda) Ltd ‘The Eurysthenes’* [1976] 2 Lloyd’s Rep 171.

581 *Ibid* 179 (Denning MR); 184 (Roskill LJ); 188 (Lane LJ); See S Hodges *Cases and Materials on Marine Insurance Law* Cavendish London 1999, 319–24.

582 *Manifest Shipping & Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [1997] 1 Lloyd’s Rep 360, 377–8 (Leggatt LJ).

583 *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd* [2001] 1 All ER 743, 753 (Lord Hobhouse) 780–2 (Lord Scott).

584 *Ibid* 781.



9.161 As a consequence of this analysis, privity virtually requires a conscious decision by the insured to ignore circumstances that it was aware of and that it knew probably amounted to unseaworthiness. This verges on fraud and, accordingly, places a very heavy onus of proof on the insurer. However, it must be remembered that an insured is buying insurance against the consequences of negligence, including its own. Introducing a lower standard than ‘privity’, even that of ‘gross negligence’, undermines this to some degree and puts greater pressure on the insured to comply with all requisite standards, at least to the extent that this can be reasonably expected of it.

9.162 The Commission has concluded that the state of mind that must be shown in order to prove ‘privity’ is inappropriately high. For this reason the Commission’s recommended new provision on seaworthiness refers to the discharge from liability of the insurer where the insured ‘knew, or ought to have known of the facts and circumstances that rendered the ship unseaworthy and that they rendered the ship unseaworthy’. However, the Commission does not consider that it is appropriate to seek to define in the MIA the range of natural person whose decisions or mental state are relevant to a determination that a body corporate knew or ought to have known the relevant facts. That would rob the Act and the courts of the flexibility that is, in the Commission’s view, essential to ensure that a fair assessment can be made in each fact situation. It is unlikely that a statutory formulation could be worded in such a way as to provide real guidance and preserve flexibility.

### **Burden of proof**

9.163 The present law clearly establishes that the burden of proof of unseaworthiness lies with the insurer.<sup>585</sup> Further, in order to mount a defence based on MIA s 45(5), the insurer has the burden of proving both privity of the insured and that the loss was attributable to unseaworthiness.<sup>586</sup> MLAANZ submitted that this should remain the position under an amended MIA.<sup>587</sup>

9.164 The Commission considers that under a reformed MIA, while the insurer should continue to have the burden of proving that a ship was unseaworthy, in order to recover the insured should then be required to prove that the unseaworthiness did not occur with its knowledge and that it took all reasonable steps that were available to it to remedy the position. Such an approach is consistent with the position recommended in reform of express warranties, where the insured has the burden of proving that the breach of an express contractual term

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585 Skandia Insurance Company Ltd v Skoljarev (1979) 142 CLR 375. See ALRC DP 63 para 5.105-5.109.

586 See Manifest Shipping & Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea) [1997] 1 Lloyd’s Rep 360, 372.

587 MLAANZ Submission 12.

was not a proximate cause of the loss (recommendation 19). It is also consistent with the approach of the Norwegian Marine Insurance Plan.

### **Submissions on seaworthiness**

9.165 Submissions agreed with the proposal to abolish the distinction between time and voyage policies with regard to the warranty of seaworthiness<sup>588</sup> and, therefore, with the suggestion that there should be only one statutory formulation of the insured's obligations with respect to seaworthiness.

9.166 The Discussion Paper proposed that the MIA should be amended to provide that an insurer may not avoid a contract of marine insurance by reason of a breach of the implied warranty of seaworthiness

- if the loss in respect of which the insured seeks to be indemnified was not caused or contributed to by the breach of warranty and
- the insured neither knew nor ought to have known about the defects at such a time that it would have been possible for the insured to intervene.<sup>589</sup>

9.167 The approach suggested by the Discussion Paper received support in some submissions.<sup>590</sup> The Insurance Council of Australia stated that the seaworthiness provisions of the Norwegian Plan were an attractive model for reform and were consistent with the Commission's intended approach to warranties generally.<sup>591</sup> One submission expressed concern that, while the position with regard to express warranties might be amended, the status quo ought to be maintained with respect to the implied warranty of seaworthiness in order to ensure that marine safety is not prejudiced.<sup>592</sup>

9.168 As discussed above, where time policies are concerned, MIA s 45(5) already contains elements of causation and knowledge of the insured. That is, the insurer is not liable for loss 'attributable' to unseaworthiness where the ship was sent to sea in an unseaworthy state with the 'privity' of the insured and the meaning of each of these elements is elaborated by case law.

9.169 No submissions dealt with the warranty in MIA s 46(2) and its effect on insured cargo owners. However, the Commission considers that it is unreasonable

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588 Law Society of WA Submission 7; K Carruthers Submission 9; Insurance Council of Australia Submission 11; A Street Submission 15.

589 ALRC DP 63, draft proposal 4.

590 K Carruthers Submission 9; MLAANZ Submission 12.

591 Insurance Council of Australia Submission 11. This view was also taken by Phil Grieve of Associated Marine Insurers Agents Pty Ltd: P Grieve Submission 6.

592 Law Society of WA Submission 7.

to impose this implied warranty on cargo owners and recommends that it be removed from the Act (see recommendations 10 and 12).

### **Conclusions in relation to seaworthiness**

9.170 The Commission considers that if an implied warranty of seaworthiness is to be retained it should include elements of causation, knowledge and reasonable response. In accordance with its measured approach to reform of the MIA, the Commission has closely considered whether the most desirable option for reform is simply to retain the wording of s 45(5), but with application to both voyage and time policies. Even within a more extensive reform it may be desirable to retain some of the wording of the existing section so as not to lose the benefit of the existing case law.

9.171 However, the Commission's preferred approach is to remove the concept of implied warranties altogether and substitute a regime that permits similar express terms to be inserted in contracts of marine insurance. On breach of an express contractual term relating to seaworthiness, the remedies available to an insurer will be restricted by comparison with the current Act, but have broader scope (if the contract so states) than for breaches of other express contractual terms. The Commission's approach removes some of the obscurity surrounding warranties by taking them out of the legislation and requiring them to be expressed in the contract.

9.172 The Commission concludes that reforms relating to obligations of seaworthiness should incorporate causation and knowledge elements, as is presently the case under MIA s 45(5). The causation element should be whether loss was 'attributable' to the breach, adopting the existing language of MIA s 45(5). The explanatory memorandum to the amending Bill should state that the legislative intent is that the terms 'attributable' and 'seaworthy' should bear the same meaning as they presently do.

9.173 One other significant change to the existing position recommended by the Commission is that the obligations of seaworthiness may apply not only at the commencement of the voyage but throughout the voyage, if the relevant express term is so drafted. An insurer should not be liable if the vessel becomes unseaworthy after leaving port and the insured fails to take such remedial steps as were reasonably available to it. This better recognises that with modern communications and technology an insured shipowner or management company may have knowledge of unseaworthiness that has arisen in the course of a voyage and may be in a position to take steps to remedy the deficiency. Consistently with the Commission's approach to reform of express warranties, breach by the insured of an express contractual term relating to seaworthiness will be remediable.

9.174 The Commission does not consider that its recommended reforms will in any way prejudice marine safety. The deterrent effect of the consequences of breach of the implied warranty of seaworthiness is maintained. In some circumstances the effect of the recommended reform will make it more difficult for an insured to recover than under the current law, notably where unseaworthiness arises during the course of the voyage, unless it acts reasonably to counter the unseaworthiness when circumstances permit.

9.175 The Commission's recommendations reflect the following conclusions.

- The implied warranty of seaworthiness should be abolished but a regime introduced for similar express terms to be inserted in contracts of marine insurance.
- Insurers should be at liberty to include an express term in any contract of marine insurance stipulating that the insurer will be automatically discharged from liability to indemnify the insured for any loss attributable to the unseaworthiness of the vessel where the insured knew or ought to have known of that unseaworthiness and failed to take such steps as were reasonably available to render the vessel seaworthy.
- The statute should not specify any particular relevant time for assessing the vessel's unseaworthiness. The proposed contractual term may be continuous. However, unseaworthiness that develops during a voyage will not generally prejudice an insured as, if it did not know and could not reasonably be expected to have known of the unseaworthiness, or if it did all it reasonably could to remedy the position (which might well be nothing), then it will not have breached the contractual term and the insurer will have no grounds on which to avoid liability.
- The concept of seaworthiness as defined in MIA s 45(4) does not have to be expanded to cover transit on inland waters if the MIA is amended to cover inland waters risks, as recommended elsewhere by the Commission, if references to the 'sea' and 'seas' are defined to include references to inland waters (see recommendation 5).

## **Warranty of legality**

9.176 The MIA implies a warranty of legality in all contracts of marine insurance. Section 47 provides

47. There is an implied warranty that the adventure insured is a lawful one, and that, so far as the assured can control the matter, the adventure shall be carried out in a lawful manner.

## Reform of the warranty of legality

9.177 In an era of comprehensive statutory regulation of shipping, environmental and safety matters, particular concerns have been expressed about this warranty.

A question which arises in the context of the warranty of legality is whether a breach of one of the plethora of regulations which now apply in ports worldwide is sufficient to constitute a breach of the warranty. The ever increasing concern with marine pollution will mean that this question will need to be addressed constantly.<sup>593</sup>

9.178 Section 47 is very broad in that it refers not only to the adventure being a lawful adventure (that is, having a lawful purpose) but also to the adventure being carried out in a lawful manner. It appears, therefore, that any breach of a regulation may be interpreted as a breach of warranty.<sup>594</sup>

9.179 Given the plethora of regulations, a warranty may be easily and unknowingly breached by the insured<sup>595</sup> and the insurer may avoid liability even where the breach did not contribute to loss. Concerns have been expressed that this position is inappropriate and unfair, not only to the insured, but also to third parties, such as mortgagees, who may be interested in insured vessels.

9.180 In the Discussion Paper the Commission stated that the options for reform of the implied warranty of legality included the following.<sup>596</sup>

- Amending the MIA to provide that an insurer may not avoid a contract of marine insurance by reason of a breach of a warranty if the insured proves the loss was not caused or contributed to by the breach of warranty.
- Redrafting the MIA to distinguish between technical, non-material breaches of regulations and other illegality which substantially affects the risks involved in the adventure.<sup>597</sup> As noted above, the wording of s 47 of the MIA distinguishes between adventures having a lawful purpose and being carried out in a lawful manner, but the consequences of a breach are the same in each case.

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593 S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' Ph D thesis University of Queensland November 1998, 245.

594 In *Switzerland Insurance Australia Ltd v Mowie Fisheries Pty Ltd* (1997) 74 FCR 205, 236–238; (1997) 144 ALR 234, 262–3, Beaumont J was clearly of the opinion that a breach of statutory manning requirements would be a breach of the implied warranty of legality. See also *Doak v Weekes* (1986) 82 FLR 334.

595 Insurers and brokers Consultation Sydney 27 March 2000.

596 ALRC DP 63 para 5.83.

597 Legal practitioners Consultation Sydney 1 May 2000.

- Restricting the circumstances in which the insurer is entitled to deny liability under the contract for breach of the warranty of legality to situations where the insured knew or should have known of the illegality.<sup>598</sup>

9.181 Under the Norwegian Marine Insurance Plan the requirements on the insured are less onerous than under the MIA and distinguish between illegal purposes and breaches of safety regulations. Clause 3-16 of the Plan, which deals with illegal activities, states that

The insurer is not liable for loss which results from the ship being used for illegal purposes,<sup>599</sup> unless the assured neither knew nor ought to have known of the facts at such a time that it would have been possible for him to intervene. If the assured fails to intervene without undue delay after becoming aware of the facts, the insurer may terminate the insurance by giving fourteen days' notice.

The insurance terminates if the ship, with the consent of the assured, is used primarily for the furtherance of illegal purposes.<sup>600</sup>

9.182 An illegal activity under this provision of the Norwegian Plan would not include breaches of regulations. Clause 3-16 corresponds to the first part of the implied warranty in s 47 of the MIA. The requirement that the adventure shall be carried out in a lawful *manner* finds its equivalent in cl 3-24 and 3-25, which deal with breaches of safety regulations.<sup>601</sup> Under these provisions, if the insured is in breach of a safety regulation, the insurer is liable only to the extent that it is proven that the loss is not a consequence of the breach or that the insured was not responsible for the breach.

## Conclusions in relation to warranty of legality

9.183 In the Discussion Paper, the Commission noted suggestions that, while an insurer should not be liable for loss where a ship is used for the furtherance of illegal purposes (such as drug smuggling or gun running), the use of an insured

598 Derek Luxford has stated that there is an urgent need to restrict the operation of this warranty by requiring the insurer to show that the insured knowingly engaged in the illegal activity: D Luxford 'The Marine Insurance Act: Chronologically challenged legislation?' Paper MLAANZ Annual Conference Wellington 5-8 November 1995.

599 The commentary to the Plan acknowledges that '[j]udging the causation issue may give rise to difficulty. It is not sufficient that the ship runs aground on a voyage with an illegal purpose about which the assured knew. The damage must, to a certain extent, be a foreseeable consequence of the illegal undertaking, eg, where the vessel must venture into hazardous waters in connection with a smuggling operation and runs aground': Commentary to Norwegian Marine Insurance Plan cl 3-16 <http://exchange.dnv.com/nmip/books/comm> (28 March 2000).

600 Norwegian Marine Insurance Plan cl 3-16 <http://exchange.dnv.com/nmip/books/plan> (28 March 2000).

601 S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' Ph D thesis University of Queensland November 1998, 289.

ship in an unlawful manner (which encompasses breaches of safety regulations) should only result in loss of cover if the illegality is causative of the loss.<sup>602</sup>

9.184 In the Discussion Paper the Commission proposed that

- The MIA should continue to provide that an insurer may avoid a contract of marine insurance by reason of a breach of the implied warranty that the adventure have a lawful purpose.
- The MIA should be amended to provide that an insurer may not avoid a contract of marine insurance by reason of a breach of the implied warranty that the adventure be carried out in a lawful manner if (i) the loss in respect of which the insurer seeks to be indemnified was not caused or contributed to by the breach of warranty and (ii) the insured neither knew nor ought to have known about the illegality at any time that it would have been possible for the insured to intervene.<sup>603</sup>

9.185 The Insurance Council of Australia supported the Commission's draft proposals relating to the warranty of legality.<sup>604</sup> Gault Armstrong & Kemble specifically supported the proposed distinction between the obligation that the adventure have a lawful purpose and that the adventure be carried out in a lawful manner.<sup>605</sup> MLAANZ stated that the MIA should allow non-causative trivial breaches of the implied warranty of legality to be excused.<sup>606</sup>

9.186 The recommended drafting of the amendments to the MIA is, consistently with the recommendations in relation to the warranty of unseaworthiness, to abolish the implied warranty of legality but to permit the insurer to include in any contract of marine insurance terms to the following effect.

- So far as the insured can control the matter, the insured adventure shall have no unlawful purpose. If there is a breach of such a term, the insurer is automatically discharged from all liability under the policy.
- So far as the insured can control the matter, the insured adventure shall be carried out in a lawful manner. If there is a breach of such a term, the insurer is not liable to indemnify the insured for any loss that is attributable to the breach.

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602 See ALRC DP 63 para 5.86; Advisory Committee meeting Sydney 25 May 2000; S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' Ph D thesis University of Queensland November 1998, 339–40; Draft provision I1-I4.

603 See ALRC DP 63, draft proposal 6–8.

604 Insurance Council of Australia Submission 11.

605 Gault Armstrong & Kemble Submission 17.

606 MLAANZ Submission 12.

9.187 The proposed provisions are intended to retain as much of the existing language as possible and to maintain consistency with the amended seaworthiness provisions. Section 47 already contains a knowledge element: the insured is only obliged to ensure that the adventure insured is carried out in a lawful manner ‘so far as the assured can control the matter’. These words are retained but have also be applied to the contractual requirement, if one is inserted, that the insured adventure have a lawful purpose. The causation element should be consistent with that adopted in the amended seaworthiness provisions. That is, the loss must be ‘attributable’ to the legality. This requires a lesser degree of causation than ‘proximately caused’ and, as a result, maintains pressure on the insured to comply with the law.

### **Warranties, safety and environmental concerns**

9.188 The Commission’s consultations revealed concerns that changes to the requirement of strict compliance with the implied warranties of seaworthiness and legality may have deleterious effects on compliance with safety and other regulations.<sup>607</sup> It is argued that the present law acts as a deterrent against unsafe practices. Justice Cooper has made the following observation about the role of warranties in contracts of insurance.

If non-compliance with safety standards does not put at risk marine insurance cover, there may be powerful economic incentives not to comply. This would leave with the underwriter any attendant risk of loss or injury being sustained in the course of maritime operations and require that it establish that non-compliance amounted to unseaworthiness and that unseaworthiness caused the loss. It would also leave enforcement of safety standards to the regulatory agencies requiring them to take positive steps to uncover non-compliance. The risk of losing insurance cover for breach of warranty imposes strictures of self-compliance which do not need active regulatory supervision.<sup>608</sup>

9.189 The Commission agrees that the present law encourages compliance with maritime regulation. However, it does so only by providing a disproportionate deterrent. The Commission’s recommendations on express warranties address this concern by providing that the insurer may only avoid liability where loss is not proximately caused by the breach.

9.190 Some breaches of an insured’s obligations to comply with safety and environmental codes or regulations may constitute breach of an express term relating to seaworthiness or be committed in the course of a voyage with an illegal

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607 Lawyers Consultation Sydney 1 May 2000; Insurers and legal practitioners Consultation Brisbane 11 May 2000; Advisory Committee meeting Sydney 25 May 2000.

608 R Cooper ‘Australian Perspectives in Marine Insurance’ Paper Shipping in the New Millennium Conference MLAANZ Brisbane 19 March 1999.



purpose and breach an express term relating to legality. If so, they will attract the stricter position recommended by the Commission in relation to these obligations. In particular, where a voyage has an illegal purpose an insurer may still avoid liability for loss not attributable to the insured's breach.

9.191 The Commission has considered whether the amended position recommended with respect to seaworthiness and legality of purpose provides sufficient deterrence against non-compliance with safety and environmental codes or regulations, or whether specific provision should be made in the MIA to cover such matters. This issue is examined below with particular reference to the International Safety Management Code (ISM Code). The Commission has also considered whether the insured's obligations with respect to loss of class or change of classification society should attract different treatment from other express contractual terms.

### The ISM Code

9.192 An important international development in the regulation of safety at sea is the adoption of the International Safety Management Code (ISM Code). The ISM Code has been adopted by 128 countries, including Australia, binds more than 97% of world merchant shipping tonnage<sup>609</sup> and provides an international standard for the safe management and operation of ships and for the prevention of pollution.<sup>610</sup>

9.193 Under the ISM Code shipowners are required to possess certificates granted by independent authorities, normally classification societies,<sup>611</sup> that state that systems for safety and environmental management are in place and are fully operative. The Commission understands that standard hull insurance terms now require vessels to be certified in accordance with the ISM Code and the vessel's owners or operators to hold current documents of ISM compliance. In cargo insurance, the Joint Cargo Committee has produced a 'Cargo ISM endorsement'.<sup>612</sup>

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609 The International Safety Management Code was mandated in ch IX of the SOLAS Convention (International Convention for the Safety of Life at Sea). It entered into force on 1 July 1998 for passenger ships, high speed passenger craft, oil, chemical and gas carriers, bulk carriers and high speed cargo craft. From 1 July 2002 it will apply to cargo ships over 500 tons, and mobile offshore drilling units of 500 gt or more: House of Representatives Standing Committee on Communications, Transport and Microeconomic Reform *Ship Safe: An Inquiry into Australian Maritime Safety Authority Annual Report 1996–97* AGPS 1998, 21. See also R Shaw 'The ISM Code and STCW Convention — Their Impact on Marine Insurance Coverage and Claims' in M Huybrechts E Van Hooydonk & C Dierckx (eds) *Marine Insurance at the Turn of the Millennium* vol 1 Intersentia Antwerp 1999.

610 See J Donaldson "'Safer Ships; Cleaner Seas' — Full Speed Ahead or Dead Slow?' (1998) 2 *Lloyd's Maritime and Commercial Law Quarterly* 170, 173.

611 Classification societies are organisations which survey and classify ships as to their condition, for insurance and other purposes. Major classification societies include Lloyd's Register (UK); American Bureau of Shipping & Affiliated Companies (USA); Nippon Kaiji Kayoki (Japan); Det Norske Veritas (Norway); Bureau Veritas (France) and Germanischer Lloyd (Germany). There is no Australian classification society.

612 Cargo ISM Endorsement (JC 98/019, 1 May 1998).

This clause may be inserted in contracts to exclude cover where cargo is shipped on vessels not complying with the ISM Code.

9.194 Some insurers have expressed concerns that, because a failure to maintain current ISM certification would be unlikely to directly cause loss, change in the law regarding breach of warranty could weaken the practical support which insurers are providing to the ISM Code, and in turn weaken efforts to improve safety of life at sea and to protect the environment.<sup>613</sup>

9.195 The Commission appreciates the importance of these concerns, but considers that non-compliance with the ISM Code will be adequately deterred under its recommended reforms.

9.196 The ISM Code is given force of law in Australia by marine orders issued under s 191 of the *Navigation Act 1912* (Cth).<sup>614</sup> Provision 6 of Marine Order 58 renders it unlawful for the master or owner of a ship to take the ship to sea unless

- (a) there is in respect of the ship a valid Safety Management Certificate; and
- (b) there is on board the ship a copy of a valid Document of Compliance in respect of the company operating the ship.

9.197 Therefore, it appears that, in Australian law, the implied warranty of legality encompasses the obligation to have a safety certificate and to carry on board a current document of compliance. However, it does not necessarily require continuing implementation and maintenance by shipowning companies of the detailed safety management systems required by the ISM Code. Any other position would be extremely onerous for the insured. It would be difficult for any company to achieve absolute and continuing compliance with the ISM Code because, at any particular time, certain elements of the ISM Code may not be fully in place, for example due to turnover in personnel or the incomplete introduction of new management procedures.

9.198 Under the Commission's recommended reforms, failure to comply with Marine Order 58 would not amount to breach of an express term that the adventure has a lawful purpose and would not automatically discharge the insurer from all future liability. However, it could constitute a breach of an express contractual term (not necessarily relating specifically to the ISM Code) that the adventure be carried out in a lawful manner if the required causation and knowledge elements were present. Seaworthiness obligations may also have some operation in the case of breaches of the ISM Code, to the extent that some breaches of the ISM Code may be indicative of unseaworthiness.

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613 M Hill Correspondence 28 August 2000.

614 International Safety Management Code Marine Order Part 58 (Order 2 of 1998).

9.199 The Commission has considered whether compliance with safety regulations, including relevant government regulations and the ISM Code, should be separately addressed in the MIA. One model for special provisions relating to breach of safety regulations is the Norwegian Marine Insurance Plan.<sup>615</sup> The Norwegian Plan defines a safety regulation as

a rule concerning measures for the prevention of loss issued by public authorities, stipulated in the insurance contract, prescribed by the insurer pursuant to the insurance contract, or issued by the classification society.<sup>616</sup>

9.200 Safety regulations are said to include relevant government regulations and the ISM Code.<sup>617</sup> Under the Norwegian Plan where the insured breaches a safety regulation, the insurer is only liable to the extent that it is proved that the loss is not a consequence of the breach, or that the insured was not responsible for the breach.<sup>618</sup> Breach of safety regulations, as with other conditions in the Norwegian Plan, does not automatically void the contract.<sup>619</sup>

9.201 While some submissions have suggested that the implied warranty provisions could be expanded to encourage compliance with regulations and codes related to safety, pollution avoidance and other concerns,<sup>620</sup> the Commission does not consider that separate treatment of safety measures is justified within Australia's MIA-based regime. Any such reform would move Australian law significantly out of step with other common law countries and introduce unnecessary complexity when considering the consequences of a breach of safety obligations.

9.202 The Insurance Council of Australia does not believe that any amendments to the MIA are required to encourage compliance with regulations or codes relating to safety, pollution and other regulatory concerns, but that common contract clauses are sufficient to address these concerns.<sup>621</sup> The Commission agrees.

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615 See also T-L Wilhelmsen 'Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire' in CMI Yearbook 2000 Comité Maritime International, Antwerp 2000, 332, 400-5.

616 Norwegian Marine Insurance Plan cl 3-24 <http://exchange.dnv.com/nmip/books/plan> (28 March 2000).

617 Commentary to Norwegian Marine Insurance Plan cl 3-24 <http://exchange.dnv.com/nmip/books/comm> (28 March 2000).

618 Norwegian Marine Insurance Plan cl 3-25.

619 The insurer may terminate the insurance with 14 days' notice where 'a safety regulation of material significance has been violated, intentionally or through gross negligence, by the assured, or by someone whose duty it is on his behalf to comply with the regulation or ensure that it is complied with': Norwegian Marine Insurance Plan cl 3-27(c). The Plan is silent on what regulations are of 'material significance'. However, it is apparent that breaches with minor consequences, or where the insured is not intentionally or grossly negligent, will not allow the insurer to avoid liability or to terminate the insurance.

620 MLAANZ Submission 12.

621 Insurance Council of Australia Submission 11.

### **Loss of class and change of classification society**

9.203 Commonly, the insured under a hull policy will contract to ensure that at the commencement and throughout the period of insurance the vessel is classed with a classification society, that the vessel's class within the society is maintained and that any recommendations, restrictions or requirements of the society in relation to seaworthiness are complied with.<sup>622</sup> The effect of loss of class or change of classification society is often expressly stated to be that the insurer is discharged from liability.<sup>623</sup>

9.204 Similarly, some insured vessels are subject to statutory survey requirements,<sup>624</sup> and policies of insurance relating to these vessels may also contain express warranties or other contractual terms requiring compliance. While statutory survey obligations are covered by the implied warranty of legality, this is not always the case with classification obligations.

9.205 While some clauses dealing with classification, such as cl 4 of the Institute Time Clauses Hulls, are not expressed as warranties, it has been stated that for all intents and purposes, the duties imposed are warranties, the breach of which automatically discharges the insurer from liability.<sup>625</sup>

9.206 It may be argued that, given the central role of class in insurance practice and the close relationship between classification, seaworthiness<sup>626</sup> and safety, classification should attract a requirement of strict compliance. As noted above, in at least some civil code countries loss of class allows insurers to avoid liability for loss, regardless of materiality or causation (see paragraph 9.48). One justification for separate treatment of loss of class or change of classification society, as compared to other matters, is that it is not of itself capable of causing loss (as distinct from a structural or other fault in a vessel that could lead a society to refuse it classification).

9.207 Under the Commission's recommended reforms, while loss of class may be due to unseaworthiness and therefore allow the insurer to avoid liability, by itself loss of class would rarely, if ever, allow an insurer to avoid liability for loss

622 eg ITCH cl 4. Most, if not all, insured ocean-going vessels are subject to such classification requirements.

623 eg ITCH cl 4.2 states that the underwriters 'will be discharged from liability under this insurance as from the date of the breach provided that if the Vessel is at sea at such date the Underwriter's discharge from liability is deferred until arrival at her next port'.

624 Such as those imposed by the Marine Safety Act 1998 (NSW); Marine Act 1988 (Vic).

625 S Hodges Cases and Materials on Marine Insurance Law Cavendish London 1999, 133.

626 However, the surveys carried out by a classification society will necessarily be confined to the physical state of the vessel and cannot encompass other aspects of a vessel's seaworthiness, such as the competence and adequacy of the master and crew: H Bennett *The Law of Marine Insurance* Clarendon Press Oxford 1996, 306–7.

because loss would not be attributable to class status but the underlying unseaworthiness or other problem. However, the Commission does not consider that this fact justifies special treatment of classification obligations.

## **Change of voyage, deviation and delay**

9.208 The MIA contains other terms which have much in common with the Act's warranty provisions and require separate consideration. These include MIA s 48–52 and s 54 which deal with change of voyage, deviation and delay, and are relevant only to voyage policies. These sections read as follows.

### **Implied condition as to commencement of risk**

48.(1) Where the subject-matter is insured by a voyage policy “at and from” or “from” a particular place, it is not necessary that the ship should be at that place when the contract is concluded, but there is an implied condition that the adventure shall be commenced within a reasonable time, and that if the adventure be not so commenced the insurer may avoid the contract.

(2) The implied condition may be negated by showing that the delay was caused by circumstances known to the insurer before the contract was concluded, or by showing that he waived the condition.

### **Alteration of port of departure**

49. Where the place of departure is specified by the policy, and the ship instead of sailing from that place sails from any other place, the risk does not attach.

### **Sailing for different destination**

50. Where the destination is specified in the policy, and the ship, instead of sailing for that destination, sails for any other destination, the risk does not attach.

### **Change of voyage**

51.(1) Where, after the commencement of the risk, the destination of the ship is voluntarily changed from the destination contemplated by the policy, there is said to be a change of voyage.

(2) Unless the policy otherwise provides, where there is a change of voyage, the insurer is discharged from liability as from the time of change, that is to say, as from the time when the determination to change it is manifested; and it is immaterial that the ship may not in fact have left the course of voyage contemplated by the policy when the loss occurs.

### **Deviation**

52.(1) Where a ship, without lawful excuse, deviates from the voyage contemplated by the policy, the insurer is discharged from liability as from the time of deviation, and it is immaterial that the ship may have regained her route before any loss occurs.

(2) There is a deviation from the voyage contemplated by the policy:

(a) where the course of the voyage is specifically designated by the policy, and that course is departed from; or

(b) where the course of the voyage is not specifically designated by the policy, but the usual and customary course is departed from.

(3) The intention to deviate is immaterial; there must be a deviation in fact to discharge the insurer from his liability under the contract.

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**Delay in voyage**

54. In the case of a voyage policy, the adventure insured must be prosecuted throughout its course with reasonable despatch, and, if without lawful excuse it is not so prosecuted, the insurer is discharged from liability as from the time when the delay became unreasonable.<sup>627</sup>

9.209 These provisions, like the warranty provisions, imply certain terms into contracts of marine insurance and prescribe the consequences of breach of those terms. In the case of change of voyage (s 51), deviation (s 52), and delay in voyage (s 54), a breach results in the insurer being discharged from liability as from the time of the breach — the same consequence as for a breach of warranty. As with a breach of a warranty, this consequence flows regardless of whether loss is caused by the breach. The breach cannot be remedied, except where there is a relevant ‘held covered’ clause.

9.210 There is a peculiar difference between s 51 and s 52. If the destination changes, the discharge arises as soon as the decision to change it becomes apparent, but if the route is changed (but the destination remains the same), only actual deviation triggers the insurer’s remedy.

9.211 The consequence of breach of the other provisions is stated differently. The MIA provides that where a ship sails from or for a place other than that specified in the policy the ‘risk does not attach’ (s 49–50). Where there is delay in commencement of the risk under a voyage policy the insurer ‘may avoid the contract’ (s 48),<sup>628</sup> indicating that the insurer must elect to do so and, presumably, inform the insured of that election. The effect of these provisions is to discharge the insurer from liability by reason of some act of the insured or some other person which occurred after the contract was concluded. The Commission has therefore considered whether the operation of these provisions should be included in the reforms recommended concerning warranties.

9.212 The underlying basis of these provisions is that the risk to which an insurer subscribes under a voyage policy is a particular marine adventure consisting of a voyage from a named point of departure (the *terminus a quo*) to a specified destination (the *terminus ad quem*). It is only this voyage that is insured and only so long as the insured strictly and expeditiously pursues the regular course of the

627 Section 53 deals with policies that designate several ports of discharge and stipulate the order in which the insured vessel must call at them so that there is no deviation.

628 Howard Bennett states that the remedy conferred under s 48 (s 42 of the MIA (UK)) is ‘a curiosity’. He states ‘[i]t is unclear why the draftsman of the 1906 Act ignored the non-attachment of risk approach of the common law, clearly based upon deviation from the insured adventure. The Act alters the pre-existing law by imposing an implied condition breach of which permits the retrospective avoidance of the contract. Remedially, therefore, failure to commence the adventure within a reasonable time is assimilated to a breach of the duty of utmost good faith. The assured must seek to prove a waiver of the breach by the insurer’: See H Bennett *The Law of Marine Insurance* Clarendon Press Oxford 1996, 266.

voyage insured. Failure to do so alters the nature of the risk<sup>629</sup> and frees the insurer from liability for subsequent loss.<sup>630</sup> The position may be summarised as follows

Should the insured adventure not ensue, liability on the policy will never attach.  
Should the insured adventure commence but subsequently be departed from, the insurer's liability on the policy is automatically prospectively discharged.<sup>631</sup>

### Conclusions in relation to change of voyage

9.213 The Commission does not consider that the provisions of the MIA dealing with change of voyage, deviation and delay should be treated differently from the reform recommended in relation to express warranties.

9.214 As with breach of other express contractual terms, breach should not automatically discharge the insurer from all future liability under the contract of insurance. To ensure consistency, the statutory provisions creating these remedies (s 48 and 51-55) should be repealed. The parties are free to insert any express terms to similar effect in their contract but the insurer's remedies will be limited to discharge from liability for loss proximately caused by a breach.

9.215 However, the Commission regards the provisions in MIA s 49–50 to be in a different class as they relate to the non-attachment of the risk, rather than to breach of a contractual term. These provisions should be retained in their present form.

### Other issues

#### Interpretation of express warranties

9.216 Other provisions of the MIA imply terms into certain express warranties present in the contract. These provisions relate to the warranties of neutrality and good safety.<sup>632</sup> The Discussion Paper asked whether express warranties of neutrality or good safety are incorporated into modern contracts of marine insurance and if there is a need for the MIA provisions interpreting such warranties to be retained.

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629 Although it need not be shown to increase the risk: See H Bennett *The Law of Marine Insurance* Clarendon Press Oxford 1996, 267.

630 See H Bennett *The Law of Marine Insurance* Clarendon Press Oxford 1996, 261; M Mustill and J Gilman *Arnould's Law of Marine Insurance and Average* 16th ed vol III Stevens & Sons London 1997, 322.

631 H Bennett *The Law of Marine Insurance* Clarendon Press Oxford 1996, 261.

632 MIA s 42; s 44.

9.217 The Insurance Council of Australia and MLAANZ supported the repeal of these provisions which, they stated, are no longer included in modern contracts of marine insurance.<sup>633</sup> Otherwise this issue was not the subject of significant comment in submissions or in consultations. The Commission concludes that these provisions do not perform any significant modern purpose. In any case, parties remain free to include these provisions in their marine insurance policies, should they wish to do so.

9.218 The Commission recommends that these provisions, along with MIA s 43,<sup>634</sup> should be repealed as an incidental element of the proposed overhaul of the law relating to marine insurance warranties and similar contractual terms.

### **Burdens of proof**

9.219 To make a claim under a marine insurance contract, an insured has the burden to prove, on the balance of probabilities, that

- the loss was caused by a peril which was insured against in the contract, and
- the alleged cause of loss was the proximate cause.

9.220 As discussed in the Discussion Paper, in marine insurance disputes involving the operation of the warranty of seaworthiness, the question at issue is often whether the loss in question was caused by the unseaworthiness of the vessel or by a ‘peril of the sea’. In such disputes the issue of burdens of proof is complicated because the onus of proof of seaworthiness lies with the insurer.<sup>635</sup>

The co-existence of this onus with the burden of proof which is cast upon the insured on the issue of causation creates some complexity, because unseaworthiness is not only an element in the defences under s 45(1) and (5) of the Act, but it is also a cause of loss which falls outside the concept of perils of the sea.<sup>636</sup>

9.221 In the Discussion Paper the Commission asked whether there may be some benefit in codifying the law relating to evidence and burdens of proof relevant to establishing that a loss was caused by an insured peril. The Commission’s preliminary view was that to do so would be difficult and risk complicating, rather than clarifying, the law in this area.<sup>637</sup>

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633 Insurance Council of Australia Submission 11.

634 MIA s 43 provides that there is no implied warranty as to the nationality of a ship, or that her nationality shall not be changed during the risk.

635 See ALRC DP 63 para 5.105–9; *Skandia Insurance Company Ltd v Skoljarev* (1979) 142 CLR 375.

636 *Skandia Insurance Company Ltd v Skoljarev* (1979) 142 CLR 375, 387.

637 See ALRC DP 63 para 5.121.



9.222 The Insurance Council of Australia expressed support for codification of the law relating to burdens of proof.<sup>638</sup> While MLAANZ favoured provisions relating to burdens of proof in the specific context of proposed reforms to the law relating to express and implied warranties, it did not favour general reform.<sup>639</sup>

9.223 Beyond its conclusions in paragraph 9.128 and 9.164 above, the Commission has found no reason to depart from its earlier conclusion that there is little benefit in attempting to codify the law relating to burdens of proof.

9.224 The Commission has also concluded that there would be no benefit in attempting to codify the law relating to proximate cause and other principles of causation in marine insurance law or the law governing what constitutes ‘perils of the sea’. Submissions supported this position.<sup>640</sup>

### **Cancellation of contracts**

9.225 There is nothing in the MIA dealing with cancellation. The parties are free to incorporate provisions dealing with cancellation in their contracts. In contrast, ICA s 59–60 set out a comprehensive procedure for cancellation. An insurer has the right to cancel, for example, where the insured fails to comply with a provision of the contract. These provisions are connected with other provisions restricting insurers’ liberties in relation to the expiry and renewal of contracts (ICA s 58).

9.226 Dr Sarah Derrington has proposed that, in some circumstances, insurers should be given express statutory rights to terminate insurance on notice where a breach of warranty has occurred.<sup>641</sup>

9.227 Under the Commission’s recommended reforms, breach of an express term that would have constituted a warranty under the MIA no longer automatically discharges all future liability of the insurer. Discharge of liability is generally limited to that relating to loss proximately caused or attributable to the particular breach. Further, breaches are effectively remediable.

9.228 Where an insurer becomes aware that the insured has been in breach of a contractual term, but remains liable for future loss, it is fair to allow the insurer to cancel the contract with prospective effect after a reasonable period of notice. The inclusion of cancellation rights in the MIA, subject to variation by contract, would help to balance the rights of insurers and insured parties. The Commission concludes that cancellation rights should be expressly stated in the MIA (see recommendation 18). The relevant provisions in the ICA should provide the

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638 Insurance Council of Australia Submission 11.

639 MLAANZ Submission 12.

640 Ibid.

641 S Derrington Submission 13.

drafting model. These also permit the insurer to cancel the contract if the insured has breached its obligations of good faith or has made a fraudulent claim. The Commission proposes retaining these elements of ICA s 59–60 as well.

9.229 However, the parties should remain free to include express terms that deal with rights and procedures of cancellation. Accordingly, the new provisions should be expressed to be subject to the terms of the contract. The Commission does not recommend that the MIA include a provision akin to ICA s 63, which limits the rights of cancellation to those set out in that Act.

## **Recommendations**

**Recommendation 7.** The concept of warranties, both express and implied, as used in the law of marine insurance should be abolished and replaced with a system permitting the subject matter currently covered by them to be the subject of express terms of the contract. Except as provided by the Act as amended (see recommendation 14) and subject to the terms of the contract, a breach by the insured of an express term (including those replacing warranties) will entitle insurers to be relieved of liability to indemnify the insured for a loss where the breach is causative of that loss.

### *Express warranties*

**Recommendation 8.** Obligations currently covered by express warranties should be dealt with as express terms of the contract.

**Recommendation 9.** Subject to the contract, the MIA should be amended so that an insurer is entitled to be discharged from liability to indemnify the insured for any loss proximately caused by a breach by the insured of any express term of the contract.

### *Warranty of seaworthiness*

**Recommendation 10.** The MIA should be amended to repeal the implied warranties of seaworthiness. Obligations of seaworthiness should be dealt with as express terms of the contract.

**Recommendation 11.** The MIA should be amended so that an insurer is discharged from liability to indemnify the insured for any loss attributable to a breach of an express term of the contract relating to the seaworthiness of a ship where the insured knew or ought to have known of the relevant circumstances and that they rendered the vessel unseaworthy and where the insured failed to take such remedial steps as were reasonably available to it.

*Alternative recommendation*

**Recommendation 12.** If recommendations 10–11 are not adopted, the distinction between time and voyage policies with regard to the warranty of seaworthiness should be abolished and the formulation in MIA s 45(5) should be the basis of a common statement of the warranty. The implied warranty in MIA s 46(2) should be removed.

*Warranty of legality*

**Recommendation 13.** The MIA should be amended to repeal the implied warranty of legality. Obligations of legality should be dealt with as express terms of the contract.

**Recommendation 14.** The MIA should be amended so that where the insured is in breach of an express contractual term to the effect that, so far as the insured can control the matter, the insured adventure shall have no unlawful purpose, the insurer is discharged from all liability under the contract.

**Recommendation 15.** The MIA should be amended so that where the insured is in breach of an express contractual term to the effect that, so far as the insured can control the matter, the insured adventure shall be carried out in a lawful manner, the insurer is discharged from liability to indemnify the insured in relation to any loss that is attributable to that breach.

*Change of voyage*

**Recommendation 16.** The provisions of the MIA s 48 and 51–55 relating to change of voyage, deviation and delay should be repealed, permitting these concepts to be dealt with as express terms of the contract. MIA s 49–50, which deal with the attachment of the risk, should be retained.

***Interpretation of express warranties***

**Recommendation 17.** The provisions of the MIA dealing with the warranties of neutrality, nationality and good safety (MIA s 42–44) should be repealed as redundant because they are rarely used in practice and can be the subject matter can be dealt with by express terms.

***Cancellation rights***

**Recommendation 18.** The MIA should be amended to include new provisions based on ICA s 59–60 stipulating the insurer's rights of cancellation. These rights are subject to the terms of the contract. They arise when the insured has failed to comply with a term of the contract, breached the duty of utmost good faith, made a fraudulent claim under the contract or where otherwise permitted by the Act as amended in accordance with these recommendations. Written notice must be given to the insured. The cancellation may take effect either three business days after the insured received that notice or earlier if replacement insurance comes into effect before then.

***Burden of proof***

**Recommendation 19.** The MIA should be amended to insert new provisions that

- (1) the insurer bears the burden of proving that there was a breach of a term of the contract and
- (2) the insured bears the burden of showing that the loss for which it seeks to be indemnified was not proximately caused by or attributable to (as the case may be) the breach.

These provisions are not intended to alter the burdens of proof provided for elsewhere by common law or statute.

## 10. Utmost good faith

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### Introduction

10.1 Marine insurance contracts, like insurance contracts at common law, are based upon the utmost good faith of the parties. Section 23 of the MIA states

23. A contract of marine insurance is a contract based upon the utmost good faith, and, if the utmost good faith be not observed by either party, the contract may be avoided by the other party.

10.2 While it is customary to refer to the ‘duty’ of utmost good faith, the MIA does not use this expression and s 23 simply states that the contract is ‘based upon’ utmost good faith.<sup>642</sup> The requirement of utmost good faith gives rise to a range of duties, some of which apply before formation of the contract and others which apply after formation. For these reasons some legal commentators prefer to refer to the ‘doctrine’ of utmost good faith.<sup>643</sup>

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<sup>642</sup> In contrast, the ICA also states that there is implied in insurance contracts a provision requiring each party to act with utmost good faith: ICA s 13.

<sup>643</sup> See H Bennett ‘Mapping the Doctrine of Utmost Good Faith in Insurance Contract Law’ [1999] *Lloyd’s Maritime and Commercial Law Quarterly* 165, 166. See also Y Baatz ‘Utmost Good Faith in Marine Insurance Contracts’ in M Huybrechts E Van Hooydonk & C Dieryck (eds) *Marine Insurance at the Turn of the Millennium* vol I Intersentia Antwerp 1999.

10.3 This doctrine is one of the principal distinctions between insurance law and general contract law. The doctrine commences before the policy is made, manifests as the duty of disclosure, and continues as long as the parties remain in a contractual or continuing relationship.<sup>644</sup> The doctrine applies equally to the insurer and the insured.

10.4 The effect of s 23 is that if the utmost good faith is not observed by one party, the contract may be rescinded (retrospectively avoided) by the other party. There is no other remedy.

10.5 There has been some debate about whether ‘utmost’ good faith is different from mere good faith.<sup>645</sup> Irrespective of the conclusion, even if the inclusion of the word ‘utmost’ in the MIA (UK) was novel, almost a century later the term is established and the Commission does not seek to re-examine this question.

### **What are the duties of utmost good faith?**

10.6 The insured’s obligations concerning pre-contractual non-disclosure and misrepresentation, dealt with by s 24–26 of the MIA, are the most significant manifestations of breach of utmost good faith and are discussed in detail below. Once an insured has complied with the requirements of the duty of disclosure, and paid the premium, the insured’s major exposure to the duty of utmost good faith involves the presentation of claims and conduct in negotiating alterations of the risks covered by the contract.

10.7 The insurer’s duty of disclosure covers disclosure of all facts material either to the nature of the risk sought to be covered or the recoverability of a claim under the policy which a prudent insured would take into account in deciding whether or not to place the risk with that insurer.<sup>646</sup> This obligation is the ‘flip side’ of the insured’s duty of disclosure.<sup>647</sup>

10.8 The insurer’s duties of utmost good faith may apply where it has made representations about the effect of clauses restricting the ambit of the policy; where there are unusual clauses which have not been brought to the attention of the

644 *Boulton v Holder Bros* (1904) 1 KB 784, 791. See C Larkin ‘Uberrima Fides: Quo Vadis? Where to From Here?’ (1995) 7 (2) *Bond Law Review* 18.

645 It is arguable that the adjective ‘utmost’ adds nothing: S Henchcliffe ‘Insurance Claims: Fraud and the Duty of Good Faith’ (1997) 8 *Insurance Law Journal* 210, 210. See also F Hawke ‘Utmost Good Faith: What Does it Really Mean?’ (1994) 6(2) *Insurance Law Journal* 91.

646 *Banque Keyser Ullmann SA v Skandia (UK) Insurance Co Ltd* [1990] 1 QB 665, 772.

647 Although, as discussed below, since *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd* [1995] 1 AC 501, a material non-disclosure may well only be grounds for avoidance by an insured who is subjectively induced into the contract.

insured; in making determinations about particular matters under the contract of insurance;<sup>648</sup> and in dealing with and settling claims.<sup>649</sup> The nature of the parties' post-formation duties is discussed in more detail below.<sup>650</sup>

## The duty of disclosure

10.9 The duty of utmost good faith requires the insured to disclose fully and accurately every material circumstance regarding the particular contract of insurance. The classical statement of the duty and the reason for its imposition was stated by Lord Mansfield in *Carter v Boehm*.

The special facts, upon which the contingent chance is to be computed, lie most commonly in the knowledge of the insured only; the under-writer trusts to his representation, and proceeds upon confidence, that he does not keep back any circumstance in his knowledge, to mislead the underwriter into a belief that the circumstance did not exist, and to induce him to estimate the risque, as if it did not exist.<sup>651</sup>

10.10 The duty of disclosure is codified in s 24 of the MIA as follows.

24(1) Subject to the provisions of this section, the assured must disclose to the insurer, before the contract is concluded, every material circumstance which is known to the assured, and the assured is deemed to know every circumstance which, in the ordinary course of business, ought to be known by him. If the assured fails to make such disclosure, the insurer may avoid the contract.

(2) Every circumstance is material which would influence the judgment of a prudent insurer in fixing the premium, or determining whether he will take the risk.

10.11 Duties relating to pre-contractual representations are dealt with in s 26, which contains a definition of materiality framed in similar terms.<sup>652</sup>

26(1) Every material representation made by the assured or his agent to the insurer during the negotiations for the contract, and before the contract is concluded, must be true. If it be untrue the insurer may avoid the contract.

(2) A representation is material which would influence the judgment of a prudent insurer in fixing the premium, or determining whether he will take the risk.

(3) A representation may be either as to a matter of fact, or as to a matter of expectation or belief.

648 See N Rein 'Utmost Good Faith in Marine Insurance' (1999) 10 *Insurance Law Journal* 145, 160–1.

649 See authorities cited in Y Baatz 'Utmost Good Faith in Marine Insurance Contracts' in M Huybrechts E Van Hooydonk & C Dieryck (eds) *Marine Insurance at the Turn of the Millennium* vol I Intersentia Antwerp 1999, 15, 18–19. See also para 12.5 on subrogation.

650 See para 10.121–10.130.

651 (1799) 3 Burr 1905, 1909.

652 For most purposes it is not necessary to distinguish between non-disclosure and misrepresentation and the discussion in this chapter proceeds on that basis.

(4) A representation as to a matter of fact is true, if it be substantially correct, that is to say, if the difference between what is represented and what is actually correct would not be considered material by a prudent insurer.

10.12 It is a question of fact whether or not a particular circumstance or representation is material or not.<sup>653</sup> The insurer may avoid the contract if a material circumstance was not disclosed or if a material misrepresentation was made, even if the non-disclosure or misrepresentation had nothing to do with the losses sustained. This is the only remedy provided by the Act — an all-or-nothing position.

10.13 There is a great deal of jurisprudence<sup>654</sup> but little consensus among courts in the United Kingdom and Australia as to the interpretation of the MIA's definition of a material circumstance or representation.<sup>655</sup> The Commission takes the decision of the House of Lords in *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd*,<sup>656</sup> the leading English decision on what constitutes a material circumstance, as its starting point in understanding the present law in this area.

10.14 In relevant respects the approach to materiality taken in *Pan Atlantic* was applied by the Supreme Court of Victoria in *Akedian Co Ltd v Royal Insurance Australia Ltd, Sun Alliance Australia Ltd*.<sup>657</sup> Justice Byrne considered that, at least since *Pan Atlantic*, the question of materiality should be addressed in two stages. The first stage requires an assessment of the impact of the non-disclosure or the misrepresentation upon the mind of a hypothetical prudent insurer. The second is anchored in the facts of each case and requires the court to determine whether the misrepresentation or non-disclosure in fact induced the underwriter to issue the policy.<sup>658</sup> The discussion below deals with each of these aspects of materiality in turn.

653 MIA s 24(4); s 26(7).

654 See eg *Container Transport International Inc and Reliance Group Inc v Oceanus Mutual Underwriting Association (Bermuda) Ltd* [1984] 1 Lloyd's Rep 476; *St Paul Fire & Marine Insurance Co (UK) v McConnell Dowell Constructors Ltd* [1995] 2 Lloyd's Rep 116; *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd* [1995] 1 AC 501. In Australia *Mayne Nickless v Pegler* [1974] 1 NSWLR 228; *Barclay Holdings v British National Insurance Co Ltd* (1987) 8 NSWLR 514; *Visscher Enterprises Pty Ltd v Southern Pacific Insurance Co Ltd* [1981] Qd R 561; *Akedian Co Ltd v Royal Insurance Australia Ltd, Sun Alliance Australia Ltd* (1997) 148 ALR 480.

655 See S Derrington 'The Requirement of Inducement and the Concept of Materiality in Section 24 of the Marine Insurance Act 1909' (2000) 11 *Insurance Law Journal* 236, 237–4.

656 [1995] 1 AC 501. Although the issues in this case arose under a policy of non-marine insurance, the House of Lords considered that it was convenient to state them by reference to the Marine Insurance Act 1906 (UK) since it was accepted in argument that in relevant respects the common law relating to general and marine insurance was the same: 518.

657 (1997) 148 ALR 480.

658 *Ibid* 487.



## The ‘prudent insurer’

10.15 As noted above, the MIA states that a material circumstance or representation is one which ‘would influence the judgment of a prudent insurer’. This raises questions about whether, for example, influence means ‘mere influence’, as in a simple effect on the thought process of the prudent insurer, or ‘decisive influence’, where full disclosure of the material circumstance would have led a prudent insurer to a different decision on accepting or rating the risk.

10.16 The case law indicates that English and Australian courts have adopted differing views of what this part of the test of the materiality involves. In *Pan Atlantic* the House of Lords clearly rejected a ‘decisive influence’ test. Justice Kirby has summarised the policy objection to this test as follows.

A risk of the decisive influence test was that assureds would disclose only circumstances which they were advised would be of decisive influence to the prudent insurer. Aware of that fact, a truly careful insurer would have to inquire for itself, specifically, as to all those circumstances which, while not decisive, would collectively influence the assessment and acceptance of the risk. Of course, the insurer’s gathering of such information would have a price. It is not unreasonable to suppose that, ultimately, the consumers of goods which had been the subject of some form of marine insurance would pay that price.<sup>659</sup>

10.17 However, their Lordships’ speeches do not make clear precisely what lesser standard the courts are to apply. The majority appears to have found in favour of a definition requiring merely that the circumstance would have an effect, but not necessarily a decisive effect, on the insurer. That is, an insured must disclose all circumstances which would tend to increase the risk in the mind of a prudent insurer, even though a prudent insurer might not have increased the premium.<sup>660</sup>

10.18 Lord Goff required no more than that the circumstance would have ‘an effect on the mind of the insurer in weighing up the risk’<sup>661</sup> and Lord Mustill spoke of the relevant circumstance having ‘an effect on the thought processes of the insurer in weighing up the risk’ and extending to ‘all matters which would have been taken into account by the underwriter when assessing the risk’.<sup>662</sup>

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659 M Kirby ‘Marine Insurance: Is the Doctrine of “Utmost Good Faith” Out of Date?’ (1995) 13(1) *Australian Bar Review* 1, 12.

660 *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd* [1995] 1 AC 501, 517, 531, 538.

661 *Ibid* 517.

662 *Ibid* 531, 538.

10.19 *Arnould's Law of Marine Insurance and Average* concludes that the test laid down by the majority in *Pan Atlantic* is 'whether the matter would have been taken into account by the hypothetical prudent insurer when assessing the risk'.<sup>663</sup> One commentator has observed that

[t]he degree of dissent between the judges in the House of Lords on this issue is illustrated by the fact that Lord Lloyd regarded the "decisive influence" test, which he favoured, as "precise and clear-cut", giving "certainty and practicality", whereas Lord Mustill considered that the "decisive influence" test "presented great difficulties".<sup>664</sup>

10.20 A broader test of materiality was later applied by the English Court of Appeal in *St Paul Fire & Marine Insurance Co (UK) v McConnell Dowell Constructors Ltd*<sup>665</sup> — that a non-disclosed fact is material where, had it been disclosed, the prudent underwriter would have appreciated that it was a different risk. This alternative formulation was rejected by Justice Byrne of the Victorian Supreme Court in *Akedian*<sup>666</sup> as inconsistent with *Pan Atlantic* and with New Zealand and earlier Australian authorities.<sup>667</sup>

10.21 In *Akedian* Justice Byrne adopted the test enunciated in the New South Wales Supreme Court case *Mayne Nickless v Pegler*, in which Justice Samuels held that a fact is material 'if it would have reasonably affected the mind of the prudent insurer in determining whether he will accept the insurance, and if so, at what premium and on what conditions'.<sup>668</sup> In New Zealand, the High Court held in *Quinby Enterprises (in liq) v General Accident Fire & Life Assurance Corporation Public Ltd* that the test since *Pan Atlantic* is 'whether the relevant information would have had an effect on the mind of a prudent insurer in weighing up the risk'.<sup>669</sup>

663 M Mustill and J Gilman *Arnould's Law of Marine Insurance and Average* 16th ed vol III Stevens & Sons London 1997, 462.

664 P Griggs 'Is the Doctrine of Utmost Good Faith Out of Date?' *Paper Marine Insurance Seminar CMI 35th International Conference, Sydney October 1994* referring to *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd* [1995] 1 AC 501, 531 (Lord Mustill), 558 (Lord Lloyd).

665 [1995] 2 Lloyd's Rep 116, 122–4.

666 (1997) 148 ALR 480, 488–90.

667 *Quinby Enterprises (in liq) v General Accident Fire & Life Assurance Corporation Public Ltd Co* [1995] 1 NZLR 736; *Mayne Nickless v Pegler* [1974] 1 NSWLR 228, 239; *Barclay Holdings (Australia) Pty Ltd v British National Insurance Co Ltd* (1987) 8 NSWLR 514. However, these earlier authorities do not specifically require inducement of the actual insurer, as in *Pan Atlantic*.

668 [1974] 1 NSWLR 228, 239; *Akedian Co Ltd v Royal Insurance Australia Ltd, Sun Alliance Australia Ltd* (1997) 148 ALR 480, 490. The test in *Mayne Nickless v Pegler* was followed, but given a narrower interpretation, by the New South Wales Court of Appeal in *Barclay Holdings (Australia) Pty Ltd v British National Insurance Co Ltd* (1987) 8 NSWLR 514; see K Sutton *Insurance Law in Australia* 3rd ed LBC Information Services Sydney 1999, 211–6. Justice Carruthers submitted that the test in *Mayne Nickless v Pegler* has 'worked well in practice': K Carruthers *Submission* 9.

669 [1995] 1 NZLR 736, 740.

10.22 Professor Sutton has concluded that the various judicial pronouncements make it likely that Australian courts will adopt a test based on that in *Mayne Nickless v Pegler*. In Sutton's formulation such a test would require the disclosure of facts

which *at the time of making* the crucial decision whether or not to accept the risk and if so, on what terms, are relevant in the sense that they have a bearing on that decision, although if known they need not cause the proposal to be rejected or more onerous terms to be imposed.<sup>670</sup>

### Criticism of the prudent insurer test

10.23 It is not enough to fulfil the duty of disclosure that the insured disclose all facts which a prudent or reasonable insured would believe it necessary to disclose. The test assumes that the insured has the business knowledge of a prudent insurer and requires the insured to disclose those facts that would influence the insurer's judgment. An insured who does not know what circumstances would be influential to the prudent insurer may inadvertently breach the duty of disclosure. This aspect of the duty of disclosure has been widely criticised as imposing an unrealistic and unfair burden on the insured.

10.24 The prudent insurer is, like other 'objective' standards, such as that of the 'reasonable person', a malleable concept. As Anthony Diamond QC has observed

Suppose that you or I, as reasonable prospective assureds, were to go in search of the prudent insurer. He is to be found, if anywhere at all, in the Room at Lloyd's. So let us suppose that you or I were to go to Lime Street ... to interrogate the working underwriters, or least those of them that write marine business and are thus subject to the Act of 1906. What would we find if we began to ask a few questions? Surely we would find a few prudent underwriters. But also, in all probability, even in that ancient institution, we would find some who are not prudent at all. And even the great majority who are without question prudent underwriters, would tell us, if we persisted in our questioning, that there are occasions when they simply cannot afford to be prudent. For example, one might say that he cannot afford not to write a fixed line on every risk presented by a certain broker; otherwise he would never see that broker again. Or another might tell us that he has on occasion to write "loss leaders" knowing that the business will be unprofitable and in the hope of getting an entrée into a particular line of business in the future.<sup>671</sup>

10.25 Diamond suggested that consideration should be given to replacing the MIA test of the 'prudent insurer' with a duty to disclose what a reasonable insured would disclose,<sup>672</sup> along the lines of the ICA (see paragraphs 10.55–10.57). However, a problem may be that

<sup>670</sup> K Sutton *Insurance Law in Australia* 3rd ed LBC Information Services Sydney 1999, 216.

<sup>671</sup> A Diamond 'The Law of Marine Insurance: Has it a Future?' (1986) *Lloyd's Maritime and Commercial Law Quarterly* 25, 30–1.

<sup>672</sup> *Ibid* 34.

[s]uch a formulation ... whilst still apparently objective, in fact would result in greater difficulty in assessing the standard by which to judge the information which ought to be disclosed to the insurer and would result in a greater degree of uncertainty. This is because the benchmark of a “prudent insurer” is relatively easy to fix as compared with the myriad of “reasonable assureds” who could vary as widely as minor exporter/importer to multibillion dollar ship owning company. Generally, an insurer is a more certain beast than an assured.<sup>673</sup>

10.26 The MIA does place some limits on the scope of the duty of disclosure. Section 24(3) states

24(3) In the absence of inquiry the following circumstances need not be disclosed, namely:

- (a) Any circumstance which diminishes the risk;
- (b) Any circumstance which is known or presumed to be known to the insurer. The insurer is presumed to know matters of common notoriety or knowledge, and matters which an insurer in the ordinary course of his business, as such, ought to know;
- (c) Any circumstance as to which information is waived by the insurer;
- (d) Any circumstance which it is superfluous to disclose by reason of any express or implied warranty.

10.27 There are difficulties in defining the scope of the information which, under s 24(3), need not be disclosed to an insurer. For example, fertiliser has a tendency to ‘cake’ on exposure to moisture, a relevant factor in the level of risk involved in its carriage by sea. This fact would be well known to insurers who specialise in the insurance of this commodity but perhaps not to others.<sup>674</sup>

10.28 Dr Malcolm Clarke has suggested that in practice s 24(3) has been narrowly interpreted.<sup>675</sup> He observed that while the insurer can be expected to know less about the particular risk than the insured whose risk it is, the insurer could be expected to have considerable general knowledge of the kind of risk and of the social, commercial and political context.<sup>676</sup> For example, an insurer of pleasure boats is taken to know that, if they are laid up for the winter in Spain, a certain level of theft and vandalism is to be expected.<sup>677</sup>

10.29 However, an insurer is not expected to recall events reported in the past, however prominent, which later turn out to be relevant to a risk proposed later. Clarke cites the leading case of *Bates v Hewitt*,<sup>678</sup> in which a former Confederate

673 S Derrington ‘The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform’ *Ph D thesis* University of Queensland November 1998, 82.

674 Judges *Consultation* Sydney 15 May 2000.

675 M Clarke ‘The Marine Insurance System in Common Law Countries — Status and Problems’ Paper Marine Insurance Symposium Oslo 4–6 June 1998.

676 *Ibid.*

677 *Sharp and Roarer Investments Ltd v Sphere Drake Insurance plc, Minster Insurance Co Ltd and EC Parker and Co Ltd (The Moonacre)* [1992] 2 Lloyd’s Rep 501.

678 (1867) LR 2 QB 595.

warship of some notoriety was converted into a merchant vessel. This material fact (material since it rendered the vessel liable to capture by the US Navy) was not disclosed by the insured. Even though the insurer admitted that he knew that a vessel of the same name in Confederate service had been sold and was found to have had ‘abundant means of identifying the ship’, the duty of disclosure was found to have been breached by the insured.

### The role of brokers

10.30 An insured is protected to some extent from the consequences of a breach of the duty of disclosure by the use of specialist brokers as intermediaries between the insurer and the insured in the traditional United Kingdom and related markets, including Australia.

10.31 Section 25 of the MIA provides that, subject to the provisions of s 24 as to circumstances which need not be disclosed,

where an insurance is effected for the assured by an agent, the agent must disclose to the insurer:

- (a) every material circumstance which is known to himself, and an agent to insure is deemed to know every circumstance which in the ordinary course of business ought to be known by, or to have been communicated to, him; and
- (b) every material circumstance which the assured is bound to disclose, unless it come to his knowledge too late to communicate it to the agent.

10.32 Similarly, duties relating to pre-contractual representations are placed on both the insured and the insured’s broker or other agents.<sup>679</sup>

10.33 Most harshly, the insured’s agent is required to disclose every material circumstance, which in the ordinary course of business ought to have been communicated to him or her. Failure to do so may visit upon the insured the calamity of avoidance by the insurer. There is no restriction in the Act as to who ought to have communicated the information to the agent. An insured can, therefore, be left without cover because a third party over whom the insured has no control fails to pass on to the agent material information not known either to the insured or the agent.

10.34 In many situations of non-disclosure or misrepresentation, the insured will have an action available against its broker. For example, *Helicopter Resources Pty Ltd v Sun Alliance Insurance Ltd*<sup>680</sup> involved a policy of marine insurance over

<sup>679</sup> MIA s 26(1).

<sup>680</sup> (Unreported) Supreme Court of Victoria 26 March 1991 (Ormiston J). See S Hetherington ‘Marine Insurance: Non-disclosure — *Helicopter Resources Pty Ltd v Sun Alliance Australia Ltd*’ (1992) 5 *Insurance Law Journal* 86.

four helicopters to be carried on a ship from Hobart to the Antarctic. In the Supreme Court of Victoria, Justice Ormiston found that the underwriters were entitled to avoid the policy due to the failure of the insured party to disclose, among other things, the nature of arrangements relating to the securing and lashing of the helicopters on board the ship. The judge went on to consider whether the broker was liable to the insured for having failed to disclose those matters which had been successfully relied upon by the underwriters as not having been disclosed. While the judge found that the broker had no direct knowledge of the method of stowing the helicopter, he found that the broker's duty to a client was not limited to disclosing that information of which the broker is directly aware.

A reasonable broker ... must do more for his client. If his client may be at risk of having his insurance cover avoided for non-disclosure, the broker must have a duty to inform himself of sufficient of the business activities of his client to carry out his duties adequately and in particular to prevent the avoidance of liability under any policy written ... The broker cannot, of course, discover everything, but he must attempt to discover those elements in the activities of the client which might put its cover in jeopardy.<sup>681</sup>

10.35 Stuart Hetherington has observed that the obligation imposed on brokers to understand the business of the client places an onus on the broker which may be unrealistic in many circumstances.<sup>682</sup>

## Inducement of the actual insurer

10.36 In reaching its decision in the *Pan Atlantic* case,<sup>683</sup> the House of Lords overruled, in part, the decision of the English Court of Appeal in *Container Transport International Inc and Reliance Group Inc v Oceanus Mutual Underwriting Association (Bermuda) Ltd*<sup>684</sup> (the CTI case). In the CTI case, the Court of Appeal held, essentially, that so long as an undisclosed fact was something a hypothetical prudent insurer would have liked to have known about, the actual insurer could avoid the contract, regardless of whether the undisclosed fact had any bearing on the actual insurer's decision to accept the risk on the terms the insurer did.<sup>685</sup> A reckless underwriter could write risks without caution, accept

681 *Helicopter Resources Pty Ltd v Sun Alliance Insurance Ltd* (Unreported) Supreme Court of Victoria 26 March 1991 (Ormiston J) as cited in S Hetherington 'Marine Insurance: Non-disclosure — Helicopter Resources Pty Ltd v Sun Alliance Australia Ltd' (1992) 5 *Insurance Law Journal* 86, 89.

682 S Hetherington 'Marine Insurance: Non-disclosure — Helicopter Resources Pty Ltd v Sun Alliance Australia Ltd' (1992) 5 *Insurance Law Journal* 86, 90–1.

683 *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd* [1995] 1 AC 501.

684 [1984] 1 Lloyd's Rep 476.

685 S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' *Ph D thesis* University of Queensland November 1998, 83. See *Container Transport International Inc and Reliance Group Inc v Oceanus Mutual Underwriting Association (Bermuda) Ltd* [1984] 1 Lloyd's Rep 476, 492, 529, 507, 510, 511.

premium, and then avoid the policy if the circumstances presented themselves based on the standards of a prudent underwriter which the actual underwriter had ignored.

10.37 In *Pan Atlantic*, the Court unanimously held that in order to avoid the contract the actual insurer had to be induced to enter the contract on the agreed terms by the material misrepresentation or non-disclosure. That is, an insured has a duty to disclose all circumstances which would tend to increase the risk in the mind of the prudent insurer; however, if the actual insurer was not induced by the non-disclosure or misrepresentation the insurer could not avoid the contract.

10.38 In his judgment, Lord Mustill stated the underlying policy reason for implying a requirement of inducement — that it would be unjust for an insurer who did not rely on a non-disclosure or misrepresentation to be entitled to avoid the contract. Lord Mustill rejected arguments that the absence of any reference to causation in the MIA stemmed from a ‘disciplinary element in the law of marine insurance’, which should be confirmed in the law. He stated

The existing rules [as stated in *Pan Atlantic*], coupled with a presumption of inducement, are already stern enough, and to enable an underwriter to escape liability when he has suffered no harm would be positively unjust, and contrary to the spirit of mutual good faith recognised by section 17 [MIA s 23], the more so since non-disclosure will in a substantial proportion of cases be the result of an innocent mistake.<sup>686</sup>

10.39 To some extent Australian courts anticipated the *Pan Atlantic* decision. In *Visscher Enterprises Pty Ltd v Southern Pacific Insurance Co Ltd*,<sup>687</sup> the Full Court of the Supreme Court of Queensland held that regard could be had to the fact that the actual insurer would not have declined to take the risk had the insurer known of the undisclosed circumstance, and the requirement for the actual insurer to be induced to issue the policy was confirmed after *Pan Atlantic* in *Akedian*.<sup>688</sup>

### Problems with actual inducement

10.40 It is worth noting that the statutory definitions of materiality in MIA s 24(2) and 26(2) make no reference at all to the inducement of the actual insurer. Desirable as it may be, the requirement that the actual insurer be induced to enter into the contract is a judicial invention.

<sup>686</sup> *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd* [1995] 1 AC 501, 549.

<sup>687</sup> [1981] Qd R 561. The Court distinguished between cases in which the undisclosed fact was ‘obviously’ material and those cases in which the undisclosed fact was ‘not obviously material’. In the latter situation the Court held that the actual inducement of the underwriter is necessary to find a breach of the duty of disclosure, but not in the former: 582–3.

<sup>688</sup> *Akedian Co Ltd v Royal Insurance Australia Ltd, Sun Alliance Australia Ltd* (1997) 148 ALR 480, 487.

10.41 *Pan Atlantic* establishes that no breach of the duty of disclosure is actionable unless it induces the actual insurer into the contract. However, it is not entirely clear what ‘inducement’ means.

Ascertaining the meaning of inducement requires an answer to the same question as arose in the context of materiality. Must a misrepresentation decisively influence the actual underwriter into concluding the contract? Must it be shown that disclosure of the relevant circumstance would have caused the actual underwriter either to refuse the risk or alter the terms? Alternatively, does it suffice that the misrepresentation was a factor present in the mind of the underwriter when making his decision, even if not a decisive factor, or simply that the fact misrepresented was taken into account by the actual underwriter when assessing the risk?<sup>689</sup>

10.42 Howard Bennett concluded that a decisive influence test of inducement is correct and has the support of legal authority.<sup>690</sup> However, in *Pan Atlantic*, Lord Mustill simply stated that he was using ‘induced’ in the sense in which it is used in the general law of contract.<sup>691</sup> At least in Australia, this may mean that the representation need not be the sole inducement and it may be sufficient so long as it plays some part even if only a minor part in contributing to the formation of the contract.<sup>692</sup>

10.43 Some doubt also remains about which party bears the burden of proof in relation to inducement. In *Pan Atlantic*, Lord Mustill referred to a presumption of inducement, which would go against the general law of inducement in other contexts.<sup>693</sup> If there is a presumption of inducement in marine insurance cases the insured would have the difficult task of producing evidence to prove that the insurers were not actually induced into making the contract.<sup>694</sup>

10.44 There can also be evidentiary problems associated with proof of what the actual underwriter would have done if it had been aware of the circumstances not disclosed or misrepresented and the terms on which the underwriter would have

689 H Bennett *The Law of Marine Insurance* Clarendon Oxford 1996, 55.

690 Ibid 57–8. Bennett states that the decisive influence test of inducement is preferable on principle as, if the breach of the duty of disclosure causes the insurer no prejudice (in that the insurer would have underwritten the risk on the same terms even had the duty not been breached) to deprive the insured of cover would be ‘unwarrantably punitive’.

691 *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd* [1995] 1 AC 501, 549.

692 See the rules relating to inducement and pre-contractual misrepresentations stated by the High Court in *Gould v Vaggelas* (1984) 157 CLR 215, 236; N Seddon and M Ellinghaus *Cheshire and Fifoot’s Law of Contract* 7th Australian ed Butterworths Sydney 1997, 391–5.

693 [1995] 1 AC 501, 551.

694 In *St Paul Fire & Marine Insurance Co (UK) v McConnell Dowell Constructors Ltd* [1995] 2 Lloyd’s Rep 116, 127, the English Court of Appeal presumed the inducement of one of the four underwriters who had not given evidence at the trial. However, it has been observed that the facts in this case were exceptional enough to warrant such a presumption — the three other underwriters had given evidence tending to show inducement, but at a time when inducement of the actual underwriter was not a legal necessity (as the trial took place before the House of Lords’ decision in *Pan Atlantic*): Y Baatz ‘Utmost Good Faith in Marine Insurance Contracts’ in M Huybrechts E Van Hooydonk & C Dieryck (eds) *Marine Insurance at the Turn of the Millennium* vol I Intersentia Antwerp 1999, 15, 18.



accepted the risk.<sup>695</sup> In *Akedian*, Justice Byrne referred to the difficulty of the court evaluating the evidence of insurers that they were induced.

Whether one calls it a presumption of fact or a matter of inference, there is a very short step between a conclusion that the mind of a prudent underwriter would be affected by a matter and the further conclusion that this underwriter before the court was so induced. This is more difficult in the case of a non-disclosure because the question cannot be that these insurers were induced to issue the policy in question by something of which they were ignorant; it must be that they would not have issued that policy if they had been aware of the non-disclosed fact.<sup>696</sup>

10.45 Similar evidentiary problems can occur in disputes concerning contracts under the ICA. For example, s 28(1) of the ICA provides that the insurer's remedies for non-fraudulent non-disclosure or misrepresentation are not available where 'the insurer would have entered into the contract, for the same premium and on the same terms and conditions, even if the insured had not failed to comply with the duty of disclosure or had not made the misrepresentation before the contract was entered into'.

10.46 There also may be problems in establishing actual inducement of the underwriter where market practice involves the placement of insurance through the use of slips. This results in a series of separate contracts with the terms negotiated between the broker and the leading underwriters. Following underwriters generally rely on the line initialled by the leaders. The question arises as to how the inducement of the following underwriters can be established. Howard Bennett suggests that for the requirement for actual inducement<sup>697</sup> to be reconciled with the practice of the London market, non-disclosure or misrepresentation made to a leading underwriter would have to be considered to have been made to following underwriters as well.<sup>698</sup>

## **Reform of the scope of the duty of disclosure**

### **The purpose of the duty**

10.47 The common law duty of disclosure, which was codified in the MIA and reformed by the ICA, developed around the idea that, because of the subject matter of insurance, the facts that might materially affect the risk were usually within the knowledge of the insured rather than the insurer. Therefore, the insured was required to provide full and complete disclosure.

<sup>695</sup> G Staring and G Waddell 'Marine Insurance' (1999) 73 *Tulane Law Review* 1619, 1656–7.

<sup>696</sup> *Akedian Co Ltd v Royal Insurance Australia Ltd, Sun Alliance Australia Ltd* (1997) 148 ALR 480, 494.

<sup>697</sup> As required by the test for material non-disclosure established by *Pan Atlantic*.

<sup>698</sup> H Bennett *The Law of Marine Insurance* Clarendon Oxford 1996, 59 citing *Pawson v Watson* (1778) 2 Cowp 785.

10.48 The question arises whether this assumption is as valid in modern market practice. Certainly insurers possess ever more sophisticated statistical data to assist in determining and managing risk. In its 1982 report *Insurance Contracts*, the Commission stated

The origin of the duty of disclosure lay in the superior knowledge of factors relevant to the risk which the insured possessed in early marine insurance, when underwriting expertise was in its infancy. It is often said that position has, in most cases of insurance, now been reversed: insurers have available to them sophisticated statistical data and obtain information on many aspects of the risk which they undertake.<sup>699</sup>

10.49 Dr Malcolm Clarke has observed that exceptions to the duty of disclosure have not developed to recognise changes in the means of collating, collecting and recalling information. In particular, the duty allows the insurer to plead ignorance of information which the insurer has on file. Clarke has questioned whether insurers need this level of protection and noted that in Canada general insurance law provides that, if the insurer fails to look in its own files, it is deemed to have waived disclosure of the information which they contain.<sup>700</sup>

10.50 In this context Clarke noted his preference for a disclosure rule that minimises the joint costs of a potential mistake by assigning the risk of its occurrence to the party who is the better (cheaper) information gatherer. For example, in Canada aviation insurers must scan the public records of accidents that might have a bearing on the risk.<sup>701</sup> In contrast, he suggests that the traditional interpretation of the duty of disclosure in marine insurance law is not efficient because it does nothing to encourage the insurer to acquire available information by investigation. The insurer knows that if the risk turns out to be greater than appears on a superficial presentation the insurer can fall back on rules to avoid the contract.

10.51 In relation to such criticisms, commentators, including the Commission in its report on insurance contracts, have noted the distinction between general information and information on the particular risk. The Commission noted

It is true that the insurer has superior, even exclusive knowledge of statistical matters relevant to numerous categories and subcategories of risk. But it does not have superior knowledge of the particular risk.<sup>702</sup>

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699 ALRC 20 para 175.

700 M Clarke 'The Marine Insurance System in Common Law Countries — Status and Problems' *Paper Marine Insurance Symposium Oslo 4–6 June 1998* citing *Coronation Insurance Company v Taku Air Transport Ltd* (1991) 85 DLR (4th) 609, 623. However, the Commission queries whether some of these problems could not be resolved by applying MIA s 24(3)(b), which provides that the insured does not have to disclose circumstances that the insurer knows or ought to know.

701 *Coronation Insurance Company v Taku Air Transport Ltd* (1991) 85 DLR (4th) 609.

702 ALRC 20 para 175.

10.52 Further, other commentators consider that the rule of utmost good faith remains grounded in economic efficiency.

It is a rule designed to minimise cost to both insurers and assureds. Investigation of risks costs money. In marine insurance cases the particulars of the risk are peculiarly within the knowledge of the assured ... Some have disputed the necessity for the rule based upon modern social and economic conditions. In some areas of insurance, risks may no longer be individually evaluated and the rule may be less compelling. But marine insurance remains an industry where individualized risk calculation and negotiation still play a key role. Thus, the doctrine of utmost good faith is of continuing importance, particularly in marine insurance.<sup>703</sup>

10.53 The onerous duty of disclosure in marine insurance has been justified by reference to the speed with which marine insurance is sometimes effected and the potential range of inquiry.<sup>704</sup> Insurers have expressed the view that the timing of going on risk means that insurers have to be able to rely absolutely on the information disclosed by the insured or their broker.<sup>705</sup> Even with technological advances, the insured in many situations still has access to information not available to the insurers. The difficulty of inspecting ships, as opposed to most other insured property, may be seen to justify more onerous disclosure obligations than are applicable to other insurance.

10.54 In addition, reforming the scope of the duty of disclosure may have implications for the costs of insurance premiums.

Marine insurance may be negotiated over a considerable period of time and given only on condition that a survey is carried out. In those circumstances where the insurer has had the time and opportunity to carry out its own investigations there may not be such a great need for the duty of utmost good faith. However, this is not the norm and furthermore where the insurer has to carry out its own investigations this would no doubt increase the level of insurance premiums.<sup>706</sup>

### ***Insurance Contracts Act 1984 (Cth)***

10.55 One alternative formulation of the duty of disclosure is provided by ICA s 21.

703 T Schoenbaum 'The Duty of Utmost Good Faith in Marine Insurance Law: A Comparative Analysis of American and English Law' (1998) 29(1) *Journal of Maritime Law and Commerce* 1, 3-4.

704 Y Baatz 'Utmost Good Faith in Marine Insurance Contracts' in M Huybrechts E Van Hooydonk & C Dieryck (eds) *Marine Insurance at the Turn of the Millennium* vol I Intersentia Antwerp 1999, 15, 31. *Advisory Committee meeting* Sydney 25 May 2000.

706 Y Baatz 'Utmost Good Faith in Marine Insurance Contracts' in M Huybrechts E Van Hooydonk & C Dieryck (eds) *Marine Insurance at the Turn of the Millennium* vol I Intersentia Antwerp 1999, 15, 31-2.

21(1) Subject to this Act, an insured has a duty to disclose to the insurer, before the relevant contract of insurance is entered into, every matter that is known to the insured, being a matter that:

- (a) the insured knows to be a matter relevant to the decision of the insurer whether to accept the risk and, if so, on what terms; or
- (b) a reasonable person in the circumstances could be expected to know to be a matter so relevant.

10.56 In relation to representations s 26(2) of the ICA states that

26(2) A statement that was made by a person in connection with a proposed contract of insurance shall not be taken to be a misrepresentation unless the person who made the statement knew, or a reasonable person in the circumstances could be expected to have known, that the statement would have been relevant to the decision of the insurer whether to accept the risk and, if so, on what terms.

10.57 This test has been labelled a ‘compromise objective and subjective test’ though it appears to blur the distinction between accuracy and materiality. The objective standard of the existing ‘prudent insurer’ test was abandoned and a ‘reasonable person in the circumstances’ test was introduced.<sup>707</sup> However, the ‘prudent insurer’ test may still have some relevance under ICA s 21(1). It has been suggested in some cases that, in determining what facts known to the insured or a hypothetical reasonable person in the circumstances are ‘relevant’, regard must be had to a prudent insurer acting reasonably.<sup>708</sup>

10.58 The resolution of whether a subjective (the actual insurer) or objective (the prudent insurer) test operates under ICA s 21 remains to be definitively determined. However, the preponderance of case law and commentary now suggests that ‘the insurer’ for the purposes of s 21(1) is the particular insurer.<sup>709</sup> This conclusion is supported by the High Court’s statement in *Advance (NSW) Insurance Agencies Pty Ltd v Matthews*<sup>710</sup> that ICA s 21 was intended to replace the antecedent common law. The fact that ICA s 21A now contains specific provisions dealing with disclosure of matters to the actual insurer (see paragraph 10.59–10.60 below) also tends to suggest that the prudent insurer is no longer an element of the test for disclosure.

707 See ALRC 20 para 182–3.

708 See *Toikan International Insurance Broking v Plasteel Windows Australia Pty Ltd* (1989) 94 ALR 435; *Ayoub v Lombard Insurance Co (Aust) Pty Ltd* (1989) 166 CLR 606.

709 See *Twenty-First Maylux Pty Ltd v Mercantile Mutual Insurance (Aust) Ltd* (1989) 92 ALR 661; *Burns v MMI-CMI Insurance Ltd* (1994) 8 ANZ InsCas ¶61-228; K Sutton ‘An Assured’s Duty of Disclosure’ (1995) 23 *Australian Business Law Review* 225; C McCarthy ‘The “Prudent Insurer”: The Test and its Impact on Section 21’ (1997) 8 *Insurance Law Journal* 125; F Marks and A Balla *Guidebook to Insurance Law in Australia* 3rd ed CCH Sydney 1998, 231–3.

710 (1989) 166 CLR 606, 615 (Mason CJ, Dawson, Toohey, Gaudron JJ); see also ALRC 20 para 183 referring to marketing methods which increase the risk of non-disclosure.

10.59 The ICA provides that where a person has failed to answer or given an obviously incomplete or irrelevant answer to a question included in a proposal form, the insurer is deemed to have waived compliance with the duty of disclosure in relation to the matter.<sup>711</sup> In 1998 the ICA was amended by the introduction of a new s 21A,<sup>712</sup> partly in response to a report by the operators of the General Insurance Enquiries and Complaints Scheme, which concluded that ICA s 21 still placed too onerous a burden on an insured in requiring it to assess what matters are relevant to an insurer's decision to accept the risk.<sup>713</sup>

10.60 Section 21A requires an insurer to pose specific questions to an insured that are relevant to the risk and to request expressly that the insured disclose each 'exceptional circumstance' which is known to the insured, and which the insured knows, or could be expected to know, is a matter relevant to the insurer. Where the insured properly answers these questions the insured is deemed to have complied with the duty of disclosure.<sup>714</sup>

### ***Insurance Act 1902 (NSW)***

10.61 In 1983 the *Insurance Act 1902* (NSW) was amended to reform the law relating to misrepresentations and non-disclosure in relation to general insurance contracts.<sup>715</sup> Section 18A of the Act provides that

- 18A. A contract of insurance ... is not void, voidable or otherwise rendered unenforceable:
- (a) by reason only of a false or misleading statement ... unless the statement was material to the insurer in relation to the contract of insurance and:
    - (i) the statement was fraudulent; or
    - (ii) the insured knew or a reasonable person in the insured's circumstances ought to have known that the statement was material to the insurer in relation to the contract of insurance; or
  - (b) by reason only of an omission of matter from the contract or a proposal, offer or document that led to the entering ... of the contract unless the matter omitted was material to the insurer in relation to the contract of insurance and:
    - (i) the omission was deliberate; or
    - (ii) the insured knew or a reasonable person in the insured's circumstances ought to have known that matter material to the insurer in relation to the contract of insurance had been omitted.

711 ICA s 21(3).

712 *Insurance Laws Amendment Act 1998* (Cth). The new provision came into effect on 1 September 1999.

713 General Insurance Enquiries and Complaints Scheme Ltd 1995 *Annual report* 4–5.

714 Section 21A applies only to new contracts of insurance and not to renewals: ICA s 21A(1).

715 As inconsistent state law under s 109 of the Constitution, these provisions of the NSW legislation do not apply to contracts subject to the ICA.

10.62 This provision, like s 21 of the ICA, relies on the assumed knowledge of a reasonable person in the insured's position of what is material to an insurer, and may be criticised on similar grounds (see paragraph 10.63).

### **New Zealand reform proposals**

10.63 The Law Commission of New Zealand (NZLC) considered reform of the duty of disclosure in 1998.<sup>716</sup> The NZLC did not recommend that provisions similar to s 21 of the ICA be adopted because in its view

- the ICA formulation still results in avoidable uncertainty about the precise extent of an insured's duty of disclosure and
- while the ICA provisions modify the unfairness to an insured of an insurer's current all or nothing remedy, they also introduce the need to make and prove difficult hypothetical and retrospective assessments of an insurer's likely response to an insured having disclosed a matter.<sup>717</sup>

10.64 The NZLC also considered whether the duty of disclosure should be abolished and substituted with an obligation to answer questions correctly.

Does not the insurer's duty of good faith ... require an insurer — by asking appropriate questions of an insured — to notify the insured of the information required to assess accurately a risk to be accepted? Equally, does not an insured's reciprocal duty of good faith require the insured to answer correctly an insurer's questions? If these limits to the duty of good faith are accepted then the law could more simply provide an insurer with a remedy only for any incorrect responses which could constitute misrepresentations.<sup>718</sup>

10.65 However, the NZLC concluded that in effect substituting an obligation to answer questions for the duty to disclose was an inappropriate response to reform because it would interfere unduly with existing commercial practices that make it impractical for insurers to always obtain answers to questions before they take on risk.<sup>719</sup>

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716 Law Commission (NZ) *Some Insurance Law Problems* (Report 46) Law Commission Wellington 1998, 11.

717 *Ibid* 10–11.

718 *Ibid* 11.

719 *Ibid*. The NZLC's recommendations on reform of the duty of disclosure included a provision that the limits on the right of an insurer to cancel a contract of insurance retrospectively for non-disclosure do not apply where 'the insured answers a specific question expressly put by the insurer in a way which is substantially incorrect because of the failure to disclose a fact': 16–17, draft Insurance Law Reform Amendment Act s 7A(2)(c).

### Civil code countries

10.66 While laws of civil code countries have no direct equivalent to the general duty of good faith, rules concerning duties of disclosure are found in the public and private marine insurance legislation of most countries. The way in which the scope of the duty of disclosure is defined varies. At the core of these provisions, as in common law countries, is a duty to disclose material information. However, the definition of materiality differs.<sup>720</sup>

10.67 In Norway, the insured must give full and correct disclosure of all circumstances that would be material to an objective prudent insurer, whether or not the insured has knowledge of the information or knowledge that the information would be material to an insurer.<sup>721</sup>

10.68 In Germany, the scope of the duty is similar, but only applies to information that is known to the insured.<sup>722</sup> In France, the question of materiality is determined by reference to the subjective influence of information on the actual insurer. The insured must disclose all circumstances that might influence the actual insurer in assessing the risk, as far as the insured is aware of this possible influence.<sup>723</sup>

### The implications of *Pan Atlantic*

10.69 In relation to calls for reform of the duty of disclosure in marine insurance law Justice Kirby has observed

It is imperative that an element of causality be introduced into the doctrine. In that respect, the decision of the House of Lords in *Pan Atlantic Insurance* may offer a desirable judicial reform of the pre-existing understanding of the law. It is similarly desirable that the test of materiality should be modified so as to control somewhat the onerous burden which it now presents to the assured who seeks faithfully and

720 Although it appears that in most countries some form of 'decisive influence' test applies: T-L Wilhelmssen 'Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire' in *CMI Yearbook 2000* Comité Maritime International, Antwerp 2000, 332, 351-2. That is, information is material if disclosure would have led to a different decision on accepting or rating the risk.

721 Norwegian Marine Insurance Plan Commentary cl 3-1; *Ibid.* While subjective knowledge of the information has no direct significance to the scope of the duty of disclosure, it is relevant to the nature of the sanction that the insurer may invoke in the event of the breach of the obligation.

722 T-L Wilhelmssen 'Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire' in *CMI Yearbook 2000* Comité Maritime International, Antwerp 2000, 332, 354-5; *Allgemeine Deutsche See-versicherungsbedingungen* (ADS) 19(1).

723 *Ibid* 355; S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' *Ph D thesis* University of Queensland November 1998, 139-40 citing Code des Assurances Art L. 172-19.

honestly to comply with it. However, that modification should not go so far as to encourage an unduly restrictive flow of information between the parties.<sup>724</sup>

10.70 The central question is whether the formulation of the duty settled upon by the House of Lords in *Pan Atlantic* should be embraced in Australia. There has been much critical comment on the implications of the *Pan Atlantic* case. It has been stated that *Pan Atlantic* has failed to clarify the law on non-disclosure.<sup>725</sup> Some commentary also suggests that *Pan Atlantic* may be an undesirable and uncertain basis for restatement of the duty of disclosure.<sup>726</sup> For example, Dr Derrington states

The definition [of materiality] ultimately adopted by the House of Lords in the *Pan Atlantic* case, namely something a prudent insurer would have liked to know about, casts the net so widely as to remove the objective element from the definition. In reality it will be relatively easy to find prudent insurers who will swear that they would have simply liked to have known about a particular fact, regardless of whether or not it ultimately impacted on their underwriting decision.<sup>727</sup>

10.71 Even though *Pan Atlantic* introduced (or confirmed) a subjective requirement for the actual insurer to be induced into entering the contract by the non-disclosure or misrepresentation, in most cases the test may favour insurers, as compared to a decisive influence test of materiality. This is true of any formulation of materiality that requires less than a decisive influence. Howard Bennett observes that, in practice

a finding of materiality gives rise to a fair, although flexible, inference of fact that the actual underwriter was induced (in the decisive influence sense) into the contact which the assured will face an uphill task in rebutting. In consequence, once the insurer proves that the assured made a false statement of fact or failed to disclose a circumstance in presenting the risk, his chances of being able to rescind the contract if he so wishes are extremely strong.<sup>728</sup>

10.72 Others have stated that proving actual inducement need not be a major evidentiary problem for an insured. Reference may be made to the insurer's underwriting guidelines or underwriting files to show what the insurer would have done if the undisclosed circumstance had in fact been disclosed.<sup>729</sup>

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- 724 M Kirby 'Marine Insurance: Is the Doctrine of "Utmost Good Faith" Out of Date?' (1995) 13(1) *Australian Bar Review* 1, 20. The Commission takes Kirby J's reference to 'causality' to refer to the requirement for a causal connection between the misrepresentation or non-disclosure and the making of the contract of insurance (that is, inducement of the insurer).
- 725 S Derrington 'Does the Marine Insurance Act 1909 (Cth) Still Serve the Needs of the Business Community?' (1995) 7(1) *Insurance Law Journal* 31.
- 726 P Griggs 'Is the Doctrine of Utmost Good Faith Out of Date?' *Paper* Marine Insurance Seminar CMI 35th International Conference, Sydney October 1994; H Bennett *The Law of Marine Insurance* Clarendon Oxford 1996, 57-60.
- 727 S Derrington 'The Requirement of Inducement and the Concept of Materiality in Section 24 of the Marine Insurance Act 1909' (2000) 11 *Insurance Law Journal* 236, 256.
- 728 H Bennett *The Law of Marine Insurance* Clarendon Oxford 1996, 59.
- 729 Barrister *Consultation* Perth 22 November 2000.



### Reform of the duty of disclosure and international harmonisation

10.73 Professor Thomas Schoenbaum has observed that a serious divergence has developed between American and English marine insurance law over the issue of disclosure, a divergence accentuated by *Pan Atlantic*.

10.74 American law on this issue appears to require a decisive influence test for both materiality and inducement of the actual insurer.<sup>730</sup> The decisive influence test adopted by US courts applying federal admiralty law requires that, at a minimum, ‘the risk must be increased so as to enhance the premium’.<sup>731</sup> A fact, in order to be material, must be something which would have ‘controlled the underwriter’s decision’.<sup>732</sup>

10.75 Another difference between American and English law is that the test of materiality is an objective test — whether a reasonable person in the insured’s position would know that the fact was material. Virtually all American admiralty cases require inducement of the actual insurer although materiality and inducement are not always distinguished. The rules of materiality under American law also provide that facts that are the subject of a specific inquiry by the insurer are deemed to be material.<sup>733</sup>

10.76 Schoenbaum states that these divergences are a strong indication that basic reforms are needed in English and American law since the marine insurance industry is international in scope, and disharmony on such a key issue is undesirable.<sup>734</sup> In his opinion the MIA (UK) is flawed in producing an unworkable and ambiguous test of materiality and by omitting an inducement requirement.

10.77 He suggests that two factors essential to the early cases on utmost good faith have been ignored in English jurisprudence, with the result that the standard for disclosure has become overly strict. Firstly, there is no need for the duty of disclosure with regard to facts and circumstances not within the special knowledge of the insured. That is, there should be no obligation to disclose matters which can be investigated and discovered independently. Secondly, the duty of disclosure should be subject to a ‘due diligence standard’ so that only negligent misrepresentations or omissions should breach the duty.<sup>735</sup>

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730 See T Schoenbaum ‘The Duty of Utmost Good Faith in Marine Insurance Law: A Comparative Analysis of American and English Law’ (1998) 29(1) *Journal of Maritime Law and Commerce* 1, 25–6.

731 Ibid 25 citing *M’Lanahan v Universal Insurance Company* 26 US (1 Pet) 170 (1828).

732 Ibid.

733 Ibid.

734 Ibid 13–14.

735 Ibid 14.

Overhaul of the 1906 Act is in order on these points, which should also be kept in mind in connection with the drafting of any future American Marine Insurance Act or similar statute in other jurisdictions.<sup>736</sup>

10.78 Dr Derrington states that any domestic reform of the scope of the duty of disclosure should be based on a ‘synthesis of the fundamental principles on which several major marine insurance jurisdictions are agreed’. In this regard she proposes the following formulation of the duty of disclosure.

An insured should be under a duty to give complete and correct information to the insurer regarding all the circumstances pertaining to the risk about which the actual insurer acting reasonably would wish to know in determining whether to accept the risk and if so on what terms.<sup>737</sup>

10.79 This formulation of the duties of the insured does not distinguish between non-disclosure and misrepresentation and does not refer directly to the necessity for the actual insurer to be induced to enter the contract by a non-disclosure. Derrington argues that, on their proper construction, neither the common law nor the MIA make it necessary that the actual insurer be induced by a non-disclosure (as distinct from a misrepresentation).<sup>738</sup>

10.80 Dr Derrington states that her formulation of materiality accords with the current English interpretation of materiality<sup>739</sup> and the similar Norwegian approach<sup>740</sup> and that the ‘more stringent test’ which obtains in French marine insurance law is not necessary in light of the objectivity of the proposed duty.<sup>741</sup> The formulation

does not incorporate any subjective element on the insured’s behalf such as appears in the French system of marine insurance law or in the Insurance Contracts Act 1984 (Cth) and such protection is not necessary in the commercial context of marine insurance.<sup>742</sup>

10.81 The formulation requires that a non-disclosure or misrepresentation be material to the actual insurer, who can, if necessary, be examined in the witness box.

736 Ibid 28–9.

737 S Derrington ‘The Requirement of Inducement and the Concept of Materiality in Section 24 of the Marine Insurance Act 1909’ (2000) 11 *Insurance Law Journal* 236, 258.

738 Ibid 252–3. See also S Derrington ‘The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform’ *Ph D thesis* University of Queensland November 1998, 135–6, 137, 341, Draft provision D1.

739 That is, the first stage of the *Pan Atlantic* test of materiality: see para 10.16–10.19.

740 See para 10.67.

741 See para 10.68.

742 S Derrington ‘The Requirement of Inducement and the Concept of Materiality in Section 24 of the Marine Insurance Act 1909’ (2000) 11 *Insurance Law Journal* 236, 258.

10.82 Dr Derrington also recommends there should be no separate requirement that contracts are *uberrimae fidei* and the insurer should be under a corresponding duty to give complete and correct information to an insured regarding all the circumstances about which the insured acting reasonably would wish to know in determining whether to place the risk with the insurer.<sup>743</sup>

## Conclusions on reform of the scope of the duty of disclosure

10.83 The Commission's research and consultations reveal a wide range of options for reform of the scope of the duty of disclosure. The Discussion Paper presented two options for reform. These were

- Amending the MIA to clarify the scope of the duty of disclosure to expressly state the requirement for the actual insurer to be induced by a non-disclosure or misrepresentation as implied by the majority in *Pan Atlantic* and so that a material non-disclosure or misrepresentation made to a leading underwriter is impliedly made to following underwriters.<sup>744</sup>
- Amending the MIA to be consistent with s 21, s 21A and s 26 of the ICA.<sup>745</sup>

10.84 It would be unattractive to devise yet another test, particularly as there is no consensus as to how it should be worded. It might be better to leave the existing MIA formulation to develop, or to abandon it entirely in favour of the ICA formulation. The only common ground that emerges from consultation is that an obligation of full and accurate disclosure, however described, should be enunciated in the MIA.

10.85 A number of submissions rejected the ICA test.<sup>746</sup> However, there was some support for the ICA test or other, similar formulation that, like the ICA provisions, concentrates on the knowledge of the actual insured rather than on the prudent insurer.<sup>747</sup> Many insurers continue to see strict disclosure requirements as necessary given the high stakes in marine claims.<sup>748</sup> Dr Sarah Derrington has observed that

The Australian general insurance law provisions shift the onus to disclose from the assured and place an onus on the insurer to, in effect, collect the information it considers relevant. The provisions are designed to protect consumers. They are inappropriate in the context of commercial marine insurance. Further, the fact that

743 Ibid 257–8.

744 Draft proposal 9.

745 Draft proposal 10.

746 P Grieve *Submission 6*; K Carruthers *Submission 9*; Insurance Council of Australia *Submission 12*.

747 National Bulk Commodities Group *Submission 14*; A Street *Submission 15*.

748 eg P Grieve *Submission 6*.

they no longer incorporate internationally used principles relating to disclosure and misrepresentation make them unlikely to gain international acceptance.<sup>749</sup>

10.86 The ICA disclosure provisions are designed to protect consumers and, while the Commission is not entirely convinced that the stakes are peculiarly high in marine insurance, the interest in harmonisation with other marine insurance jurisdictions militates against any proposal to adopt the ICA test.

10.87 Some submissions, while critical of aspects of the existing case law, suggest that there is no suitable justification for an amendment.<sup>750</sup> Others favour minor amendments to clarify the existing law as suggested by the Commission in its Discussion Paper.<sup>751</sup>

10.88 There are possible pitfalls in amending the MIA's codification of the duty of disclosure. Re-codifying some elements of the *Pan Atlantic* case, for example by including reference to the actual insurer, might be taken as approval of that decision as a whole, including its test of materiality,<sup>752</sup> rather than that approved by Australian courts.<sup>753</sup> To the extent that such an amendment simply seeks to restate the current law, it may have little benefit and might risk introducing additional uncertainty by divorcing the development of the Australian law on the interpretation of s 24–26 of the MIA from jurisprudence in the other common law countries.

10.89 The Commission has closely examined whether a new formulation of the scope of the duty of disclosure should be attempted. Such an approach may be predicated on the view that the case law relating to the duty of disclosure is not in a satisfactory state and does not provide sufficient certainty for the parties. In Australia, uncertainty about the law arises both from the split in the opinion of the House of Lords in *Pan Atlantic* and because the High Court has yet to confirm that the scope of the duty of disclosure established by the majority in *Pan Atlantic* is the law in Australia.<sup>754</sup> Consultations have confirmed that the duty of disclosure is one area in which reform of the MIA might be welcomed by insurers and brokers as creating additional certainty.

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749 S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' *Ph D thesis* University of Queensland November 1998, 182.

750 Law Society of WA *Submission 7*.

751 K Carruthers *Submission 9*.

752 See para 10.15–10.22.

753 *Advisory Committee meeting* 18 December 2000.

754 Legal practitioners *Consultation* Sydney 1 May 2000.

10.90 The formulation of the duty proposed by Dr Derrington has some attraction (see paragraph 10.78–10.79). The formulation of materiality accords with the current English interpretation of materiality (the first stage of the *Pan Atlantic* test) and the similar Norwegian approach. Importantly, the formulation contains an element of inducement or causation, which most commentators seem to find desirable. Submissions and consultations have revealed strong support for the actual inducement requirement.<sup>755</sup>

10.91 One view expressed was that fairness demands that the insurer be required to give evidence — otherwise the whole onus of proving whether the insurer would still have insured the risk is placed on the insured. Before the actual inducement requirement was developed by the case law, an insurer defending a claim only needed to lead the evidence of an expert witness, whose evidence is more easily tailored to the needs of the defence. This ‘kept the spotlight’ off the actual underwriters and their practices.<sup>756</sup> However, under *Pan Atlantic* it continues to be necessary to call expert evidence directed to the question whether the facts in issue would have an effect on the thought processes of the prudent insurer in weighing up the risks.<sup>757</sup>

10.92 The Derrington formulation would be an incremental change in an international legal environment in which there are different variants of the duty. One disadvantage of such a reform is that it would leave Australia with a unique test for disclosure in general insurance and a different unique test for disclosure in marine insurance. However, against a background of varying formulations in other countries reform would not set Australia adrift from any consistent international norm.

10.93 The Commission has concluded that the MIA should include a positive duty on the part of the insured to disclose accurately all that it knows to be material, or that a reasonable person in the same circumstances would know to be material. The range of circumstances that must be disclosed is limited to those that a reasonable insured would understand to be material, reflecting ICA s 21. The standard of disclosure required by amended MIA s 24(1) and 26(1) is essentially objective in that it is governed by the knowledge of a reasonable person in the insured’s position. It also has a subjective element, however: the insured must disclose what it actually knows to be material.

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755 K Carruthers *Submission 9; Advisory Committee meeting* Sydney 25 May 2000.

756 *Advisory Committee meeting* Sydney 25 May 2000.

757 See P Griggs ‘Is the Doctrine of Utmost Good Faith Out of Date?’ *Paper* Marine Insurance Seminar CMI 35th International Conference Sydney October 1994 referring to *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd* [1995] 1 AC 501, 531 (Lord Mustill).

10.94 Sections 24(1) and 26(1) should be further amended by deleting the last sentences in each, which deal with the insurer's right to avoid, as the remedies for breach are dealt with in a new section discussed below.<sup>758</sup> The exclusions in s 24(3) should be retained with one textual change that arises from the abolition of the concept of warranties (see paragraph 9.129).

10.95 The definition of materiality in MIA s 24(2) and 26(2) should not be amended to allow the common law to develop. The Commission is apprehensive that another formula of words imposed by statute would reduce a court's flexibility and may simply serve to add a further unhelpful phrase without adding clarity.

10.96 The agent's obligation in MIA s 25(a) should be modified to reflect the changes to s 24(1) so that it is bound to disclose what it knows to be material and what a reasonable agent in the circumstances could be expected to know to be material. In addition, the agent's obligation should be modified so that it no longer has to disclose what should have been communicated to it but was not.

10.97 The element of inducement should be introduced, not as an element of materiality, but as a condition that must be satisfied by the insurer before it is entitled to relief (except in the case of fraud). Materiality should remain primarily an objective concept based on the knowledge of the reasonable insured and the effect on a prudent insurer. In the Commission's view, what is material is determined by the overall objective context in which the insurance is proposed, considered and negotiated. Whether any particular circumstance is of such significance that, as represented, it induced the insurer to enter into the contract (or to do so on particular terms) or, if disclosed, would have induced it to decline to do so (or to amend its terms), cannot be assessed any earlier than the point at which the contract is concluded. Although an insured can be required to act reasonably in assessing and disclosing what is material, it cannot determine what will in fact induce the insurer to act. The Commission prefers, therefore, to separate objective materiality from subjective inducement and to deal with inducement as an element of the insurer's right to relief.

## **Remedies for breach of the duty of disclosure**

10.98 The present law is that if an insurer is induced to enter a contract by an insured's non-disclosure of material information or material misrepresentation, the insurer may completely avoid or rescind the contract.

10.99 A trivial non-disclosure may result in the insurer avoiding liability and a substantial loss for the insured. The consequence of an innocent non-disclosure is

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<sup>758</sup> See para 10.120.

the same as for a wilful misrepresentation since rescission is the only remedy (although if the misrepresentation or non-disclosure is fraudulent the premium is not returnable).<sup>759</sup>

10.100 Reform of the law concerning disclosure could introduce more flexible remedies appropriate to the measure of fault of the party in breach.<sup>760</sup>

The right to avoid the contract is an extremely draconian remedy. It does not, in any way, depend on fault of the party in breach of the duty ... Thus the marine insurance contract differs from the commercial contract in that first there is an obligation to disclose material facts prior to the conclusion of the contract. Secondly, unlike the law in relation to misrepresentation, where the misrepresentee's remedies will depend on whether the misrepresentation was made fraudulently, negligently, or innocently, the remedy for non-disclosure is always rescission.<sup>761</sup>

10.101 Rescission of the contract may be an appropriate remedy for insurers but is not likely to be a practical remedy for an insured who has suffered loss because of non-disclosure or misrepresentation on the part of the insurer.<sup>762</sup> For example, in *Banque Financiere de la Cite SA v Westgate Insurance Co Ltd*,<sup>763</sup> prior to the formation of the contract the insurer knew of a circumstance which would prevent the insured from recovering under the terms of the policy but failed to disclose this fact. In such a situation the insured may rescind and recover the premium but will not be indemnified for a loss which would have been avoided or covered if the insurer had disclosed the information. Breach of the duty of disclosure does not sound in damages,<sup>764</sup> which are generally available only if a contractual or tortious obligation has been breached.

## Reform of remedies for breach of the duty of disclosure

10.102 Justice Kirby has stated that

consideration needs to be given to the evolution of a system of remedies for non-disclosure whereby certain types of non-disclosure will not automatically entitle the insurer to avoid the contract entirely. This has been achieved in Australia in the field of general insurance. A like reform should be considered in the international business

759 MIA s 90(3) provides that 'where the policy is void, or is avoided by the insurer as from the commencement of the risk, the premium is returnable, provided that there has been no fraud or illegality on the part of the assured'.

760 Y Baatz 'Utmost Good Faith in Marine Insurance Contracts' in M Huybrechts E Van Hooydonk & C Dieryck (eds) *Marine Insurance at the Turn of the Millennium* vol I Intersentia Antwerp 1999, 15, 32.

761 Ibid 25.

762 Except perhaps where an insurer agrees to cover a ship for a voyage which the insurer knows already has been safely completed, allowing the insured to recover the premium. In other situations the remedy of rescission is likely to be wholly inadequate.

763 [1991] 2 AC 249.

764 Ibid 280 (Lord Templeman), 281 (Lord Jauncey).

of marine insurance but the lead will have to come from those countries which are most heavily involved in writing marine insurance.<sup>765</sup>

### ***Insurance Contracts Act 1984***

10.103 The ICA has significantly reformed the law relating to remedies for non-disclosure or misrepresentation in the context of non-marine and pleasure craft insurance.

10.104 Section 28 of the ICA provides as follows

(1) This section applies where the person who became the insured under a contract of general insurance upon the contract being entered into:

(a) failed to comply with the duty of disclosure; or

(b) made a misrepresentation to the insurer before the contract was entered into;

but does not apply where the insurer would have entered into the contract, for the same premium and on the same terms and conditions, even if the insured had not failed to comply with the duty of disclosure or had not made the misrepresentation before the contract was entered into.

(2) If the failure was fraudulent or the misrepresentation was made fraudulently, the insurer may avoid the contract.

(3) If the insurer is not entitled to avoid the contract or, being entitled to avoid the contract (whether under subsection (2) or otherwise) has not done so, the liability of the insurer in respect of a claim is reduced to the amount that would place the insurer in a position in which the insurer would have been if the failure had not occurred or the misrepresentation had not been made.

10.105 Under ICA s 28, the insurer may avoid the contract from its inception only where the non-disclosure or misrepresentation was fraudulent.<sup>766</sup> If the insurer is not entitled to avoid the contract, the liability of the insurer in respect of a claim is reduced to the amount that would place the insurer in a position in which the insurer would have been if the failure had not occurred or the misrepresentation had not been made.

10.106 Applying ICA s 28(3) involves a number of evidentiary complications, including ascertaining whether the actual insurer would have entered into the contract and if so, on what terms, had there been no misrepresentation or failure to disclose.

What will matter will be the particular underwriting philosophy of the insurer at the particular time at which the failure to disclose or the misrepresentation occurred. This may involve an underwriter in giving appropriate evidence before a court and that

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765 M Kirby 'Marine Insurance: Is the Doctrine of "Utmost Good Faith" Out of Date?' (1995) 13(1) *Australian Bar Review* 1, 20.

766 The insurer may refuse payment of a fraudulent claim but may not avoid the policy, and the court has the power to order part-payment of the claim if only a minimal or insignificant amount of the claim is made fraudulently: ICA s 56.



evidence would, of course be open to attack by way of cross-examination. The existence of firm underwriting guidelines and procedures in written form would, of course, assist in the giving of any such evidence.<sup>767</sup>

10.107 There has been some doubt over whether ICA s 28(3) permits an insurer to reduce its liability to nil in circumstances where it is able to establish that, were it not for the insured's failure to comply with its duty of disclosure, it would not have accepted the proposal at all. However, several decisions of state supreme courts have proceeded on the basis that an insurer may reduce its liability to nil<sup>768</sup> and in *Unity Insurance v Rocco Pezzano*<sup>769</sup> litigation before the High Court was conducted on this assumption. While the decision in that case rested on other issues, Kirby J referred to the decision in *Ferrcom Pty Ltd v Commercial Union Assurance Co of Australia Ltd*,<sup>770</sup> which confirmed that the insurer could reduce its liability to nil under ICA s 54 and stated that the same principles appear to apply under s 28(3).<sup>771</sup>

### New Zealand proposals

10.108 The New Zealand Law Commission has recommended placing time limits on the rights of insurers, including marine insurers, to cancel a contract of insurance retrospectively. The limits do not apply where the failure to disclose a fact is 'blameworthy'. A failure to disclose a fact would not be blameworthy unless the insured knew, or in the circumstances a reasonable person could have been expected to know, both the undisclosed fact and that disclosure of the undisclosed fact would have influenced the judgment of a prudent insurer in accepting the risk or the terms of such acceptance.<sup>772</sup>

### Civil code countries

10.109 Marine insurance law and practice in civil code countries provide alternative approaches to remedies for non-disclosure. In France, if the insured has acted in bad faith or is guilty of an intentional non-disclosure or misrepresentation the *Code des Assurances* provides for avoidance of the contract when that non-

<sup>767</sup> F Marks and A Balla *Guidebook to Insurance Law in Australia* 3rd ed CCH Sydney 1998, 253.

<sup>768</sup> See eg *Ayoub v Lombard Insurance Co (Australian) Ltd* (1989) 166 CLR 606, 621–2; *Twenty-First Maylux Pty Ltd v Mercantile Mutual Insurance (Aust) Ltd* [1990] VR 919, 927–8; *Orb Holdings Pty Ltd v Lombard Insurance Co (Australian) Ltd* [1995] 2 Qd R 51, 52 and other cases cited in *Unity Insurance v Rocco Pezzano* (1998) 192 CLR 603, 636 (Kirby J), 648 (Hayne J).

<sup>769</sup> (1998) 192 CLR 603.

<sup>770</sup> (1993) 176 CLR 332.

<sup>771</sup> (1998) 192 CLR 603, 636. See also 613 (McHugh J) 620 (Gummow J) 651 (Hayne J).

<sup>772</sup> Law Commission (NZ) *Some Insurance Law Problems* (Report 46) Law Commission Wellington 1998, 16–17, draft Insurance Law Reform Amendment Act s 7A(2)(c). Any right an insurer might have to cancel a contract prospectively is unaffected by the recommendation. New Zealand has already reformed the law with respect to remedies for breach of warranty and misstatements including in relation to contracts of marine insurance. See Insurance Law Reform Act 1977 (NZ) s 5–7, s 11.

disclosure or misrepresentation has changed the object of the risk or has diminished the insurer's opinion of the risk, whether or not the non-disclosure is causative of the loss. Where the insured demonstrates good faith and where the insurer would have accepted the insurance but asked for a higher premium, the insurer remains liable but a 'proportionality' approach is used to assess the extent of that liability.<sup>773</sup> Using this method the insurer is liable to pay a proportion of the claim calculated according to the difference between the premium that would have been charged if all the facts had been known and the premium actually charged.

10.110 The proportionality approach is not favoured by commentators from common law countries.<sup>774</sup> The first criticism of the proportionality approach is that there is no real deterrent to providing incomplete or inaccurate information. Risks could become harder to determine and insurers would probably be forced to charge higher premiums for all risks. Secondly, it is a difficult and time-consuming task to determine the figure to be used.

Proportioning the recovery to the insurance that could have been bought for the premium paid with full disclosure has a splendid equitable ring to it, but presents serious practical problems that give it limited appeal. It would be workable where risks are rated according to manuals or settled company practices and where the undisclosed fact moves the risk into another rated category. Companies selling many yacht policies probably have rating schemes that would lend themselves to this practice, if, for instance, the undisclosed fact were that the yacht was sometimes raced or used commercially or beyond the stated waters.<sup>775</sup>

10.111 Finally, litigation may increase under this system as there would be incentives to sue to determine the proportional amount due.<sup>776</sup> These criticisms

773 Code des Assurances Article L.172-2(1) cited in S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' *Ph D thesis* University of Queensland November 1998, 199–200; see also T-L Wilhelmsen 'The Marine Insurance System in Civil Law Countries — Status and Problems' *Paper* Marine Insurance Symposium Oslo June 1998; J-S Rohart 'The Doctrine of "Utmost Good Faith" in the Marine Insurance Law of Some Civil Law Countries' *Paper* Marine Insurance Seminar CMI 35th International Conference, Sydney October 1994.

774 Including the Commission: see ALRC 20 para 189–90. Derrington has observed that despite 'professing denunciation of the proportionality principle' in ALRC 20, elements of the principle were incorporated by the Commission in draft provisions that became s 28 of the ICA: S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' *Ph D thesis* University of Queensland November 1998, 196–7.

775 G Staring and G Waddell 'Marine Insurance' (1999) 73 *Tulane Law Review* 1619, 1661. The same might well apply to motor vehicle insurance. In Australia, pleasure craft are covered by the ICA: ICA s 9A.

776 See T Schoenbaum 'The Duty of Utmost Good Faith in Marine Insurance Law: A Comparative Analysis of American and English Law' (1998) 29(1) *Journal of Maritime Law and Commerce* 1, 35–6. However, it has been noted that Anglo-Australian law may also contribute to litigation. The consequences of non-disclosure can often be out of all proportion to the offence. For obvious reasons this 'all or nothing' consequence of non-disclosure has resulted in numerous court cases over the years — the stakes can be high and there is no obvious middle course available to avoid the need for trial: P Griggs 'Is the Doctrine of Utmost Good Faith Out of Date?' *Paper* Marine Insurance Seminar CMI 35th International Conference, Sydney October 1994.

were echoed in a submission to this inquiry.<sup>777</sup> The Commission has been told that even in France the proportionality approach is not used in marine insurance context because of practical difficulties where there are no set premium rates.<sup>778</sup>

10.112 In most other civil code countries, the insurer's rights in the event of non-disclosure or misrepresentation vary according to the gravity of the fault of the insured, although not necessarily by adopting the French approach.<sup>779</sup> For example, in Norway, if the non-disclosure or misrepresentation is fraudulent the insurer is relieved of liability regardless of whether the non-disclosure or misrepresentation was relevant to acceptance of the risk. Where fraud is not involved, the proposition is that the insurer should be put in the same position as it would have been were the insurer given the correct information before entering the contract. If the insurer would not have accepted the risk the contract is not binding and liability may be avoided. If the insurer would have accepted the risk but on different conditions, the insurer may avoid liability where there is a causal connection between the loss and the matter that should have been disclosed. If no causal connection is established the insurer is liable for the loss but may terminate the contract on 14 days' notice.<sup>780</sup>

### Other options

10.113 In her 1998 thesis<sup>781</sup> Dr Derrington has suggested that an insurer's remedies where an insured has failed negligently or innocently to fulfil the duty of disclosure should differentiate between situations where the insurer

- would not have entered into the contract had it known of the matter which was not disclosed and
- would have entered into the contract but only on other conditions.

10.114 In the first situation, Dr Derrington states that the contract should not be binding on the insurer and the premium should be forfeited to the insurer. In the latter situation, the insurer should be liable only to the extent that it is proved that the loss is not attributable to the undisclosed circumstance, should be able to demand an additional premium for the time that the insurer has borne the increased

<sup>777</sup> Law Society of WA *Submission 7*.

<sup>778</sup> *Marine insurance seminar* Phillips Fox Sydney 20 February 2001.

<sup>779</sup> See summary in T-L Wilhelmsen 'Duty of Disclosure, Duty of Good Faith, Alteration of Risk and Warranties: An Analysis of the Replies to the CMI Questionnaire' in *CMI Yearbook 2000* Comité Maritime International, Antwerp 2000, 332, 357–69.

<sup>780</sup> Norwegian Marine Insurance Plan cl 3-2, cl 3-6; S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' *Ph D thesis* University of Queensland November 1998, 202–15.

<sup>781</sup> S Derrington 'The Law Relating to Non-disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' *Ph D thesis* University of Queensland November 1998.

risk, and should be able to terminate the contract on giving the insured 14 days' notice in writing.<sup>782</sup>

This approach accords with the Norwegian approach and introduces the requirement of causation. It avoids the difficulties with the application of the "proportionality principle" as provided for in the French system and protects an assured from loss of cover for irrelevant breaches of the duty of disclosure.<sup>783</sup>

10.115 In Australia, some brokers negotiate the inclusion in marine insurance contracts of an 'errors and omissions' clause. One example of such a clause reads as follows.

The Assured shall not be prejudiced by any unintentional or inadvertent error, omission, non-disclosure or misrepresentation, however it is agreed as between the Assured and the Underwriter, that the Underwriter's liability in respect of a claim may be reduced to an amount that would place the underwriter in a position in which the Underwriter would have been if the error, omission, non disclosure or misrepresentation had not been made.<sup>784</sup>

10.116 This clause prevents the insurer from avoiding the contract where there has been 'unintentional or inadvertent' non-disclosure or misrepresentation, incorporating into the contract elements of the ICA s 28 approach to remedies for non-disclosure.

10.117 One shortcoming of any differentiation of remedies based on the insured's state of mind is that it fails to recognise that the impact on an insurer, even a prudent one, of any non-disclosure or misrepresentation will be determined by the nature and extent of that error, not by the insured's attitude. Although the Commission accepts that a fraudulent insured should be punished by a complete avoidance of the policy with no return of premium, whether the insured was negligent, even grossly so, or simply mistaken will not vary the effect on the insurer. If, however, there is some differentiation of remedies based on the insurer's response if there had been complete and accurate disclosure, there would in many cases be some indirect relief for insureds, for example where the error only had an impact on the levels of premium, deductible or excess.

## **Conclusions on reform of remedies for breach of the duty of disclosure**

10.118 In the Discussion Paper the Commission proposed that the MIA should be amended to restrict the right of an insurer to avoid contracts of insurance

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782 Ibid 335–6, draft provision D3.

783 Ibid.

784 Material provided by broker: *Broker Consultation* Perth 23 November 2000.

retrospectively where there has been any breach of the insured's duty of disclosure or any misrepresentation made by the insured.<sup>785</sup> The Commission asked whether such a reform should make the MIA consistent with the ICA or use some other formulation of the available remedies for breach of the duty of disclosure.<sup>786</sup> In general, submissions supported the proposition that the MIA should be amended in this regard.<sup>787</sup> However, there was no clear view on the form such an amendment should take.<sup>788</sup>

10.119 The Commission has concluded that ICA s 28 does not provide an adequate basis for reform of the remedies under the MIA. In particular, where loss is related to the undisclosed or misrepresented circumstance, the insurer should be entitled to avoid liability for that loss though not under the contract as a whole. A new formulation of the remedies is required.

10.120 The Commission's recommended amendments (see recommendations 22-27) adapts some elements of a formulation proposed in a submission by Dr Derrington of the Centre for Maritime Law, University of Queensland.<sup>789</sup> It is based on the following conclusions.

- The remedies should be limited in that the contract may not provide for any remedies more favourable to the insurer than those provided by the amended MIA.
- If a breach of s 24, 25 or 26 is fraudulent, the insurer should retain its right to avoid the contract from the outset. No premium is returnable by virtue of s 90(3)(a).

<sup>785</sup> ALRC DP 63 draft proposal 11.

<sup>786</sup> One option canvassed in the context of post-formation duties, but not specifically in the context of the duty of disclosure, was that of amending the MIA to make damages available for a breach of duty: ALRC DP 63 draft proposal 12, question 32. This question is examined in detail below (see para 10.143–10.150). The Commission recommends the MIA be amended so there is implied in a contract of marine insurance a provision requiring each party to act towards the other party with utmost good faith, making damages available for breach of post-formation duties (see recommendation 20). At least in theory remedies for breach of the duty of disclosure could also be left to be determined by the courts based on ordinary contractual principles. However, this option has been rejected. The duty of disclosure is, in practice, the most significant and frequently litigated element of the doctrine of utmost good faith and in the interests of certainty should be addressed separately.

<sup>787</sup> K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*; MLAANZ *Submission 12*; National Bulk Commodities Group *Submission 14*; A Street *Submission 15*.

<sup>788</sup> Justice Carruthers stated that a reform based on the provisions of the *Insurance Act 1902* (NSW) s 18A is the most satisfactory solution: K Carruthers *Submission 9*. MLAANZ stated that an element of causation should be introduced – ie the insurer should only be entitled to avoid the contract for breach of the duty of disclosure where the insured's non-disclosure or misrepresentation caused the insurer to enter the contract. MLAANZ also emphasised that any amendment should be consistent with the ICA: MLAANZ *Submission 12*.

<sup>789</sup> S Derrington *Submission 13*. Phil Grieve stated that Dr Derrington's proposals, as described in ALRC DP 63 para 6.82–3 had 'considerable merit': P Grieve *Submission 6*.

- If the breach is not fraudulent and the insurer proves that it would not have entered into the contract at all, it is entitled to avoid the contract but the premium must be returned. The wording of the proposed s 26A(3) makes it clear that the insurer bears the onus of proving inducement and will therefore have to give evidence. This also applies to the following paragraph.
- If the breach is not fraudulent and the insurer proves that it would have written the contract on different terms, the insurer remains on risk but is not liable to indemnify the insured for any loss proximately caused by the undisclosed or misrepresented circumstance. The insurer may also reduce any liability it does have to the insured to reflect any additional premium, deductible or excess that would have been charged and may avail itself of the new statutory right of cancellation.<sup>790</sup> This is consistent with ICA s 60(1).
- A new s 26C should provide that a contract of marine insurance may not impose a duty of pre-contractual disclosure greater than that imposed by the MIA, though without limiting the generality of the obligations of utmost good faith. This reflects ICA s 33.
- Finally, following underwriters should be deemed to have been induced to enter into the contract if all the leading underwriters were induced. For this purpose, leading underwriters should be defined to be those underwriters whose earlier acceptance of part of the risk induced the following underwriter to do so as well.

### **Post-contractual duties of utmost good faith**

10.121 While it is clear that the obligations in s 24 and 26 do not extend after the contract of insurance is concluded, s 23 casts the doctrine of utmost good faith in sufficiently general terms to support continuation of the duty of disclosure beyond formation of the contract.<sup>791</sup> Section 25 does not contain the same express restriction but must, in the Commission's view, be read in the light of the temporal restriction placed on the insured's obligation in s 24.

10.122 There has been debate over the precise legal nature of the doctrine of utmost good faith and in particular whether post-formation duties should be treated as implied terms of the contract of insurance or as derived solely from s 23 of the MIA and the common law doctrine behind it. Unlike the ICA (see paragraph

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790 See para 9.225–9.228.

791 See para 10.3.

10.144), the MIA does not specify that the duty is an implied term and there is debate over how it is to be categorised.<sup>792</sup>

10.123 The point is important because breach of s 23 may permit the insurer to rescind the contract, retrospectively avoiding all liability, including liability for all outstanding claims on the policy, whether such claims arose before or after the breach. As s 23 does not cover post-formation breach of utmost good faith the insurer's remedies are limited. So are the remedies of the insured.

10.124 While it seems clear that rescission is currently the only remedy for breach of the pre-contractual duty of disclosure in marine insurance there remains doubt whether it is also the only remedy for breach of utmost good faith generally.

[U]tmost good faith extends into the life of the contract and includes matters pertinent to claims in respect of which avoidance as a remedy fits awkwardly. If utmost good faith is an implied term of the contract, then damages for breach is an appropriate remedy. If rescission is the only remedy because the duty is not an implied term of the contract, then it is both too narrow and too wide. It is too wide because the breach, if by an insured, may relate to only one claim and the insured would then be deprived of all other entitlements under the policy. If the breach is that of the insurer the remedy is too narrow because avoidance of the policy and loss of its benefits is of no use to the insured if it has already incurred a loss.<sup>793</sup>

10.125 Howard Bennett has argued that post-formation duties of utmost good faith fall outside s 23. Instead,

each duty within the post-formation doctrine may be the subject of a separate contractual term implied by law, the precise properties of which may be moulded by the courts as appropriate to the duty in question.<sup>794</sup>

10.126 In Australia, Scott Henschcliffe has argued that there is no reason in policy or principle for the view that a breach of the post-formation duty of utmost good faith should permit retrospective avoidance of the contract.<sup>795</sup> Henschcliffe notes that there is an absence of Australian case law on the point and argues that this strongly suggests that the draconian remedy of avoidance *ab initio* is unavailable and unnecessary, and that authorities which suggest that the making of a fraudulent claim, or a breach of the post-formation duty of good faith, should allow an insurer to avoid the insurance contract *ab initio* are wrong, and cannot be legally or

792 N Rein 'Utmost Good Faith in Marine Insurance' (1999) 10 *Insurance Law Journal* 145, 165.

793 Ibid 164–5.

794 H Bennett 'Mapping the Doctrine of Utmost Good Faith in Insurance Contract Law' [1999] *Lloyd's Maritime and Commercial Law Quarterly* 165, 221–2.

795 S Henschcliffe 'Insurance Claims: Fraud and the Duty of Good Faith' (1997) 8 *Insurance Law Journal* 210, 228.

rationally justified.<sup>796</sup> He concludes that ‘a re-examination by the courts of the common law remedies in this area is clearly overdue’.<sup>797</sup>

10.127 There is some Australian authority suggesting that post-formation duties of utmost good faith have a different basis from pre-contractual duties. For example, in *NSW Medical Defence Union v Transport Industries Insurance*<sup>798</sup> Rogers J considered that while pre-contractual utmost good faith (disclosure and absence of misrepresentation) should be treated as an ‘incident of the relationship’, post-formation utmost good faith is an implied term of the contract, provided that there is a contractual duty ‘to which the duty of good faith can attach’.<sup>799</sup>

10.128 Post-formation duties of utmost good faith were recently examined by the House of Lords in *The Star Sea*.<sup>800</sup> Both parties accepted the conclusion of the English Court of Appeal in *Banque Financiere de la Cite SA v Westgate Insurance Co Ltd*<sup>801</sup> that there is no remedy in damages for breach of good faith (see paragraph 10.101). The case was conducted on the basis that good faith was not an implied term of the contract but a principle of law under which the sole remedy is a right to avoid the contract of insurance retrospectively. However, the current law was strongly criticised in the judgments. Lord Hobhouse noted that the right to avoid

is appropriate where the cause, the want of good faith, has preceded and been material to the making of the contract. But, where the want of good faith first occurs later, it becomes anomalous and disproportionate that it should be so categorised and entitle the aggrieved party to such an outcome ... The result is effectively penal. Where a fully enforceable contract has been entered into insuring the assured, say, for a period of a year, the premium has been paid, a claim for a loss covered by the insurance has arisen and been paid, but later, towards the end of the period, the assured fails in some respect fully to discharge his duty of complete good faith, the insurer is able not only to treat himself as discharged from further liability but can also undo all that has perfectly properly gone before. This cannot be reconciled with principle. No principle of this breadth is supported by any authority whether before or after the Act.<sup>802</sup>

796 Ibid 221. Henchcliffe notes that the strongest dictum supporting the view that avoidance *ab initio* is available as a remedy appears in a case where that right was a term of the policy: *Moraitis v Harvey Trinder (Queensland) Pty Ltd* [1969] Qd R 226. Other cases generally refer only to ‘avoiding’ the policy and are therefore equivocal as to whether the avoidance remedy is retrospective or prospective only: Ibid. See also ALRC 20 para 243.

797 S Henchcliffe ‘Insurance claims: Fraud and the duty of good faith’ (1997) 8 *Insurance Law Journal* 210, 228.

798 (1985) 4 NSWLR 107.

799 Ibid 112. See N Rein ‘Utmost Good Faith in Marine Insurance’ (1999) 10 *Insurance Law Journal* 145, 151–2.

800 *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] 1 All ER 743.

801 [1991] 2 AC 249.

802 *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] 1 All ER 743, 760.



10.129 Lord Hobhouse stated that a more coherent scheme could be achieved by distinguishing the nature of pre-contractual and post-contractual duties of good faith.

The former derives from requirements of the law which preexist the contract and are not created by it although they only become material because a contract has been entered into. The remedy is the right to elect to avoid the contract. The latter can derive from express or implied terms of the contract; it would be a contractual obligation arising from the contract and the remedies are the contractual remedies provided by the law of contract. This is no doubt why judges have on a number of occasions been led to attribute the post-contract application of the principle of good faith to an implied term.<sup>803</sup>

10.130 In the event, the court found that there had been no breach of the duty of utmost good faith, so it was unnecessary to rule on whether the principle of good faith should be attributed any of the characteristics of an implied contractual term.<sup>804</sup>

### The post-contractual duty of disclosure

10.131 The decision in *The Star Sea* has helped to clarify the scope of the post-contractual duty of good faith in relation to disclosure. The courts rejected the argument that the duty of disclosure continues throughout the contractual relationship with the same content and consequences. Lord Clyde stated

In my view the idea of good faith in the context of insurance contracts reflects the degrees of openness required of the parties in the various stages of their relationship. It is not an absolute. The substance of the obligation which is entailed can vary according to the context in which the matter comes to be judged. It is reasonable to expect a very high degree of openness at the stage of the formation of the contract, but there is no justification for requiring that degree necessarily to continue once the contract has been made.<sup>805</sup>

10.132 The judges clearly indicated that the content of the post-formation duty of disclosure was not co-extensive with the pre-contractual duty of disclosure. Lord Scott held that a post-formation non-disclosure would only amount to breach of good faith where there was fraud or dishonesty.

I would, however, limit the duty owed by an insured in relation to a claim to a duty of honesty. If the duty derives from section 17 [MIA s 23], nonetheless this limitation

803 Ibid 761.

804 However, Lord Hobhouse specifically stated that the judgment of Hirst J in *Black King Shipping Corp v Massie (The Litsion Pride)* [1985] 1 Lloyd's Rep 437 should no longer be treated as a sound statement of the law '[i]n so far as it decouples the obligation of good faith both from s 17 and the remedy of avoidance and from the contractual principles which would apply to a breach of contract'. See ALRC DP 63 para 6.90.

805 *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] 1 All ER 743, 748–9.

does not, in my opinion involve a judicial re-writing of section 17. On the contrary, it would be the creation out of section 17 of a duty that could be broken notwithstanding that the assured had acted throughout in good faith that would constitute a re-writing of the section. Unless the assured has acted in bad faith he cannot, in my opinion, be in breach of a duty of good faith, utmost or otherwise.<sup>806</sup>

10.133 The Commission's recommendations in relation to warranties have been motivated in part by a desire to see that all important terms of a contract of marine insurance are expressed in the contractual documents. Generally, the insured's obligations once the contract has been concluded should appear on the face of the contract or be governed by the overriding obligations of utmost good faith.

10.134 The Commission does not recommend introducing into the MIA any statutory requirement that the insured inform the insurer of any changes to the risk<sup>807</sup> or relating to post-contractual disclosure. There are no such express requirements at present in either the MIA or the ICA and such a reform would, therefore, represent a departure from Australian insurance law in other areas. Furthermore, any such requirement leads to a debate about the insured's requisite state of mind both in relation to the existence of the changed circumstances and the effect that this might or would have on a prudent as well as the actual insurer.

10.135 The parties should be at liberty to insert an express term dealing with post-contractual disclosure, presumably at the insurer's insistence. Any breach of such a term would be caught by the Commission's other recommendations concerning post-contractual breach.<sup>808</sup> The insurer's remedies in any such case would then depend on the causal link, if any, between the changed circumstances, the failure to disclose and the loss sustained. Alternatively, a breach might be caught by the Commission's recommendations concerning a re-statement of the duty of utmost good faith as an implied contractual term (see paragraph 10.143).

10.136 The Commission has concluded that, in order to remove any uncertainty as to whether there is any post-contractual duty of disclosure, the MIA should be amended to include a provision modelled on ICA s 12 stipulating that there is no duty of pre-contractual disclosure other than that imposed by the MIA itself (see paragraph 10.120 above and recommendation 26 below). This would also prevent an insurer imposing such a duty contractually. However, the MIA should for the sake of clarity expressly permit an express term in the contract dealing with post-contractual disclosure. The remedies for breach of such a term should be those that would apply to breach of utmost good faith (if applicable in the circumstances) or breach of any express term: the insurer would not be liable to indemnify the insured for any loss proximately caused by the breach.

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806 Ibid 779.

807 eg as under the civil code concept of alteration of risk: see para 9.45–9.46.

808 See para 9.129 and rec 7.

### Breach of utmost good faith and variation of the contract

10.137 Cases involving breach of the post-formation duty of utmost good faith often arise where the insured is making a claim or has sought to alter or vary the contract of insurance; for example, pursuant to a ‘held covered’ clause.<sup>809</sup> The question then arises whether the breach avoids only the additional cover or the claim or avoids the whole policy.

10.138 The consequences for the parties are of critical importance. For example, in *The Star Sea*<sup>810</sup> the underwriters could have argued that, if there had been a breach of the duty of utmost good faith, not only was the claim avoided but also the whole policy covering some 32 other ships in the same beneficial ownership or management, and many otherwise valid claims.<sup>811</sup> The Court of Appeal intimated that, since inducement of the actual underwriter is necessary, the insurer’s remedy for non-disclosure of facts material to the variation in cover is avoidance of the amended cover, not of the entire contract.<sup>812</sup> Commentators tend to agree with the view that, at least in the absence of fraud, avoidance of the amendment to the contract is all that should be permitted.<sup>813</sup> The Commission agrees with this construction but does not consider it necessary or appropriate to amend the MIA accordingly.

### The duration of the duty

10.139 Another question relating to the post-formation duty of utmost good faith is when the duty ceases to operate. It is not clear under the MIA (or the ICA) whether or not the duty of good faith continues after the insurer rejects a claim.<sup>814</sup> In *Horbelt v SGIC*,<sup>815</sup> in the Supreme Court of South Australia, Justice Bollen held that

809 A ‘held covered’ clause typically provides that in the event of an alteration of specified risks the insurer’s liability is not prospectively discharged. Instead, the insured remains (‘is held’) covered provided that there is notification of the event to the insurer and agreement on additional premium or changes of terms: H Bennett *The Law of Marine Insurance* Clarendon Oxford 1996, 309.

810 *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [1997] 1 Lloyd’s Rep 360.

811 However, in the House of Lords proceedings, counsel advised that ‘nothing turns upon whether the claim is wholly forfeit or the whole policy is treated as forfeit as well’: *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] 1 All ER 743, 766.

812 The judgments in the House of Lords do not deal with this issue, beyond suggesting that at least where there is fraud the whole policy should be avoided *ab initio*: *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] 1 All ER 743, 766–7.

813 H Bennett ‘Mapping the Doctrine of Utmost Good Faith in Insurance Contract Law’ [1999] *Lloyd’s Maritime and Commercial Law Quarterly* 165, 205. See also Y Baatz ‘Utmost Good Faith in Marine Insurance Contracts’ in M Huybrechts E Van Hooydonk & C Dieryck (eds) *Marine Insurance at the Turn of the Millennium* vol I Intersentia Antwerp 1999, 15, 27–8 citing N Legh-Jones *MacGillivray on Insurance Law* 9th ed Sweet and Maxwell 1997, 398.

814 N Rein ‘Utmost Good Faith in Marine Insurance’ (1999) 10 *Insurance Law Journal* 145, 165.

815 Unreported Supreme Court of South Australia 26 June 1992 (Bollen J).

[t]he obligation of good faith on the part of the insured towards the insurer continues, if there be litigation, until judgment. Perhaps it continues longer.

10.140 In contrast, in *The Star Sea*<sup>816</sup> Justice Tuckey, the judge at first instance, held that the duty of good faith ends once an insurer rejects a claim.<sup>817</sup> In the Court of Appeal, Leggatt LJ speaking for the court did not agree that the duty ended with rejection of the claim but held that after the writ was issued the rules of court supplanted the duty.<sup>818</sup> The judgments in the House of Lords supported this view. For example, Lord Scott stated

I can see a great deal of force in the argument that the section 17 [MIA s 23] duty does not apply to conduct in the prosecution of litigation, as to which the Rules of Court that govern litigation constitute the regulatory code. A decision as to that, too, is best left for a case where the point is critical to the result.<sup>819</sup>

10.141 There is no statement on this point in any Australian case.

10.142 The Commission is inclined to agree with Lord Scott and concludes that the duties of utmost good faith should be stated to extend for the life of the relationship between the parties to any contract of marine insurance (see recommendation 21 below). However, where a claim is litigated the duties should extend only until legal proceedings are commenced by one party against the other. The abrogation of the duties of good faith at that point must be limited to the litigated claim as the contract itself may well remain on foot and the duties must persist in relation to all remaining aspects of the contractual relationship until they too are litigated or otherwise expire. Although not strictly within its terms of reference, the Commission would also recommend that the ICA be amended in the same way.

## Making good faith an implied term of the contract

10.143 Several submissions supported the Commission's draft proposal<sup>820</sup> to amend the MIA to clarify the position in relation to remedies for post-formation breach of the obligations of utmost good faith.<sup>821</sup> The Discussion Paper specifically asked whether the ICA provided an appropriate model for reform.<sup>822</sup>

816 *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [1995] 1 Lloyd's Rep 651.

817 *Ibid* 667.

818 *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [1997] 1 Lloyd's Rep 360, 372. See N Rein 'Utmost good faith in marine insurance' (1999) 10 *Insurance Law Journal* 145, 156.

819 *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] 1 All ER 743, 779. See also 747–8 (Lord Clyde), 769–70 (Lord Hobhouse).

820 ALRC DP 63 draft proposal 12.

821 P Grieve *Submission 6*; K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*; National Bulk Commodities Group *Submission 14*.

822 ALRC DP 63 question 32.

10.144 Section 13 of the ICA provides that there is implied in a contract of non-marine insurance a provision requiring each party to act towards the other party with utmost good faith.<sup>823</sup> It is quite clear that, as utmost good faith is an implied term of contracts of insurance covered by the ICA, damages are available for breach.

10.145 This suggestion has received some support in submissions<sup>824</sup> and, given that such a position applies under ICA s 13, the Australian courts are well placed to apply similar law to marine insurance. Kate Lewins states that

In terms of a likely breach of utmost good faith by an insurer, the most critical time is while the insurer is considering a claim. The insurer has always been obliged to act in utmost good faith in assessing a claim. The ICA does not change this. But it is only now that the ICA gives the insured a useful and appropriate remedy. Therefore the insurer's conduct has become highly relevant. If the MIA is amended along the same lines, the marine insurance industry will have to become accustomed to the same level of scrutiny by insureds and their advisers.<sup>825</sup>

10.146 The recent decision of the House of Lords in *The Star Sea* also provides support for reform. Lord Hobhouse pointedly criticised the remedies available for breach of good faith.

An inevitable consequence in the post-contract situation is that the remedy of avoidance of the contract is in practical terms wholly one-sided. It is a remedy of value to the insurer and, if the defendants' argument is accepted, of disproportionate benefit to him; it enables him to escape retrospectively the liability to indemnify which he has previously and (on this hypothesis) validly undertaken.<sup>826</sup>

10.147 His Lordship subsequently warned that suitable caution should be exercised in making any extensions to the existing law of non-disclosure and that the courts should be on their guard against the 'use of the principle of good faith to achieve results which are only questionably capable of being reconciled with the mutual character of the obligation to observe good faith'.<sup>827</sup> In comments that appear as applicable to the law relating to warranties as to the doctrine of utmost good faith his Lordship noted that

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823 The ICA also prohibits parties from relying on a provision of the contract if to do so would breach the duty of utmost good faith: ICA s 14.

824 K Lewins *Submission 8*; K Carruthers *Submission 9*; MLAANZ *Submission 12*.

825 K Lewins *Submission 8*. Lewins states that the operation of ICA s 13 prescribes a sort of 'commercial morality' similar to that provided by *Trade Practices Act 1974* (Cth) s 52. In practice, these good faith obligations mostly affect the insurer where an insured's inappropriate conduct might cause the insurer to suffer a loss would rarely arise: see F Hawke 'Utmost Good Faith: What Does it Really Mean?' *Insurance Law Journal* (1994) 6(2) 91, 135.

826 *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] 1 All ER 743, 762.

827 *Ibid* 770–1.

[i]t is a striking feature of this branch of the law that other legal systems are increasingly discarding the more extreme features of the English law which allow an insurer to avoid liability on grounds which do not relate to the occurrence of the loss.<sup>828</sup>

10.148 Alexander Street SC suggested that reform should go further than providing for good faith to be an implied term of the contract to expressly state the remedies available to an insured for breach of the duty of good faith by the insurer.<sup>829</sup> Kate Lewins has also suggested such an amendment of the MIA could go further than the ICA by attempting to define some of the incidents of utmost good faith.<sup>830</sup> The Commission does not consider such an extensive amendment to be desirable in view of its overall measured approach to reform of the MIA.

10.149 The Commission concludes that MIA s 23 should be repealed and replaced by a new section incorporating the terms of ICA s 13 and 14. The new section should also include a provision reflecting recommendation 21 concerning the duration of the duties of utmost good faith.

10.150 If this is adopted, the broader range of contractual remedies becomes available in relation to all breaches of good faith and may therefore supplement the other remedies set out specifically in the MIA as amended or in the contract in relation to breach of the duty of disclosure.

## Recommendations

### *General*

**Recommendation 20.** MIA s 23 should be amended to provide that there is implied in a contract of marine insurance a provision requiring each party to act towards the other party with utmost good faith in the terms of ICA s 13 and 14.

828 Ibid 770.

829 A Street *Submission 15*.

830 K Lewins *Submission 8*. Some incidents of breach of the duty may include where the insurer: does not act fairly or honestly in settling a claim; delays in processing or paying a claim; is not candid in dealings with the insured and does to make clear the risk which the insured may run in view of the limited protection afforded by the cover; fails to have due regard to the interests of the insured in the management of litigation conducted pursuant to rights given by the policy; fails to act reasonably or fairly in the exercise of a discretion or in forming an opinion required under the policy in respect of a claim: K Sutton *Insurance Law in Australia* 3rd ed LBC Information Services Sydney 1999, 167.

**Recommendation 21.** The MIA should be amended to provide that the duties of utmost good faith extend for the life of the relationship between the parties to any contract of marine insurance, except in relation to any claim or other aspect of that relationship which is the subject of litigation between the parties. In such cases the duties of utmost good faith cease when one party commences litigation against the other but only in relation to the claim or other aspect of the relationship which is the subject of that litigation.

***Non-disclosure and misrepresentation***

**Recommendation 22.** MIA s 24(1) and 26(1) should be amended to provide that an insured must disclose accurately all circumstances that it knows, or a reasonable person in its position would know, to be material.

**Recommendation 23.** MIA s 24(1) and 26(1) should be further amended by deleting the references to the insurer's right to avoid and a new provision should be inserted to set out the insurer's modified rights covering both non-disclosure and misrepresentation. (See recommendation 25.)

**Recommendation 24.** MIA s 25(a) should be amended

- (1) to provide that an agent must disclose all circumstances that it knows, or a reasonable person in its position would know, to be material, to reflect the amended obligation owed by the insured (see recommendation 22) and
- (2) by deleting 'or to have been communicated to', removing the insured's agent's obligation to disclose what ought to have been communicated to it.

**Recommendation 25.** The MIA should be amended to insert new provisions which provide that if the insured has breached its duties relating to non-disclosure and misrepresentation

- (1) if the breach is fraudulent, the insurer is entitled to avoid the policy from its outset with no return of premium.
- (2) if the breach is not fraudulent
  - (a) where the insurer would not have entered into the contract if it had known of the undisclosed circumstance or the truth of the misrepresented circumstance, the insurer is entitled to avoid the policy from its outset but with a return of premium

- (b) where the insurer would have entered into the contract but on other conditions, the insurer is not entitled to avoid the policy but
  - (i) is not liable to indemnify the insured for a loss proximately caused by the undisclosed or misrepresented circumstance
  - (ii) is entitled to vary its liability to the insured to reflect the amount of any variation in premium, deductible or excess that would have been imposed if it had known of the undisclosed circumstance or the truth of the misrepresented circumstance and
  - (iii) is entitled to cancel the policy in accordance with the other provisions of the MIA on cancellation which are the subject of recommendation 18.

**Recommendation 26.** The MIA should be amended to include a provision based on ICA s 12 that the only duty of pre-contractual disclosure is that provided by MIA s 24–26 and that a contract of marine insurance may not impose a greater duty, or provide for remedies more favourable to the insurer, than those stipulated by the MIA as amended in accordance with these recommendations. The MIA should also be amended to permit express terms in contracts of marine insurance which provide for the insured’s post-contractual duty of disclosure.

**Recommendation 27.** The MIA should be amended to provide that following insurers are deemed to have been induced to enter into a contract if all leading insurers were induced.



# 11. Insurable interest

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## Introduction

11.1 The concept of insurable interest evolved from the statutory avoidance of wagering contracts. Until the Marine Insurance Act 1745 (UK) there was no legal requirement that an insured have any connection to the insured adventure.

Insurance policies were amenable to abuse as wagers on the continued safety of the insured property and, since the assured won the bet if the vessel sank, they provided a financial disincentive to the exercise of due care for the safety of the crew.<sup>831</sup>

11.2 Contracts of marine insurance for speculative purposes (such as gaming and wagering) are declared to be void by the MIA.<sup>832</sup> A contract is deemed to be a gaming or wagering contract where the insured does not have an insurable interest as defined by the MIA and the contract is entered into with no expectation of acquiring such an interest.<sup>833</sup>

- 10(1) Every contract of marine insurance by way of gaming or wagering is void.
- (2) A contract of marine insurance is deemed to be a gaming or wagering contract:
- (a) where the assured has not an insurable interest as defined by this Act, and the contract is entered into with no expectation of acquiring such an interest; or
  - (b) where the policy is made 'interest or no interest,' or 'without further proof of interest than the policy itself,' or 'without benefit of salvage to the insurer,' or subject to any other like term:

Provided that, where there is no possibility of salvage, a policy may be effected without benefit of salvage to the insurer.

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831 H Bennett *The Law of Marine Insurance* Clarendon Oxford 1996, 13.

832 MIA s 10(1).

833 MIA s 10(2)(a).

11.3 The principle of insurable interest is also derived from the fundamental principle of indemnity<sup>834</sup> — the insurer is under an obligation to reimburse the insured for the actual loss from the covered risk and an insured is entitled to be restored, subject to the terms and conditions of the policy, to the financial position enjoyed immediately before the loss. To confirm that the insured suffered loss, it must show that it had an insurable interest in the subject matter insured.

## Parties with an insurable interest

11.4 Persons who have an insurable interest are defined in s 11 of the MIA.

11(1) Subject to the provisions of this Act, every person has an insurable interest who is interested in a marine adventure.

(2) In particular, a person is interested in a marine adventure where he stands in any legal or equitable relation to the adventure, or to any insurable property at risk therein, in consequence of which he may benefit by the safety or due arrival of insurable property, or may be prejudiced by its loss, or by damage thereto, or by the detention thereof, or may incur liability in respect thereof.

11.5 The MIA does not define an insurable interest exhaustively but does give some specific examples. In order to have an insurable interest it is not necessary to have ownership in or title to the insured property. For example, mortgagees<sup>835</sup> and lessees of insured property have an insurable interest. An insurable interest may be partial,<sup>836</sup> defeasible or contingent.<sup>837</sup>

It is sufficient to have a right in the thing insured, or to have a right or be under a liability arising out of some contract relating to the thing insured, of such a nature that the party insuring may have benefit from its preservation, or prejudice from its destruction.<sup>838</sup>

11.6 The MIA also refers specifically to certain other interests as being insurable interests, such as that of a lender of money on bottomry or respondentia,<sup>839</sup> the master or crew members in respect of their wages,<sup>840</sup> a person advancing freight,<sup>841</sup> the insured in costs of insurance which it effects,<sup>842</sup> and a mortgagor or mortgagee of insured property.<sup>843</sup>

834 M Mustill and J Gilman *Arnould's Law of Marine Insurance and Average* 16th ed vol I Stevens & Sons London 1997, 25 fn 89.

835 MIA s 20.

836 MIA s 14.

837 MIA s 13(1).

838 M Mustill and J Gilman *Arnould's Law of Marine Insurance and Average* 16th ed vol I Stevens & Sons London 1981, 218, citing *Lucena v Craufurd* (1806) 2 B & PNR 269, 302 (Lawrence J), 321 (Eldon LJ); *Crowley v Cohen* (1832) 3 B & Ad 478.

839 MIA s 16. See para 11.99–11.101.

840 MIA s 17.

841 MIA s 18.

842 MIA s 19.

843 MIA s 20.

## Judicial interpretations

11.7 The classical statements of what constitutes an insurable interest at common law are found in the 1806 case *Lucena v Craufurd*.<sup>844</sup> These statements by Lawrence J and Lord Eldon contain competing definitions. Professor Sutton observes that the decision of Lawrence J was

couched in terms of a moral certainty of profit or loss, with a man being regarded as having a sufficient interest if he was so placed with respect to the subject matter of the insurance exposed to certain risks as to have a moral certainty of advantage but for those risks.

11.8 In contrast Lord Eldon preferred to define insurable interest in terms of a legally enforceable right in property, or a right derivable from some contract about the property, which might be lost upon some contingency affecting the possession or enjoyment of the assured.

In other words, his Lordship insisted on there being some direct relationship to the property itself, otherwise the interest was too remote.<sup>845</sup>

11.9 Lord Eldon's view ultimately prevailed and this has led to insurers and courts taking a technical approach to the requirement for an insurable interest. The Commission concluded in its 1982 report *Insurance Contracts* (ALRC 20) that this may unduly inhibit recovery for loss.<sup>846</sup>

11.10 For example, in *Macaura v Northern Assurance Co Ltd*,<sup>847</sup> a non-marine case relevant in this context, timber was sold to a company by the owner of the timber in return for shares in the company. The timber was destroyed by fire and the former owner claimed under his policy of insurance. The House of Lords held that the insured had no insurable interest either as a sole shareholder or as a creditor of the timber company. A strict approach was also taken in the South Australian Supreme Court case *Truran Earthmovers Pty Ltd v Norwich Union Fire Insurance Society Ltd*,<sup>848</sup> which involved the purchase of a bulldozer. The purchaser was held to have no insurable interest in the bulldozer even though he had lent the owner money which was to be deducted from the purchase price.<sup>849</sup>

844 (1806) 2 B & PNR 269, 302 (Lawrence J), 321 (Eldon LJ).

845 K Sutton *Insurance Law in Australia* 3rd ed LBC Information Services Sydney 1999, 516.

846 See ALRC 20 para 118–9.

847 [1925] AC 619.

848 (1976) 17 SASR 1.

849 See discussion in ALRC 20 para 119 and LBC *The Laws of Australia* vol 22 Insurance and Income Security '22.1 Insurance' para 33.

11.11 In Canada, the restrictive approach taken by the House of Lords in *Macaura* was rejected in the non-marine case *Constitution Insurance Co of Canada v Kosmopoulos*.<sup>850</sup> The submission was made that *Macaura* should no longer be followed in Canada. The Supreme Court of Canada agreed, finding that there was no basis in public policy for the restrictive approach adopted by Lord Eldon. The Court noted that this approach had been abandoned in many American jurisdictions in favour of the test of any lawful economic interest in the preservation of the property from loss or damage without leading to any difficulties. The Court also noted that commentators in the USA and Canada seemed to be uniformly in favour of the adoption of a test based on whether the insured has a factual expectation of loss.<sup>851</sup>

11.12 More recent English case law is said to have seen a ‘push’ on the ‘frontiers of insurable interest’.<sup>852</sup> For example, in *The Moonacre*<sup>853</sup> the issue of insurable interest arose in a hull insurance case where the insured was not the registered owner of the vessel which had been acquired for his benefit. The vessel was registered for tax purposes in the name of a Gibraltar company. The individual had powers of attorney from the company to sail and manage the vessel and the vessel was insured in his name. A fire on board the vessel resulted in a constructive total loss and the insured claimed under the policy. The judge found that the insured had an insurable interest and stated that

the essential question to be investigated in those cases which, since 1745, have been concerned to test the existence of an insurable interest, has been whether the relationship between the assured and the subject matter of the insurance was sufficiently close to justify his being paid in the event of its loss or damage, having regard to the fact that, if there were no or no sufficiently close relationship, the contract would be a wagering contract.<sup>854</sup>

## Insurable interest at the time of loss

11.13 Even if it did not possess an insurable interest when the contract was made, the insured must possess an insurable interest at the time of the loss, unless the subject matter is insured ‘lost or not lost’. The MIA states

12(1) The assured must be interested in the subject-matter insured at the time of the loss, though he need not be interested when the insurance is effected: Provided that where the subject-matter is insured ‘lost or not lost,’ the assured may recover although he may not have acquired his interest until after the loss, unless at

850 (1987) 34 DLR (4th) 208 as discussed in S Hodges *Cases and Materials on Marine Insurance Law* Cavendish London 1999, 70–2.

851 (1987) 34 DLR (4th) 208, 226–7. See also ALRC 20 para 120; J Long ‘The Concept of Insurable Interest and the Insurance Law Reform Act 1985’ (1992) 7(1) *Auckland University Law Review* 80, 90–1.

852 S Hodges *Cases and Materials on Marine Insurance Law* Cavendish London 1999, 70.

853 *Sharp and Roarer Investments Ltd v Sphere Drake Insurance plc, Minster Insurance Co Ltd and EC Parker and Co Ltd (The Moonacre)* [1992] 2 Lloyd’s Rep 501.

854 *Ibid* 510.

the time of effecting the contract of insurance the assured was aware of the loss, and the insurer was not.

(2) Where the assured has no interest at the time of the loss, he cannot acquire interest by any act or election after he is aware of the loss.

11.14 In addition, the Lloyd's SG Policy wording set out in the Second Schedule to the MIA states

1. Where the subject-matter is insured "lost or not lost", and the loss has occurred before the contract is concluded, the risk attaches unless, at such time, the assured was aware of the loss, and the insurer was not.

11.15 *Arnould's Law of Marine Insurance and Average* states

The "lost or not lost" clause is technically an infringement of the principle requiring that the insured should have an insurable interest in the subject-matter of the insurance at the time of the loss, but it is one well warranted by the requirements of business, and does not offend against the evil which this principle is designed to prevent, *viz.*, that the agreement should not be a mere wager. Indeed, just as the principle of insurable interest is derived from the fundamental principle of indemnity the "lost or not lost" clause is necessary in order that this principle may not be sacrificed to a narrow interpretation of insurable interest.<sup>855</sup>

11.16 A further exception to the rule that the insured must possess an insurable interest at the time of loss is that an assignee of a policy can acquire an interest in the subject matter insured even if the policy was assigned after the loss.<sup>856</sup>

11.17 Whether an insured possesses an insurable interest at the time of loss is an issue which arises most frequently in connection with cargo insurance. Resolving this question often requires careful examination of the terms of contracts for the sale of goods to ascertain exactly when property or risk in the insured cargo passed to or from the insured.

11.18 For example, in the pre-MIA case *Anderson v Morice*<sup>857</sup> a cargo of rice was loaded but before loading was complete the vessel sank. One of the issues raised was whether or not risk had passed to the buyer. The House of Lords held that under the terms of the contract of sale, risk only passed to the buyer when a complete cargo had been shipped and, therefore, the buyer did not have an insurable interest in the goods. Similarly, in *Colonial Insurance Company of New Zealand v Adelaide Marine Insurance Company*<sup>858</sup> the vessel and cargo were lost

855 M Mustill and J Gilman *Arnould's Law of Marine Insurance and Average* 16th ed vol I Stevens & Sons London 1981, 25 fn 89.

856 'Where the assured has parted with or lost its interest in the subject-matter insured, and has not, before or at the time of so doing, expressly or impliedly agreed to assign the policy, any subsequent assignment of the policy is inoperative: Provided that nothing in this section affects the assignment of a policy after loss': MIA s 57.

857 (1876) 1 App Cas 713.

858 (1886) 12 App Cas 128.

after loading had begun but before completion of loading. However, in this instance the Privy Council, after considering the terms of the contract of sale and the circumstances of delivery, held that risk passed to the buyer as and when any portion of the cargo was loaded on board the vessel. Therefore, the buyer did have an insurable interest in the goods on board the vessel.

11.19 A more recent example of the application of the insurable interest requirement is *Fuerst Day Lawson Ltd v Orion Insurance Co Ltd*.<sup>859</sup> In this case, Mocatta J in the English High Court found that a cargo of scented oil purchased by the insured on C&F terms was substituted with water before shipment. Since the insured could not prove that the cargo they agreed to buy had ever been shipped, risk under the policy never attached and this fact was sufficient to dismiss the insured's claim.<sup>860</sup>

11.20 Whether the insured had an insurable interest at the time of loss may also arise in connection with hull insurance. For example, in the case of *Piper v Royal Exchange Assurance*<sup>861</sup> the buyer claimed under his insurance policy for damage that occurred to the vessel on the voyage to the buyer but before its delivery to him. It was held that since the risk was on the seller during the voyage, the buyer had no insurable interest at the time of loss and could not recover. *The Moonacre*<sup>862</sup> case (see paragraph 11.12 above) is another example of insurable interest arising as an issue in a hull insurance context.

11.21 These cases emphasise the strict application of the insurable interest requirement in circumstances where the 'insured' claimants suffered economic or pecuniary loss (to use the words of ICA s 17) and presumably thought they were covered for such loss. Adverse outcomes for claimants resulted, notwithstanding that, in the words of MIA s 11(2), they stood in positions where they would have benefited by the safety or due arrival of insurable property and were prejudiced by its loss.

## Insurable interest in general insurance law

11.22 Even prior to the enactment of the MIA, the strict insurable interest requirement was not unanimously endorsed. Case law established a principle that a court should favour finding an insurable interest where possible. Pleading

859 [1980] 1 Lloyd's Rep 656.

860 See discussion in S Hodges *Cases and Materials on Marine Insurance Law* Cavendish London 1999, 55-6. The fact that the cargo was insured 'lost or not lost' did not assist the insured, cf *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* (1991) 25 NSWLR 699 discussed at length below, where the NSW Court of Appeal held that an insured in similar circumstances was able to recover relying on the 'lost or not lost' clause in the policy.

861 (1932) 44 Lloyd's Rep 103.

862 *Sharp and Roarer Investments Ltd v Sphere Drake Insurance plc, Minster Insurance Co Ltd and EC Parker and Co Ltd (The Moonacre)* [1992] 2 Lloyd's Rep 501.

‘insurable interest’ as the sole defence to avoid a claim is considered by many to be a mere technicality and an unmeritorious defence, particularly where the underwriters have accepted the premium from the claimant.<sup>863</sup> The reticence of courts to accept such a defence to a claim is reflected in the following comments of Justice Mance.

[T]he present policy is not on its face one which the parties made for other than ordinary business reasons; it does not bear the hallmarks of wagering or the like. If underwriters make a contract in deliberate terms which covers their assured in respect of a specific situation, a Court is likely to hesitate before accepting a defence of lack of insurable interest.<sup>864</sup>

11.23 The common law required that there be an insurable interest both at the time of entering the contract and when the loss occurred. That is, the insured must show a strict proprietary interest, or some legal or equitable interest, in the subject matter of the insurance, although the interest need not be continuous.<sup>865</sup> This was changed by MIA s 12 (see paragraph 11.13).

11.24 In ALRC 20, the Commission noted that the requirement that the insured have an insurable interest in the subject matter was said to serve ‘two main policies’. Firstly, it discourages gaming and wagering in the form of insurance;<sup>866</sup> secondly, it minimises the risk of destruction by the insured of the subject matter of the insurance.<sup>867</sup> However, the Commission concluded that insurable interest requirements were the result of a combination of imprecise drafting and historical accident rather than the coherent implementation of clear legislative policy.<sup>868</sup> The policies said to be served by the insurable interest requirement were adequately protected by the indemnity principle itself since potential recovery is limited to actual loss.<sup>869</sup>

863 D Galbraith ‘An Unmeritorious Defence — The Requirement of Insurable Interest in the Law of Marine Insurance and Related Matters’ (1993) 5(3) *Insurance Law Journal* 177; *Stock v Inglis* (1884) 12 QBD 564.

864 *Cepheus Shipping Corporation v Guardian Royal Exchange Assurance PLC* [1995] 1 Lloyd’s Rep 622 (Mance J).

865 F Marks and A Balla *Guidebook to Insurance Law in Australia* 3rd ed CCH Sydney 1998, 91–2 citing *Macaura v Northern Assurance Co Ltd* [1925] AC 619; *FAI Insurances Ltd v Custom Credit Corp Ltd* (1980) 29 ALR 505.

866 *Newbury International Ltd v Reliance National Insurance Co (UK) Ltd* [1994] 1 Lloyd’s Rep 83 is a modern example of a contract of insurance being found to be a wagering contract. In this case, the insured took out a policy to ‘indemnify’ the insured in respect of a contractual obligation to pay £425 000 in event of a particular racing car driver achieving a top three series position. It was a contractual condition precedent that the relevant sum should first have been received from the insurers before the plaintiffs could be sued for it. The judge found that the insured ‘never in truth had any insurable interest’ and the contract was merely a device to raise money by, in substance, placing a bet on the outcome of the motor racing. The judge stated that ‘[I]f policies of prize indemnity insurance are to be valid contracts of insurance there must be a true liability to another which is the subject matter of the insurance’. The reforms to insurable interest requirement made by the ICA do not appear to affect this reasoning, which is based on an application of the indemnity principle.

867 ALRC 20 para 107.

868 *Ibid* para 107–49.

869 *Ibid* para 117.

11.25 The Commission's suggestion in 1978 that the indemnity principle should be restated in terms of actual economic loss was supported by both the Insurance Council of Australia and the Insurance Brokers' Council of Australia.<sup>870</sup> The Commission recommended the introduction of an economic interest test so that where an insured is economically disadvantaged by loss, the insurer should not be relieved of liability by reason only that the insured did not have a legal or equitable interest in the property.<sup>871</sup>

11.26 These recommendations were implemented in the ICA,<sup>872</sup> which modified the concept of insurable interest in the context of non-marine general insurance.<sup>873</sup> Section 16 of the ICA states that a 'contract of general insurance is not void by reason only that the insured did not have, at the time when the contract was entered into, an interest in the subject matter of the contract'. The ICA uses an economic loss test to determine whether the insured has a sufficient interest to claim under the policy. Section 17 states where the insured has suffered a pecuniary or economic loss the insurer is not relieved of liability by reason only that, at the time of loss, the insured did not have an interest in law or in equity in the property.<sup>874</sup> These changes do not appear to have been controversial since their introduction 15 years ago in that there have been very few cases involving ICA s 16 and s 17 (see paragraph 11.89).

## Insurable interest and the FOB or C&F buyer

11.27 The Discussion Paper examined arguments for reform of the requirement for an insurable interest in marine insurance law and asked whether the MIA should be reformed so as to be consistent with the ICA in this regard.

870 ALRC DP 7 para 22-27; ALRC 20 para 120.

871 ALRC 20 para 119-20, Appendix A Draft Insurance Contracts Bill 1982 cl 17.

872 ICA s 16-17. In addition, s 48 of the ICA implemented the Commission's recommendation that third parties who are specified or referred to in a contract of insurance should be entitled to recover under the contract, notwithstanding that the person is not a party to the contract: ALRC 20 para 124; Draft Insurance Contracts Bill s 48; ICA s 48.

873 The ALRC recommended the retention of insurable interest requirements for contracts of life insurance: ALRC 20 para 134-48. The ICA, as enacted, provided that life insurance contracts were void if the insured did not, at the time when the contract was entered into, have an insurable interest in the life of the insured. However, in 1995, the *Life Insurance (Consequential Amendments and Repeals) Act 1995* (Cth) repealed and substituted these provisions so that a contract of life insurance is not void by reason only that the insured does not have an interest in the subject-matter of the contract: ICA s 18.

874 In New Zealand, the Insurance Law Reform Act 1977 s 7 appears to remove the requirement for an insurable interest in relation to non-marine 'indemnity' insurance, but the scope of the reform is uncertain: See J Long 'The Concept of Insurable Interest and the Insurance Law Reform Act 1985' (1992) 7(1) *Auckland University Law Review* 80, 92-7. Julian Long concludes that the New Zealand Act does nothing to alter the common law position 'whereby an insured can suffer no loss without an insurable interest'. However, following the Supreme Court of Canada's decision in *Constitution Insurance Co of Canada v Kosmopoulos* (1987) 34 DLR (4th) 208 (see para 11.11) 'there are clear indications that a New Zealand Court might mitigate the harshness of the strict interest requirement where appropriate': 96-7.



11.28 A particular focus of this discussion was *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd*,<sup>875</sup> a case often referred to as illustrating a need for such reform.<sup>876</sup> The problem highlighted by *NSW Leather* is that a buyer of goods on FOB (or C&F) terms<sup>877</sup> may be unable to insure against pre-shipment losses.

That is, when a buyer purchases goods on FOB terms (which are desirable because of their flexibility), unless the insurer provides 'lost or not lost' or other pre-shipment cover, the buyer will be uninsured for the goods prior to loading. In these circumstances, unless the buyer is able to recover from the seller or carrier, its position may be hopeless.<sup>878</sup>

11.29 In *NSW Leather*, the insured had an insurance policy, stated to be insurance 'lost or not lost',<sup>879</sup> for consignments of leather that it had purchased FOB from various Brazilian suppliers. The insurance policy contained a 'warehouse-to-warehouse' or 'transit' clause in the terms of the Institute Cargo Clauses (A) stating that

This insurance attaches from the time the goods leave the warehouse or place of storage at the place named in the policy for the commencement of the transit, continues during the ordinary course of transit and terminates [on delivery].

11.30 The goods were loaded in containers but most of them were stolen before the containers were loaded on board the ship. The insurers denied the claim on the grounds that the insured did not have an insurable interest at the time of loss.

11.31 Under a standard FOB contract, the risk in respect of goods, whether or not loaded in a sealed container, does not pass to the buyer until the container has passed the ship's rail. In the Supreme Court of New South Wales, Justice Carruthers confirmed the rule that a purchaser FOB does not have an insurable interest in goods during transit from the seller's warehouse to the ship's rail. The judge held that the transit clause could not operate to extend the cover to an earlier point in time in the absence of an insurable interest.

11.32 On appeal, the New South Wales Court of Appeal agreed with the trial judge that the insured did not have an insurable interest in the goods at the time of loss,

875 (1990) 103 FLR 70; (1991) 25 NSWLR 699 (NSWCA).

876 D Galbraith 'An Unmeritorious Defence — The Requirement of Insurable Interest in the Law of Marine Insurance and Related Matters' (1993) 5(3) *Insurance Law Journal* 177; A Mason 'The Future of Marine Insurance Law' 1995 Ebsworth & Ebsworth Maritime Law Lecture; M Taylor 'Is the Requirement of an Insurable Interest in the Marine Insurance Act Still Valid?' (2000) 11 *Insurance Law Journal* 147.

877 That is, in policies covering goods sold on 'Free on Board' (FOB) or 'Cost and Freight' (C&F) terms under which the risk (but not necessarily the property) in the goods passes to the purchaser at the ship's rail. The term C&F has been replaced with CFR in the Incoterms 1990 and Incoterms 2000.

878 M Taylor 'Is the Requirement of an Insurable Interest in the Marine Insurance Act Still Valid?' (2000) 11 *Insurance Law Journal* 147, 149–50.

879 *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* (1990) 103 FLR 70, 77.

and therefore could derive no assistance from the transit clause.<sup>880</sup> The pre-loading portion of the warehouse-to-warehouse is, viewed in isolation, worthless to a purchaser on FOB terms and does not in fact provide the cover that its name suggests.

### **‘Lost or not lost’ clauses**

11.33 The position of an insured buyer FOB or C&F may be improved by the insertion of a ‘lost or not lost’ clause in the policy. In *NSW Leather*, the New South Wales Court of Appeal ultimately held that the insured was able to recover, relying on the ‘lost or not lost’ clause in combination with warehouse-to-warehouse cover.

11.34 At first instance, Justice Carruthers stated the proposition that, consistently with the fundamental principle that a contract of insurance is a contract of indemnity, an insured cannot rely on a ‘lost or not lost’ clause unless the loss falls on it. He held that the loss in question had clearly not fallen on the insured, even though it had already paid for the goods, who was entitled to recover the purchase price from the sellers.<sup>881</sup> In contrast, the Court of Appeal found that the insured had suffered a loss even though the insured was not at risk when the goods were stolen. It was sufficient that the ‘insured suffered financial loss because of the prior loss of the goods’. The fact that it had contractual remedies against its sellers was no barrier to a claim on the insurance.<sup>882</sup>

11.35 *NSW Leather* appears to be authority for the proposition that where an insured suffers a loss prior to obtaining an insurable interest in the goods (for example, by paying cash against documents) and subsequently acquires an insurable interest in those goods, a combination of a ‘lost or not lost’ and warehouse-to-warehouse clause entitles the insured to indemnity.

11.36 This interpretation has been criticised as inconsistent with the ‘common understanding and usage of ‘lost or not lost’ clauses’, said to be where cover is provided after an insurable interest has been acquired (by the first buyer in the chain), as with purchase of cargo in transit at sea, where the insured is not aware the goods have been lost.<sup>883</sup> One view is that it has never been insurers’ intention that ‘lost or not lost’ clauses should cover cases where loss occurs before an insurable interest has been acquired by an insured. This is supported by the wording of the definition of ‘lost or not lost’ found in the first Rule for

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880 However, Handley JA noted that the insured did have an insurable interest prior to loading in the profits it expected to derive from the safe arrival of the goods and in the risk that it would pay in good faith for shipping documents relating to goods which had been stolen before loading, or would otherwise suffer loss because the shipping documents were forged or fraudulent: (1991) 25 NSWLR 699, 707.

881 (1990) 103 FLR 70, 88.

882 (1991) 25 NSWLR 699, 711.

883 Associated Marine Insurers Agents Pty Ltd *Correspondence* 17 April 2000.

Construction in the second schedule to the MIA, which deals with losses occurring before the contract is concluded of which the insured is unaware but has nothing to say about losses occurring before the insured acquires an insurable interest. However, others in the insurance industry have contested this understanding and consider that there is little historical evidence to support a narrow application of such clauses.<sup>884</sup> The difference in understanding in this area is one example of the unreliability of common shorthand expressions in insurance contracts which are thought to have a common and accepted meaning. In fact, without a clear definition in an approved, widely accessible and authoritative source, understandings can and do vary considerably.

11.37 The inconsistency of understanding in this respect only serves to exacerbate uncertainty in this area. If the New South Wales Court of Appeal's interpretation of these clauses is subject to dispute, there is the risk that other courts not bound by its decision will conclude otherwise, possibly accepting Justice Carruthers' interpretation. If that position received endorsement, a purchaser who pays for goods before it acquires an insurable interest under the contract of sale will find that its exposure to financial loss due to loss of or damage to the goods occurring before it acquires that interest is simply uninsurable. No combination of special terms can remedy that predicament. As the payment of goods in international contracts of sale conventionally proceeds through the banking system and is not synchronised with events during transit, there can be no guarantee that payment and the transfer of risk occur at the same time. Purchasers must therefore often be exposed to the risk of financial loss if payment occurs earlier than shipment. No such problem arises if payment occurs after shipment.

11.38 The insertion of 'lost or not lost' clauses in contracts of marine insurance does not appear to be a complete solution to the needs of insured buyers FOB or C&F. Such clauses may assist the insured (assuming that it is aware of the loss) only where

- the loss occurs before the contract of insurance is concluded but after the risk or insurable interest has passed to the insured or
- the loss occurs before the insurable interest passes to the insured but it subsequently does pass (without any further act or election by the insured).<sup>885</sup>

11.39 The extent to which 'lost or not lost' cover is commonly available from Australian insurers is unclear.<sup>886</sup> However, the Commission is principally

884 Broker *Consultation* Perth 23 November 2000; Gault Armstrong & Kemble *Submission 18*.

885 M Taylor 'Is the Requirement of an Insurable Interest in the Marine Insurance Act Still Valid?' (2000) 11 *Insurance Law Journal* 147, 155.

886 It has been stated that such cover is not commonly available: *Advisory Committee meeting* 18 December 2000. However, the Institute Cargo Clauses (A) cl 11.2 contains a lost or not lost clause. One broker has

concerned that an insured have the legal ability to be insured. The parties to a contract of insurance should be able to contract in such a way as to break the link between cover for pre-shipment loss and the passing of risk or property under the contract for sale, if this is commercially desirable. At present, the MIA constrains their ability to do so. Market forces will dictate the availability and cost of such cover. Insurers should be able to assess the nature of the relevant risks in advance.

11.40 Importantly, if goods are lost prior to loading the ‘lost or not lost’ clause will not assist unless the buyer of goods on FOB or C&F terms also purchases ‘warehouse-to-warehouse’ cover because the risk will not attach until the goods are loaded onto the ship.<sup>887</sup>

It is difficult for buyers on FOB terms to purchase “warehouse to warehouse” cover, as many underwriters will not offer such terms to FOB buyers, on the basis that they will not attain an insurable interest until the cargo has passed the ship’s rail. In addition, “lost or not lost” clauses are not offered in most standard policies offered by marine underwriters.<sup>888</sup>

11.41 Even if both types of clause are included in the contract, an insurer may still resist liability where cargo is lost or stolen prior to loading by arguing that under the contract of sale the insured never acquired an insurable interest in the cargo and therefore the ‘lost or not lost’ cover does not operate. While this point was argued unsuccessfully in *NSW Leather*, in some circumstances the total destruction or loss of goods may frustrate the contract of sale so that the buyer never obtains an interest in any of the goods.<sup>889</sup>

11.42 Based on *NSW Leather* it seems that the ‘lost or not lost’ clause in a warehouse-to-warehouse policy will cover a buyer on FOB or C&F terms for pre-loading loss or damage to goods, at least where goods are lost or damaged in part. Neither the ‘lost or not lost’ clause nor the warehouse-to-warehouse clause in isolation is adequate to allow recovery for pre-loading loss or damage to the goods in all circumstances. It remains unclear if recovery for loss or damage to goods is possible in the event of their total loss or destruction.

11.43 Loss of profits related to goods not loaded seems to be recoverable even in the absence of a ‘lost or not lost’ clause as the New South Wales Court of Appeal found that the buyer in *NSW Leather* had an insurable (and insured) interest in its

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submitted that there has been little market reaction to *NSW Leather* and Australian insurers continue to issue cargo policies incorporating both warehouse-to-warehouse and lost or not lost clauses: Gault Armstrong & Kemble *Submission 18*.

887 M Taylor ‘Is the Requirement of an Insurable Interest in the Marine Insurance Act Still Valid?’ (2000) 11 *Insurance Law Journal* 147, 155–6. In *NSW Leather*, an open policy had been issued several years before the theft so commencement of cover was not at issue: (1991) 25 NSWLR 699, 710.

888 *Ibid* 155.

889 (1991) 25 NSWLR 699, 711–3.

anticipated profits at the time of loss, though warehouse-to-warehouse terms are still necessary.

### **FOB or C&F pre-shipment clauses**

11.44 It has been argued that the practice of inserting ‘FOB or C&F pre-shipment clauses’ in policies provides insureds with adequate additional protection for pre-shipment loss. The clauses provide that, notwithstanding the provisions of the contract of sale, the insurance attaches from the beginning of the transit, or that loss or damage to the goods discovered at destination is deemed to have occurred during the transit insured.<sup>890</sup> The first type of clause is akin to a warehouse-to-warehouse clause in that it purports to fix the attachment of the risk at a point in time before the insured acquires its insurable interest; the second type is simply a deeming provision to obviate the need to investigate the time of loss and is presumably intended to override any evidence that loss occurred before loading.

11.45 The idea behind the development of such pre-shipment clauses was to give the insured the choice of making a claim against either the seller or their insurer when it is not clear at what point in time the loss has occurred.<sup>891</sup> Under some of these clauses, the insured is able to recover for loss or damage that may have occurred before risk in the property passes but is placed under an express obligation to pursue any claim against the seller or assist the insurer to do so.<sup>892</sup> A FOB or C&F pre-shipment clause is said to provide the insured with ‘seamless cover’, allowing it to obtain payment for losses either immediately from its own insurer or later, after first attempting to recover from the seller.

11.46 Michelle Taylor has highlighted problems with the FOB and C&F pre-shipment clauses currently used in the Australian market. These problems are said to include ambiguity about when cover first attaches and the extent of the obligation on the insured to use all reasonable means to first recover from the exporter or supplier.<sup>893</sup> Most importantly for present purposes, she states that an insurer can argue that the cover provided by such clauses is not enforceable as they are in contravention of the insurable interest requirements of the MIA.

[An FOB or C&F pre-shipment clause] provides cover for an assured who does not have an insurable interest. Furthermore, it is not a “lost or not lost” clause, as it is not dependent upon the assured subsequently attaining an insurable interest after the loss has occurred.<sup>894</sup>

890 Example clauses provided by Associated Marine Insurers Agents Pty Ltd *Consultation* Melbourne 7 April 2000.

891 *Advisory Committee meeting* 18 December 2000.

892 *Ibid.*

893 M Taylor ‘Is the Requirement of an Insurable Interest in the Marine Insurance Act Still Valid?’ (2000) 11 *Insurance Law Journal* 147, 156–7.

894 *Ibid* 157.

11.47 In this regard FOB and C&F pre-shipment clauses do not have the statutory basis enjoyed by 'lost or not lost' clauses. Taylor confirms that there has been no judicial consideration of the validity of pre-shipment cover offered to FOB buyers. As stated in the Discussion Paper, some insurers have indicated to the Commission that they consider pre-shipment clauses as 'commercially' rather than legally enforceable against the insurer because they are in breach of the insurable interest requirements of the MIA.<sup>895</sup> They may simply be void. This is less likely with the deeming type of pre-shipment clause as described in paragraph 11.44 as they do not purport to extend cover but simply deem loss to have occurred during transit.

11.48 At least where there is some uncertainty about the time of loss, courts may be reluctant to allow an insurer to avoid liability under a pre-shipment clause. The *Trade Practices Act 1974* (Cth) and equitable doctrines of estoppel, unjust enrichment and restitution may provide possible avenues of relief for an insured. However, the courts have not had the opportunity to consider the effect of pre-shipment clauses and the likely outcome in such a case remains uncertain. Taylor has observed that

[i]f an insurer declined indemnity to an assured on the basis that the cover was not legally enforceable, the issue of an insurer providing illusory cover to an assured would have to be reconciled. Nevertheless, it would be open for a court to find that the contract of insurance was void ab initio and that the remedy for the assured would be no more than the refund of the premium.<sup>896</sup>

11.49 It can be argued that buyers on FOB or C&F terms have other means by which to protect their interests against pre-shipment loss and that, therefore, reform of the MIA's insurable interest requirements is not justified.<sup>897</sup>

### **CIF contracts**

11.50 A buyer can purchase goods on CIF (cost, insurance, freight) terms so that the seller is obliged to procure marine insurance against the buyer's risk of loss during the carriage. The seller contracts for insurance and pays the insurance premium. If the goods are lost before the buyer acquires an insurable interest, the seller's policy of insurance will provide indemnity, at least to the seller.

11.51 However, there are many reasons why buyers (and specifically Australian importers) may justifiably prefer to buy FOB or C&F. These include possible advantages in terms of control of premium costs, policy conditions and claims

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895 Associated Marine Insurers Agents Pty Ltd *Correspondence* 17 April 2000.

896 M Taylor 'Is the Requirement of an Insurable Interest in the Marine Insurance Act Still Valid?' (2000) 11 *Insurance Law Journal* 147, 157.

897 eg Insurance Council of Australia *Submission* 29 May 1997.

handling.<sup>898</sup> However, in some cases, commercial pressure may force them to buy FOB or C&F, and CIF terms may simply not be available. As discussed in chapter 6, there may be important national economic reasons to encourage Australian importers to arrange insurance with Australian insurers.<sup>899</sup>

11.52 In any event, purchasers on CIF terms are not necessarily better placed than buyers on other terms. Under Incoterms 2000, the risk in a CIF contract passes to the buyer when the goods cross the ship's rail at the port of shipment, which is the same time as under FOB and CFR contracts.<sup>900</sup> Payment before this time under a CIF contract exposes the buyer to the same potential for economic loss as under an FOB contract.

### Terms of the contract of sale

11.53 If buyers wish to trade on FOB terms they may be able to negotiate appropriate departures from the usual FOB terms to help protect their interests. Parties may contract so that the risk in the goods passes at an earlier point in time than at the ship's rail.

11.54 In 1980 the Incoterm 'Free Carrier' (FCA) was introduced to cater for the situation (frequently arising with containerisation) where the reception point for goods is not at the ship's rail but the point at which the goods are stowed into a container, on land prior to transport by sea or other means.<sup>901</sup> The International Chamber of Commerce, which develops and publishes the Incoterms, noted that parties to contracts for sales of goods still continue to use FOB terms in situations where the goods are handed over to the carrier before loading on board the ship.

Regrettably, merchants continue to use FOB when it is totally out of place thereby causing the seller to incur risks subsequent to the handing over of the goods to the carrier named by the buyer. FOB is only appropriate to use where the goods are intended to be delivered "across the ship's rail" or, in any event, to the ship and not

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898 For example, it is said that, by importing on CIF terms, the importer pays a premium in the CIF price, even if a separate charge is not specified in the invoice, and the importer may have no control over, and often no knowledge of, the amount of this premium or the terms of the policy. A buyer FOB can arrange the policy on insurance conditions which meet the buyer's requirements but when buying CIF may receive an insurance policy with conditions which suit the seller. Importers buying on CIF terms who need to make a claim for lost or damaged goods will have to do so under a policy issued overseas, which may present a range of practical disadvantages: See <http://associatedmarine.com.au/import.htm> (12 October 2000).

899 Australian importers buying on FOB and C&F terms assist the Australian marine insurance industry as, by and large, they will purchase their insurance in Australia whereas insurance purchased by overseas exporters as part of a CIF package will be generally purchased overseas.

900 International Chamber of Commerce *Incoterms 2000* ICC Publishing SA Paris 1999, 69.

901 *Ibid.*, 24. Alternatively, the parties may adopt American Uniform Commercial Code terms of trade, under which 'FOB' (as opposed to 'FOB vessel') means that the seller is to deliver the goods to the carrier and the buyer obtains the risk at the delivery point nominated by the buyer, which may be prior to shipment: P Evans 'FOB and CIF Contracts' (1996) 67 *Australian Law Journal* 844, 844-5 citing US *Uniform Commercial Code* s 2-319(1).

where the goods are handed over to the carrier for subsequent entry into the ship, for example stowed in containers or loaded on lorries or wagons in so-called roll on roll off traffic.<sup>902</sup>

11.55 The Chamber might also have observed that not only does the seller incur unintended risks but the buyer's interest in the goods may not be insurable until loaded. The extent to which its observation about the use of inappropriate contractual terms holds true in respect of contracts entered by Australian buyers is not known.

11.56 Another option is for buyers to contract to delay payment for the goods until they have been adequately inspected. However, even assuming that the buyer is able to negotiate such terms, adequate inspection is not always possible.<sup>903</sup> In practice, common forms of international contracts for sale of goods include 'cash against documents' terms so that delaying payment until an inspection has taken place may not be available to the buyer. Commercial realities mean that Australian importers may find it difficult to negotiate terms of trade which are significantly different from usual FOB terms.

### Containerisation

11.57 Reform to change the point in time at which the risk passes to the buyer, and therefore the time at which the buyer obtains an insurable interest, has been suggested and was canvassed in the Discussion Paper.<sup>904</sup>

11.58 Broadly, it may be argued that, in view of cargo containerisation, the law should deem containers to be functionally part of the ship, so that loading into the container should generally be considered as the point of delivery at which risk in the goods passes.

To apply to containers the law developed for individually packaged cargo strikes me as yet another instance of the incapacity of legal principle to adapt and change to

902 International Chamber of Commerce *Incoterms 2000* ICC Publishing SA Paris 1999, 24.

903 Taylor states that unless 'foul play' is suspected, it would not be the usual practice to inspect goods between the time of delivery to the container park or wharf, and the time of loading onto the ship. In fact, it would be impractical to do so, as once the goods have been containerised, there is little or no opportunity for the buyer to inspect the goods prior to loading. Primary difficulties are that the goods are usually sealed into containers for shipment and the goods often pass through numerous transit entities prior to shipment: M Taylor 'Is the Requirement of an Insurable Interest in the Marine Insurance Act Still Valid?' (2000) 11 *Insurance Law Journal* 147, 159–60.

904 D Galbraith 'An Unmeritorious Defence — The Requirement of Insurable Interest in the Law of Marine Insurance and Related matters' (1993) 5(3) *Insurance Law Journal* 177; A Mason 'The Future of Marine Insurance Law' 1995 Ebsworth & Ebsworth Maritime Law Lecture; *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* (1991) 25 NSWLR 699, 701 (Kirby P).



reflect new technological and commercial realities. When such developments as containerisation occur, it is desirable that the law should reflect a new principle.<sup>905</sup>

11.59 Containerisation can make it more difficult to establish precisely when and where damage to, or loss of, goods took place and, therefore, whether the insured had an insurable interest at the time of loss. While this problem is not new,<sup>906</sup> problems in inspecting cargo have multiplied significantly with containerisation.<sup>907</sup>

[T]here are now more individuals involved in the handling process after goods leave their supplier's hands for the last time prior to export, and there are probably greater time gaps between the time when goods leave their supplier's hands and when they pass the ship's rail than was the case when cargo was shipped break bulk.<sup>908</sup>

11.60 In *NSW Leather*, the New South Wales Court of Appeal referred to US cases which have characterised containers, for some purposes, as functionally part of a ship but declined to imply from this analysis that the parties to the contract of sale should be held to have agreed that risk passed when the goods were effectively shipped by being sealed in the container.<sup>909</sup> The US authorities involve cases concerning the limitation of liability per package under the Hague Rules and the proper construction of industrial safety legislation for the protection of waterside workers. In *NSW Leather*, Handley JA cautioned that the statements in these US authorities should not be taken literally or out of their context to support the view that containers still on land have been loaded on board ship.<sup>910</sup>

11.61 The Commission does not consider that any reform of this nature is justified as part of the present review. There is nothing to prevent parties to a contract for the sale of goods expressly contracting for risk to pass at the time of loading into a container and Incoterms have provided for a 'Free Carrier' term since 1980. One view is that FOB terms should not be so commonly used 35 years after the widespread introduction of containerisation. However, this should remain a matter to be resolved by the parties to contracts for international sale of goods.<sup>911</sup> Unilateral change to the MIA may have unintended implications far beyond insurance law, notably in respect to carrier's liability under the Hague-Visby Rules and the *Carriage of Goods by Sea Act 1991* (Cth) (COGSA). Any such change

905 *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* (1991) 25 NSWLR 699, 701 (per Kirby P). Justice Kirby also observed that 'any such new principle should, if possible, command widespread international acceptance'.

906 See for example the comments of Carruthers J in *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* (1990) 103 FLR 70, 82, quoted in ALRC DP 63, para 7.19.

907 See M Taylor 'Is the Requirement of an Insurable Interest in the Marine Insurance Act Still Valid?' (2000) 11 *Insurance Law Journal* 147, 159–60.

908 D Galbraith 'An Unmeritorious Defence — The Requirement of Insurable Interest in the Law of Marine Insurance and Related Matters' (1993) 5(3) *Insurance Law Journal* 177, 181.

909 *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* (1991) 25 NSWLR 699, 701 (Kirby P) 704 (Handley JA).

910 Ibid 704, referring to *Northeast Marine Terminal Co Inc v Caputo* 432 US 249 (1977) and *Mitsui and Co Ltd v American Export Lines Inc* 636 F 2 807 (1981).

911 *Advisory Committee meeting* 18 December 2000.

should, in the Commission's view, be part of a co-ordinated change to the law in relation to international contracts of sale and carriage of goods.

### **Remedies against the seller or carrier**

11.62 Where goods are lost or damaged before loading, FOB buyers have a range of possible statutory, contractual or tortious remedies, as do buyers on other terms. Possible remedies against the seller include those under the contract of sale, sales of goods legislation, trade practices legislation and in the tort of negligence (where the damage to the goods was reasonably foreseeable by the seller). Possible remedies against the carrier include remedies in tort, under the contract of carriage and COGSA or similar legislation.<sup>912</sup>

11.63 For example, a FOB buyer may sometimes be able to reject goods if they do not conform to the contract of sale or recover the purchase price if this has been paid. However, remedies depend on the specific terms of the contract of sale and the extent to which these remedies are legally or commercially viable will vary.

11.64 A survey of possible remedies by Michelle Taylor concludes that contractual remedies that are available to buyers who have unknowingly paid for stolen or vandalised goods are subject to conflicting authorities which may discourage buyers from litigating. Contractual or other remedies against the seller will be unrewarding where the seller is impecunious and may be prohibitively difficult and costly where proceedings must be taken overseas. Further, as a result of broad exclusion clauses, COGSA and limited tortious remedies, a buyer on FOB terms is unlikely to have recovery rights against a carrier for most pre-shipment loss.<sup>913</sup> However, to the extent that any remedies are available to a buyer against a seller, they are also available to the buyer's subrogated insurer.

### **Reform of insurable interest**

11.65 At least in relation to cargo insurance there seems to be a strong case for reform of the insurable interest requirements of the MIA. The discussion above highlights the fact that FOB and C&F buyers face difficulties in recovering for pre-shipment losses which stem from the Act itself. There seems no reason why FOB or C&F buyers should effectively be prevented from insuring against pre-shipment losses. It is clearly a recurring commercial risk for which insurance cover should be available in principle.

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912 See M Taylor 'Is the Requirement of an Insurable Interest in the Marine Insurance Act Still Valid?' (2000) 11 *Insurance Law Journal* 147, 161–6.

913 *Ibid.*

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As regards obtaining indemnity from an adequate policy of insurance, the cover available to buyers is, at best, limited and, at worst, illegal (as it is in contravention of s 11 of the MIA).<sup>914</sup>

11.66 As discussed in the Discussion Paper, it appears that insurers commonly enter contracts of insurance — using either FOB and C&F pre-shipment clauses or, more rarely, a ‘lost or not lost’ clause — which purport to indemnify an insured for loss even though the insured may not have an insurable interest at the time of loss. The willingness of insurers to provide such cover is evidence of market demand for effective insurance against pre-shipment losses. The Commission does not consider that there would be any significant uncertainty created if buyers are able to insure pre-shipment losses, subject of course to the market availability of such cover.

### Assignment of policies

11.67 A marine policy is assignable unless it contains terms expressly prohibiting assignment and may be assigned either before or after loss.<sup>915</sup> Under MIA s 57, the assignment of the contract of insurance is inoperative if the agreement to assign occurs after the assured ‘has parted with or lost his interest in the subject-matter insured’. The actual assignment, it seems, can take place later. *Arnould’s Law of Marine Insurance and Average* states

Valid assignment before loss supposes the coexistence of three things at the time of assignment: (1) an insurable interest in the subject-matter of the policy in the assignor; (2) the continuance of the risk insured in the policy; (3) the assignment of an insurable interest in the subject-matter of the policy to the assignee, and its exposure to the perils during the continuance of the risk.<sup>916</sup>

11.68 If the requirement for an insurable interest is reformed, s 57 should also be repealed.

11.69 Nevertheless, under a reformed MIA cover provided by contracts of marine insurance would still generally be assigned in conjunction with passing of the legal or equitable interest. While it would be possible for the policy of insurance to be validly assigned before the assignor (or assignee) obtained an interest in the subject matter, the liability of the insurer would continue to depend on the indemnity principle — whether the assignee of the policy has suffered actual loss caused by an insured peril during the period of cover.

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914 Ibid 168. The cover is perhaps better described as ‘void’ rather than ‘illegal’.

915 MIA s 56.

916 M Mustill and J Gilman *Arnould’s Law of Marine Insurance and Average* 16th ed vol I Stevens & Sons London 1981, 169.

11.70 The Commission has received no information suggesting that reform of the insurable interest requirements in the ICA has produced problems with regard to the assignment of policies of general insurance.

### **Overlapping insurance**

11.71 If FOB buyers more commonly have pre-shipment cover, there will be an increased incidence of overlapping insurance where a loss is potentially covered by both the seller's and buyer's insurance. As discussed in the Discussion Paper, some insurers have claimed that this situation could work to the detriment of Australian insurers and insureds, among other reasons by creating a situation where overseas sellers would be more likely to resist claims made against them.<sup>917</sup> However, reform of the insurable interest requirement would not prevent the terms of the contract providing that the buyer's cover is subsidiary to, or contingent on the inadequacy or non-existence of, the seller's insurance or being limited to meeting a shortfall in other inadequate insurance.

11.72 In any event, the situation would be no worse than at present if the buyer has pre-loading transit cover and 'lost or not lost' cover (and so falls within the *NSW Leather* position) or has FOB or C&F pre-shipment cover. In these situations, the extended cover would likewise encourage an overseas exporter to resist claims under the contract of sale.

11.73 The current situation, as illustrated by *NSW Leather* and the confusion about the status of FOB and C&F pre-shipment clauses, is uncertain. To ascertain whether there was an insurable interest at the time of loss, it is relevant to consider the details of the contract of sale, whether the goods are specific or unascertained, the intention of the parties, the sale of goods rules for ascertaining the parties' intentions (which may well be governed by foreign law), whether risk passes with property and whether property passes with delivery.

11.74 The Commission is not convinced that removal of the requirement for an insurable interest would be disadvantageous to the Australian insurance industry or lead to a rise in premiums. Where pre-shipment cover is offered, premiums may be higher than for policies which do not cover pre-shipment losses, but this should not lead to any general rise in premiums. This rise represents a greater cost for greater cover. Whether pre-shipment cover is offered and on what terms is a matter for the market.

11.75 International competitiveness may be enhanced if Australian insurers are able to offer pre-shipment cover to FOB buyers in Australia and overseas which is

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<sup>917</sup> ALRC DP 63 para 7.32; Materials provided by Associated Marine Insurers Agents Pty Ltd: *Consultation Melbourne* 7 April 2000. It was claimed that pre-shipment cover would, in effect, become primary rather than subsidiary cover and premiums for Australian importers would have to increase because of the reduced prospects of recovery against suppliers.

not available, or not available in an effective form, in other markets such as those which require an insurable interest.

### Arguments against reform

11.76 In a 1997 submission to the Attorney-General's Department, the Insurance Council of Australia strongly opposed reform of the requirement for an insurable interest. The submission stated that the requirement for an insurable interest is dictated by the special nature of marine cargo insurance where the marine insurance contract follows moving goods through many changes of ownership. This contrasts with general insurance contracts, which are deemed cancelled when the insured disposes of the insured property. The Council considered that any attempt to reform insurable interest would bring confusion for all parties to a contract of marine insurance.<sup>918</sup>

The [marine] insurance contract follows the terms of sale. To do otherwise is to insure the consequences of poor commercial practices. This, inevitably, would be at the cost of increased premiums falling as a burden on all policy holders.<sup>919</sup>

11.77 In its submission to the present inquiry the Insurance Council of Australia stated that it continues to believe strongly that the provisions of the MIA relating to insurable interest should be retained.<sup>920</sup> Opposition to the idea of reforming the insurable interest requirement has been widely expressed but not explained in detail in consultations and submissions.<sup>921</sup>

11.78 There are several broad themes identifiable in comments and submissions received by the Commission opposing reform of the insurable interest requirement. Firstly, as reflected by the Insurance Council of Australia quoted above, concerns are expressed about the effect of reform on contracts for the international sale of goods. Reform, it is said, may 'undermine the fundamental nature of international sale contracts'.<sup>922</sup> It is said that 'a buyer should not through legislation be able to let a seller off the hook as to its obligations to the buyer'.<sup>923</sup>

11.79 This objection to reform does not withstand scrutiny. While it may be expected that the period of insurance cover will coincide with the period that the insured has the property (or bears the risk) in the goods, current insurance practices are such that the events defining the period of insurance cover and the passing of risk under the contract of sale to and from the insured may not coincide. There are

918 Insurance Council of Australia *Submission* 29 May 1997.

919 *Ibid.*

920 Insurance Council of Australia *Submission* 11.

921 eg P Grieve *Submission* 6; Law Society of WA *Submission* 7; K Carruthers *Submission* 9; Insurance Council of Australia *Submission* 11; MLAANZ *Submission* 12.

922 Law Society of WA *Submission* 7.

923 P Grieve *Submission* 6.

two distinct contracts. If the goods are lost or damaged, the insured buyer may have rights against the seller under the contract of sale or on other legal bases, and the insurer is subrogated to those rights if it pays out under the policy. Warehouse-to-warehouse clauses and FOB and C&F pre-shipment clauses are examples of insurance terms that purport to extend cover to periods beyond those during which the buyer bears the risk of the goods under standard FOB and C&F (and CIF) terms. Although it may be argued that these clauses must be read down in the light of the statutory requirement for an insurable interest, that is not necessarily clear from the face of the documents and simply begs the question of when the insurable interest arises and ceases.

11.80 Furthermore, the seller is not let off the hook unless the subrogated insurer declines to take action or, where appropriate, both the insured and the insurer decline to. Reform of the insurable interest requirement would continue to allow insurers to exercise rights of subrogation in respect of the buyer's claim in appropriate cases.<sup>924</sup>

11.81 Some insurers have distinguished so called 'trade' or 'commercial' risks from insurance risks and stated that under FOB terms where goods are clearly not shipped or there is loss prior to shipment the insured should be able to claim only against the seller as the matter is a trade dispute and 'nothing to do with insurance'. The Commission suggests that this is an artificial distinction, especially from the perspective of an insured business. While insurers may have good commercial reasons to choose not to insure certain risks of trade, this does not constitute a sufficient justification for legislatively hindering such insurance. There are many insurable risks during transit that involve commercial risks and commercial claims against third parties such as sellers and carriers. Insurers regularly insure these risks and pursue these claims under their rights of subrogation.

11.82 Those opposing reform of the insurable interest requirement also argue that the marine insurance law is different from other general insurance law because of 'the rapid succession in title to goods, as compared with general insurance contracts'.<sup>925</sup> This characteristic, it is said, 'highlights the specialist nature of marine cargo insurance'.<sup>926</sup> The Commission recognises that, generally speaking, marine cargo insurance is distinctive in this regard. However, other insurance contexts also see goods changing hands a number of times in the course of transit or the assignment of the contract of insurance.

11.83 In any event, even if there is an extended chain of owners of a particular cargo that is damaged or lost during transit, it is difficult to see how more than one of those interested parties could suffer the same pecuniary or economic loss. Only

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924 Associated Marine Insurers Agents Pty Ltd *Correspondence* 17 April 2000.

925 Law Society of WA *Submission* 7.

926 Insurance Council of Australia *Submission* 11.

one party will have paid for the goods and either not been paid by the next purchaser in line or not received the goods that it paid for. That party would be the only one entitled to claim for the value of the goods themselves as it would be the only one to have suffered economic or pecuniary loss in that respect. Other parties might suffer different forms of loss covered by different policies, and each such loss might be recoverable from the relevant insurer. For example, the owner of goods at the time of loss will presumably suffer loss equivalent to the value of the lost goods. Either that party or subsequent purchasers who did not receive the goods would also lose anticipated profits and could claim accordingly, assuming that loss of this type is in fact covered by their respective policies.

11.84 The NSW Court of Appeal in *NSW Leather* has confirmed that anticipated profits are an insurable interest under the current regime, so recovery for such profits is nothing new. Whether anticipated profits are to be covered is a commercial and underwriting consideration.

11.85 The Commission considers that objections to reform of the insurable interest requirement are largely answerable by reference to the indemnity principle from which it was derived, as potential recovery is limited to actual loss. The Commission's reforms will simply have the effect of making parties to commercial contracts think carefully about what they are agreeing to.

### The reform options

11.86 Reform of the requirement for an insurable interest has received support from Australian importers and exporters, who have emphasised the commercial benefits of obtaining effective cover of pre-shipment and post-delivery risks,<sup>927</sup> even at the cost of higher premium.<sup>928</sup> Others have agreed that reform of the insurable interest requirement merits careful consideration.<sup>929</sup>

11.87 Some of those opposed to substantive reform of the law in relation to insurable interest also accept that problems may arise with insurable interest through lack of legal understanding amongst brokers and their clients.<sup>930</sup> In particular, while cargo policies commonly contain 'warehouse to warehouse' clauses stating that risk attaches when the goods leave the seller's warehouse, the

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927 Australian exporters have noted that some overseas buyers, even though buying under CIF terms, may nevertheless refuse to pay for, or seek offsets from the exporter in respect of, goods found to be damaged on delivery to the buyer's warehouse. Just as the statutory requirement for an insurable interest may prevent the parties to a contract of insurance agreeing that pre-shipment loss related to a FOB contract will be covered, similarly it prevents them from agreeing that post-shipment loss related to a CIF contract will be covered.

928 Insured interests and lawyers *Consultation* Perth 24 November 2000; National Bulk Commodities Group *Submission 14*.

929 National Bulk Commodities Group *Submission 14*.

930 *Advisory Committee meeting* 18 December 2000.

insured does not always appreciate that an insurable interest is also required for the insurance to be effective.<sup>931</sup> There is a risk that the sale by insurers of cover on terms that may later be seen to be illusory will expose them to suit on other legal bases. In any event, insurance contracts which in law do not provide the cover that they appear to provide are clearly unsatisfactory.

11.88 In order to address the position of FOB and C&F buyers, it may not be necessary to provide for a wide reform of the insurable interest requirement. For example, it might be possible for legislative reform to provide that the parties to a contract of marine cargo insurance may deem that a buyer under a contract of sale has an insurable interest from or for a defined time, regardless of when risk or property is to pass under the contract of sale. A narrower reform, which received some support in submissions, involved amending the MIA to provide expressly that there exists an insurable interest where an insured bears the risk of goods noted on an invoice or bill of lading not actually being loaded.<sup>932</sup> Such an approach may avoid any unforeseen effects on the marine insurance industry of broader reform of the insurable interest requirement.

11.89 In its Discussion Paper the Commission asked whether the MIA should be consistent with the ICA in relation to the requirements for an insurable interest and what problems, if any, might be caused by the application of an economic loss test.<sup>933</sup> Submissions have not disclosed any particular problems associated with these reforms. The insurable interest provisions of the ICA do not seem to have given rise to significant controversy, either in relation to contracts of insurance related to contracts for the sale of goods or in other contexts. A recent case law search revealed only three cases dealing with s 16 or s 17 of the ICA.<sup>934</sup> The enactment of the ICA has not produced extensive litigation or uncertain case law principles.

931 eg that the Institute transit clause (ICC(A) cl 8.1) is subject to ICC(A) cl 11.1, which states that ‘In order to recover under this insurance the Assured must have an insurable interest in the subject-matter insured at the time of loss’, reiterating s MIA 12(1).

932 As suggested by Associated Marine Insurers Agents Pty Ltd *Correspondence* 17 April 2000; K Carruthers *Submission 9*.

933 ALRC DP 63 ch 7 Questions 34–6.

934 See *Pacific Dunlop Limited v Maxitherm Boilers PL* (1997) 9 ANZ Ins Cases ¶¶61-357 in which Teague J in the Supreme Court of Victoria noted uncertainty as to whether s 17 could be relied upon by a non-party insured; *Howard v Australian Jet Charter Pty Ltd* (1991) 6 ANZ Ins Cases ¶¶61-054 in which Hill J in the Federal Court held that, by virtue of ICA s 16 and 17, a company that had contracted to maintain and crew an aircraft could not be said to have interest in a contract of insurance covering loss from damage to that aircraft; *Advance (NSW) Insurance Agencies Pty Ltd v Matthews* (1988) 12 NSWLR 250 in which Samuels JA found that under ICA s 17 a husband had an economic, and therefore insurable, interest in his wife’s clothing and other personal effects.



11.90 In practice, a person who suffers a pecuniary or economic loss within the meaning of ICA s 17 is likely to have an insurable interest under the common law.<sup>935</sup>

11.91 The Commission concludes that the preferable course is to abolish the requirement for an insurable interest and replace MIA s 10–12 with provisions in the terms of ICA s 16–17.

11.92 The purpose of doing so is simply to permit purchasers of insured goods to obtain insurance to cover their exposure to loss if they pay for the goods before they acquire an insurable interest in them under the contract of sale. Whether such cover is in fact commercially available is a matter for the marine insurance market. The availability under the MIA of such cover does not in any way undermine the basic principle that insurers are only liable to indemnify an insured for a loss proximately caused by an insured peril and are not liable for a loss which is not so caused. MIA s 61(1) makes this clear. The mere fact that the insured has suffered economic or pecuniary loss does not entitle it to recover under the policy. The loss must satisfy all other conditions of the cover; for example, it must occur during the period of cover and not arise from a cause excluded by the contract or under the MIA.

11.93 Insurers are free to decline to insure buyers for losses occurring prior to the time that they acquire an insurable interest in the insured property but that can be made clear in the express terms of the insurance contract. One of the Commission's concerns is that the use of warehouse-to-warehouse clauses or pre-shipment clauses, which are express and may the insured give a certain as to the extent of cover, may not accurately state the extent of cover if they are subject to limitations based on the requirement for an insurable interest, which is not apparent on the fact of the contract.

11.94 In the Discussion Paper the Commission noted that MIA s 13–21, which provide guidance on various categories of insurable interest, may be inadequate for modern use and benefit from redrafting. While this suggestion received some support in submissions,<sup>936</sup> the Commission does not make any recommendation in this regard, with one exception.<sup>937</sup> However, if the Commission's recommendation to abolish the requirement for an insurable interest is adopted, MIA s 13–21 become unnecessary and should also be repealed.

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935 Especially if Australian courts were to follow the lead of recent decisions in the UK and Canada such as *Constitution Insurance Co of Canada v Kosmopoulos* (1987) 34 DLR (4th) 208; *Sharp and Roarer Investments Ltd v Sphere Drake Insurance plc*, *Minster Insurance Co Ltd and EC Parker and Co Ltd (The Moonacre)* [1992] 2 Lloyd's Rep 501 (see para 11.11–11.12).

936 ALRC DP 63 para 7.46; K Carruthers *Submission 9*.

937 See para 11.99–11.102 in relation to MIA s 16 and bottomry.

11.95 MIA s 57 deals with the purported assignment of a policy by an insured who has lost or parted with its insurable interest. It becomes redundant and should be repealed. MIA s 90(3)(c)–(d) both rely on the concept of insurable interest and should also be repealed.

## **Recommendations**

**Recommendation 28.** MIA 10–12 should be amended to be consistent with ICA s 16–17 in relation to the requirements for an insurable interest. That is, the MIA should provide that

- (1) a contract of marine insurance is not void by reason only that the insured did not have an interest in the subject matter of the contract at the time when the contract was entered into; and
- (2) where the insured under a contract of marine insurance has suffered a pecuniary or economic loss by reason of damage to the insured property, the insurer is not relieved of liability under the contract by reason only that the insured did not have an interest at law or in equity in the property.

**Recommendation 29.** MIA s 32–21, 57 and 90(3)(c)–(d), which rely on the concept of insurable interest, should be repealed as a consequence of the abolition of the requirement for an insurable interest.

## **Alternative recommendations**

11.96 In acknowledgement of the strength of the opposition against the abolition of the requirement for an insurable interest, the Commission considers that two alternative amendments should be made to the MIA if the Commission's principal recommendations are not adopted.

### **Purchasers' insurable interest**

11.97 The first alternative recommendation is the insertion of a new s 19A in the MIA to provide that buyers of insurable property acquire an insurable interest in insurable property by no later than the time when they pay of the property, or when they become bound to pay for the property provided that they do in fact subsequently pay for it.

11.98 This would mean that there would be no legal impediment in principle to the insurance of goods prior to loading aboard a ship or at any other early stage of

transit. The purchaser can seek cover for any loss of the value of the goods or any profit that it might earn from them once with the risk attaching as soon as the goods are paid for, thus obtaining seamless cover without the need to resort to contractual terms of dubious status. Whether it can in fact obtain such cover, and at what cost, is a matter for the market.

### **Bottomry and respondentia**

11.99 Section 16 of the MIA provides

16. The lender of money on bottomry or respondentia has an insurable interest in respect of the loan.

11.100 Bottomry is a charge over a ship (that is, its hull or bottom) given by the master to secure money for necessities so that the voyage can continue. The charge is created by a master who is unable to make contact with the shipowner by virtue of an agency of necessity. Respondentia is a similar charge over the ship's cargo.<sup>938</sup>

11.101 These concepts were important when global communications were poor. With modern communications and international funds transfer it is generally accepted that these arrangements are obsolete and reference to them can be removed from the MIA. The Discussion Paper asked whether there was a need to retain MIA s 16 to ensure that a current holder of a bottomry or respondentia bond retained an insurable interest in the ship or cargo.<sup>939</sup> The Discussion Paper also asked whether or not such an interest would be covered by s 11(2), which is the general statement of when a person is interested in a marine adventure and therefore has an insurable interest under s 11(1).

11.102 Consultations did not disclose any reason for retaining these concepts in the MIA and submissions generally were in favour of repealing these provisions.<sup>940</sup> One submission noted that the insurable interest of the lender of money on bottomry or respondentia would be covered by MIA s 11(2).<sup>941</sup>

11.103 One alternative to repealing s 16 would be to amend it to bring the range of secured interests up to date and to generalise the interests referred to so that the old forms of security would still be covered but modern forms of security would also be covered without the need to specify them, bearing in mind that mortgages of insured property are expressly referred to in s 20. This has already been adopted in s 15 of the Canadian MIA, which reads

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938 M Davies and A Dickey *Shipping Law* The Law Book Company Sydney 1990, 112–15.

939 ALRC DP 63 Question 45.

940 D Chaplin *Submission 3*; Law Society of WA *Submission 7*; K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*.

941 K Carruthers *Submission 9*.

15. A lender of money on security of a ship or a ship's cargo has an insurable interest in respect of the loan.

11.104 The Commission recommends that, if s 16 of the MIA is retained, it be amended in terms of s 15 of the Canadian Act but expanded to cover secured loans over all insurable property.

**Recommendation 30.** If recommendation 28 is not adopted and the requirement for insurable interest is retained, a new provision should be inserted into the MIA providing that a purchaser of insurable property acquires an insurable interest in that property by no later than the time when it pays for the property or when it becomes bound to pay for the property provided that it subsequently pays for it.

**Recommendation 31.** If recommendation 28 is not adopted and the requirement for insurable interest is retained, MIA s 16 should be amended to cover secured loans over insurable property generally, not just bottomry and respondentia.

## 12. Subrogation

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### Introduction

12.1 On payment of a total or partial loss of the insured property, the insurer is subrogated to the rights and remedies of the insured in respect of the subject matter insured.<sup>942</sup> In particular, the insurer may bring an action in the insured's name against any third party who has caused the loss. The Commission has considered a number of options for reform of the MIA provisions dealing with subrogation.

### Control of subrogated proceedings

12.2 Levingstons submitted that the MIA should expressly provide for the appointment and involvement of a lawyer appointed by the insured in proceedings for recovery.<sup>943</sup> This suggestion received no comment in other submissions.

12.3 David Kelly and Michael Ball state that it is well settled that there is an obligation on whoever controls the recovery proceedings against a third party to have proper regard to the interests of the other party to the insurance contract.<sup>944</sup>

12.4 An insurer must not act in such a way as to prejudice the insured. For example, *Arnould's Law of Marine Insurance and Average* states that if the insurer were to settle a claim in the insured's name against a third party on unreasonably unfavourable terms where the third party was liable for an amount greater than the measure of indemnity under the policy, the insured could have a claim for damages

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942 MIA s 85.

943 Levingstons Solicitors *Submission 1*: See ALRC DP 63 para 8.67–8.68. There is no similar provision in the ICA or in any other legislation of which the Commission is aware.

944 D Kelly and M Ball *Principles of Insurance Law in Australia and New Zealand* Butterworths Sydney 1991, 509 citing *Yorkshire Insurance Co v Nisbet Shipping Co* [1962] 2 QB 330.

against the insurers.<sup>945</sup> Similarly, if the insurer, while acting in defence of a claim brought by a third party against the insured, settled the claim on terms unduly unfavourable to the insured where, for example, a good defence existed, a claim by the insured against the insurer may lie.

12.5 This rule is said to be an aspect of the doctrine of subrogation and may also have a basis in the duty of utmost good faith.<sup>946</sup> Section 13 of the ICA implies a duty of utmost good faith into every contract of insurance covered by the ICA. Professor Sutton states that this provision requires both the insured and the insurer to act reasonably towards each other in respect of claims by way of subrogation and settlement of such claims and that even in other contracts of insurance (such as a contract of marine insurance), a similar term will be implied in the contract.<sup>947</sup>

12.6 At all times the insured is entitled to appoint lawyers at its own expense to protect its interests if, for example, it feels that the insurer is not doing so adequately or if there are significant uninsured losses, or for any other reason. There is no justification for the costs of such additional representation falling on the insurer.

12.7 The Commission has concluded that the current state of the law and practice in this area is such that this suggested reform of the MIA is not warranted. In any event, to the extent that the conduct of the parties is dictated by the strictures of good faith, the recommended enhancements to the concept of good faith should provide some further support for insureds (or insurers) who feel that the other party is acting unreasonably in relation to any third party action in the name of, or against, the insured.

## **Recovery of money from third parties**

12.8 Another reform option relates to the disposition of money recovered in an action against a third party. The MIA is silent on this question except to say that, where the insured is underinsured, the insured is deemed to be its own insurer in respect of the uninsured balance.<sup>948</sup> The position in marine insurance is otherwise governed by the common law.

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945 M Mustill and J Gilman *Arnould's Law of Marine Insurance and Average* 16th ed vol I Stevens & Sons London 1981, 1097.

946 D Kelly and M Ball *Principles of Insurance Law in Australia and New Zealand* Butterworths Sydney 1991, 509.

947 K Sutton *Insurance Law in Australia* 3rd ed LBC Information Services Sydney 1999, 1276 citing *Lord Napier and Etterick v Hunter* [1993] AC 713, 736.

948 MIA s 87.

12.9 At common law the general principle is that where recovery is made from a third party, the insured is entitled to the money recovered only until fully indemnified for its loss.<sup>949</sup> Where the insured has not been fully indemnified under the policy, the following principles apply.

- If the insurer takes proceedings against the third party, any money recovered by it over the amount it paid to the insured belongs to the insured, and the insurer cannot even claim any amount on account of its costs.
- If the insured takes proceedings against the third party, it is entitled to deduct any reasonable costs from the sum recovered before accounting to the insurer for any amounts in excess of full indemnity.
- As a qualification to the first of these propositions, it has been held that the insured is entitled to any windfall profit resulting from the proceedings (for example, as a result of exchange rate fluctuations between the time of loss and recovery against the third party).<sup>950</sup>

12.10 In effect, the insurer can only recover the amount it paid the insured under the contract of insurance.

12.11 Section 67 of the ICA made substantial reforms to the common law position applicable to non-marine insurance. The basic effect of s 67 is that where the insurer exercises a right of subrogation and recovers an amount from a third party, the insured is entitled to that amount from the insurer less the administrative and legal costs connected with the recovery action with the following provisos (unless the contract expressly provides otherwise).

- The insurer is entitled to retain an amount equal to the amount that it has paid to the insured under the insurance contract and the insured receives the excess above this amount (if any).<sup>951</sup> In other words, if the amount paid to the insured under the insurance contract and the amount recovered<sup>952</sup> together do not exceed the insured's loss, the insured is entitled to the amount recovered less the insurer's administrative and legal costs and the amount already paid to it by the insurer.

949 D Kelly and M Ball *Principles of Insurance Law in Australia and New Zealand* Butterworths Sydney 1991, 512.

950 F Marks and A Balla *Guidebook to Insurance Law in Australia* 3rd ed CCH Sydney 1998, 524-525 citing *Yorkshire Insurance Co v Nisbet Shipping Co* [1962] 2 QB 330.

951 ICA s 67(2)(a).

952 After deducting the insurer's administrative and legal costs.

- The insured is not entitled to any further money once it has received an amount equal to its loss either under the insurance contract, from the money recovered or both, and the insurer retains the balance.<sup>953</sup> If the insured is fully indemnified for its loss from the policy alone, it is not entitled to any of the money received from the third party.<sup>954</sup>

12.12 One view is that the provisions of ICA s 67 ‘inject certainty’ into an area that has been ‘devoid of specific authority’.<sup>955</sup> However, that certainty can be regarded as partial only. Section s 67 has been criticised for not referring to the situation where the insured brings the action against the third party and because the working of s 67(2) gives the insurer the benefit of a recovery in excess of the insured’s actual loss, allowing the insurer to make a profit, reversing the position at common law.<sup>956</sup>

12.13 The Discussion Paper asked whether the provisions of the MIA dealing with subrogation should be amended by including provisions dealing with the recovery by an insured of surplus money obtained by the insurer exercising rights of subrogation and, in particular, whether there is a need for provisions similar to those in ICA s 67.

12.14 This suggestion received no support in submissions. Submissions generally rejected the notion that the MIA needs reform related to subrogation.<sup>957</sup> For example, the Insurance Council of Australia stated

Broadly, ICA does not believe that there is any need to alter the provisions of the MIA dealing with subrogation. Australian marine insurers and marine insurance practitioners worldwide are very familiar with the issues of subrogation. It remains an important aspect for insurers in recovering from negligent carriers, whose liability is recognised by international conventions and legislated in the Carriage of Goods by Sea Act.<sup>958</sup>

12.15 The Commission agrees that subrogation is central to the law of all insurance. Indeed, there was never any suggestion that the concept of subrogation generally would be removed or altered. The only issues raised were those

<sup>953</sup> ICA s 67(2)(b).

<sup>954</sup> See F Marks and A Balla *Guidebook to Insurance Law in Australia* 3rd ed CCH Sydney 1998, 526. This is a reiteration of the common law position except that s 67(4) provides that the amount recovered is to be construed as the amount recovered less the administrative and legal costs incurred in connection with recovery of the amount.

<sup>955</sup> F Marks and A Balla *Guidebook to Insurance Law in Australia* 3rd ed CCH Sydney 1998, 528.

<sup>956</sup> D Kelly and M Ball *Principles of Insurance Law in Australia and New Zealand* Butterworths Sydney 1991, 513. See ALRC DP 63, para 8.69–8.73.

<sup>957</sup> P Grieve *Submission 6*; K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*; MLAANZ *Submission 12*.

<sup>958</sup> Insurance Council of Australia *Submission 11*.



mentioned by Levingstons and the disposition of money recovered from third parties.

12.16 In relation to the former, the Commission has concluded that the established principles and the obligations of utmost good faith, particularly if amended as the Commission has recommended elsewhere in this Report (see recommendation 20–21), provide the insured with adequate protection and further statutory reform is not required.

12.17 However, the disposition of money received from third parties is another area where there is divergence between the MIA and the ICA. There seems to be no reason in principle why this should be the case. The Commission therefore recommends that the provisions of ICA s 67 be enacted into the MIA as a new s 85A, but modified and extended to meet the criticisms of ICA s 67 and to provide a comprehensive scheme for the disposition of money recovered from third parties. The Commission's recommendations are in accordance with the following statements of principle setting out the order or priority in which the recovered money should be distributed. The following statements of principle are subject to the express terms of the contract.

- Firstly, the party taking the recovery action should be entitled to reimbursement for the administrative and legal costs of that action from any moneys recovered. This reflects the effect of ICA s 67(4) and the common law, so far as they go. If both parties contribute, they should both be reimbursed, or share in the reimbursement pro rata if there is insufficient recovered money to reimburse both in full.
- There are then three possibilities depending on who has funded the recovery action.
  - (a) If the insurer funds the recovery action pursuant to its rights of subrogation, it is entitled to an amount equal to the amount that it has paid to the insured under the insurance contract. This reflects the intention of ICA s 67(1) and s 67(2)(a). The insured is then entitled to any further amount that may be required so that it ultimately recovers from the insurer under the insurance contract or the third party in the recovery action, or both in combination, the full amount of its loss (not just the measure of indemnity under the policy). This entitlement does not diminish the insured's right to receive payment promptly under the policy in accordance with its terms and the insurer's obligation to pay promptly, subject to any contrary agreement between the parties.

- (b) If the insured funds the recovery action, the order in the preceding paragraph is reversed. The insured is entitled to retain an amount so that the total that it receives from the recovery action and under the policy is equal to its total loss. The insurer is entitled at this point to an amount equal to the amount that it has paid to the insured under the insurance contract.
- (c) If the action is funded jointly by both insurer and insured, they are entitled to the same amounts as those referred to in (a) and (b) above, pro rata if there are insufficient funds to reimburse them in full.
- Thirdly, any excess or windfall recovery is then distributed to both parties in the same proportions as they contributed to the administrative and legal costs of the recovery action. Thus the party (or parties) shouldering the cost and risk of the recovery action for the benefit of all concerned receives the benefit of the windfall. This would most commonly be the insurer, but the insurer only gets this benefit after the insured has received full recovery for all its losses as the insured would have been entitled to these losses as damages from the third party as a matter of principle whether or not there was any insurance in place.
- Finally, any separate or identifiable component in respect of interest should be paid to the parties in such proportions as fairly reflects the amounts that they have each recovered and the periods of time for which they have each lost the use of their money.

12.18 Although not strictly within its terms of reference, the Commission would also recommend that the ICA s 67 be amended in the same way.

**Recommendation 32. The MIA should be amended to provide that, subject to any agreement between the insurer and the insured, money recovered from third parties either by the insurer under its rights of subrogation or by the insured is distributed in the following order:**

- (1) The party or parties funding the recovery action are reimbursed for the administrative and legal costs of that action, pro rata if there is more than one such party and there are insufficient funds to reimburse them in full.**

***Recommendation 32 (continued)***

- (2) (a) **If the insurer has funded the recovery action, it is entitled to retain an amount equivalent to the amount it has paid to the insured under the contract of marine insurance. The insured is then entitled to be paid an amount so that the total amount that it receives under the contract of marine insurance and from the recovery action equals its total loss.**

(b) **If the insured has funded the recovery action, it is entitled to retain an amount so that the total amount that it receives under the contract of marine insurance and from the recovery action equals its total loss. The insurer is then entitled to be paid an amount equal to the amount that it has paid under the contract of marine insurance.**

(c) **If the insurer and the insured have both funded the recovery action, they are entitled to the amounts referred to in (a) and (b) above, pro rata if there are insufficient funds to reimburse them in full.**
- (3) **Any excess or windfall recovery is paid to the parties in the same ratio that they contributed to the administrative and legal costs of the recovery action.**
- (4) **Notwithstanding the statements of principle above, any separate or identifiable component in respect of interest should be paid to the parties in such proportions as fairly reflect the amounts that each has recovered and the periods of time for which each lost the use of its money.**

**Contracts affecting rights of subrogation**

12.19 The Discussion Paper noted that there may be other issues related to subrogation which should be examined in the context of the review of the MIA and requested comments on other possible reforms.

12.20 During consultations the Commission's attention was drawn to one such issue, which relates to the effects of an insured party contracting to limit or exclude a third party's liability for subsequent losses covered by the contract of insurance.<sup>959</sup> For example, a shipowner may indemnify a ship repairer or a port authority for

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959 Gault Armstrong & Kemble *Submission 16*.

liability for damage to an insured ship, or a cargo owner may indemnify a carrier for damage to the cargo.<sup>960</sup> These third party contracts may be entered into before or after the contract of insurance. In some cases, such as towage contracts, the contracts are effectively contracts of adhesion with the shipowner having little, if any, power to alter the tow operator's standard terms, which as a matter of course include a complete indemnity in favour of the tow operator. In the event of loss, these contracts rule out the exercise of rights of subrogation by the insurer.

12.21 It has been said that in some cases insurers then seek to rely on the insured's act in entering such a contract as a breach of an express or implied term of the insurance contract. For example, P&I rules commonly provide that liability arising under the terms of an indemnity given or made by the insured member are covered only to the extent that such cover has been agreed by the managers of the P&I Club.<sup>961</sup>

12.22 This situation must be distinguished from cases where the insured's actions or words after a loss has occurred have the effect of compromising its claim (and therefore the insurer's rights) against a third party or compromising its defence to (and therefore the insurer's ability to resist) a third party claim brought against the insured. Actions or comments of this nature are typically contrary to express terms of insurance contracts and could well be in breach of the insured's obligations of good faith. The Commission received no comment in relation to these issues in submissions or consultations.

12.23 In its 1982 report *Insurance Contracts* (ALRC 20), the Commission noted that, in the absence of similar terms in the contract dealing explicitly with contractual exclusions of liability, the liability of the insurer depends on the terms that a court will be willing to imply into the contract. In *SGIC v Brisbane Stevedoring*<sup>962</sup> the High Court rejected an insurer's argument that the insured was under a duty not to do anything to prevent contribution being recoverable from a third party. However, the decision left open the possibility that in some circumstances the insured might be in breach of an implied obligation not to enter into any arrangements which might prevent rights from arising.<sup>963</sup> The Commission stated

960 Examples of such contracts are said to include: UK Standard Towage Conditions; Shiprepairers/Slipway Operators Disclaimer Clauses; Bill of Lading/Airway Bills; Supplytime 89 Charterparty; Towage Contracts Under Towcon/Towhire: Gault Armstrong & Kemble *Submission 16*.

961 eg The Shipowners' Mutual Protection and Indemnity Association (Luxembourg) Class 1 Rules 2000, Rule 2, section 11.

962 (1969) 123 CLR 228.

963 See ALRC 20 para 307–8.

No clear criterion of the relevant circumstances emerges from the judgments. The insured may therefore prejudice his entitlement to recovery by engaging in conduct which is not specifically forbidden and which, at least in some circumstances, may appear to the justifiable, perhaps even required, by commercial practice. The owner of a small business cannot be expected to know when it is and when it is not permissible for him to sign an agreement which excludes liability for negligence by service contractors. If an insurer wishes to protect itself against the additional burden which results from the loss of subrogation to 'potential' rights, it should be required to insert a special term to that effect in its policies. It should also be required to bring the term to the attention of its client at the time of entering into the contract of insurance. It should not be allowed to avoid this obligation by relying on the duty of disclosure.<sup>964</sup>

12.24 Section 68 of the ICA was subsequently enacted to deal with contracts affecting rights of subrogation. It states as follows.

68(1) Where a contract of general insurance includes a provision that has the effect of excluding or limiting the insurer's liability in respect of a loss by reason that the insured is a party to an agreement that excludes or limits a right of the insured to recover damages from a person other than the insurer in respect of the loss, the insurer may not rely on the provision unless the insurer clearly informed the insured in writing, before the contract of insurance was entered into, of the effect of the provision.

(2) The duty of disclosure does not require the insured to disclose the existence of a contract that so limits the insured's rights.

12.25 One submission suggested that the MIA should be amended to include an equivalent of ICA s 68(2).<sup>965</sup> While the law applying to marine insurance contracts, based on *SGIC v Brisbane Stevedoring*,<sup>966</sup> makes it clear that entering contracts affecting rights of subrogation will not usually breach an implied term of the contract of insurance, this fact is sometimes not recognised by marine insurers, for example where such arrangements are entered into by the insured in order to gain access to slipways and towage.<sup>967</sup>

12.26 Some marine brokers negotiate the inclusion in marine insurance contracts of a 'waiver and release' clause that expressly permits the insured to enter contracts releasing third parties from liability without prejudicing the insured's rights of recovery against the insurer.<sup>968</sup> The existing law appears to indicate that terms prohibiting such contracts are unlikely to be implied into contracts of insurance unless the particular indemnity arrangements are an 'abnormal or unusual incident'<sup>969</sup> of the type of transaction between the insured and the third party.

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964 ALRC 20 para 308.

965 Gault Armstrong & Kemble *Submission 16*.

966 (1969) 123 CLR 228.

967 *Broker Consultation* Perth 23 November 2000.

968 Material provided by broker: *Broker Consultation* Perth 23 November 2000.

969 See *SGIC v Brisbane Stevedoring* (1969) 123 CLR 228, 258 (Kitto J).

12.27 The Commission appreciates these concerns. Although most contracts governed by the MIA are business-to-business transactions often involving well informed insured parties, the Commission's consultations have demonstrated that there is some misunderstanding of the position. ICA s 68 does not prevent insurers from relying on exclusions in third party contracts in order to reduce their liability under the insurance policy; it merely requires them to inform the insured clearly of any such provisions in the policy so that the insured can make an informed decision about its commercial and insurance arrangements.

12.28 Accordingly, the Commission recommends that ICA s 68 be re-enacted in the MIA as a new s 85A.

**Recommendation 33. ICA s 68 should be re-enacted in the MIA as a new s 85A to provide that**

- (1) the insurer cannot rely on a term of a contract of marine insurance that has the effect of limiting or excluding the insurer's liability under the contract of marine insurance because the insured is party to an agreement with a third party that limits or excludes its rights to recover damages from the third party unless the insurer clearly informed the insured of that term before the contract of marine insurance was concluded and**
- (2) such agreements with third parties do not have to be disclosed by the insured before the contract of marine insurance is concluded.**

## **13. Intermediaries**

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### **Introduction**

13.1 One element in the legal patchwork governing insurance contracts is the law relating to insurance agents and brokers. Those operating in marine insurance and in areas of insurance covered by the ICA are presently subject to the *Insurance (Agents and Brokers) Act 1984* (Cth) (IABA) although, it seems, to varying degrees.

13.2 The IABA applies to all contracts of insurance governed by Australian law, including those covered by the MIA.<sup>970</sup> The IABA deals with issues such as the registration of insurance brokers and, of particular relevance, with payments to and disclosure by agents and brokers. The MIA also contains provisions dealing with insurance agents and brokers: s 25–26 (disclosure and misrepresentation), s 58 (payment of premium and issue of policy) and s 59–60 (policy effected through a broker). The ICA does not deal with insurance intermediaries in any detail at all as this has been left to the IABA.

### **Inconsistency between MIA and IABA**

13.3 There is potential for inconsistency between the provisions of the MIA relating to brokers and agents and the IABA. The IABA states that it is not intended to override other legislation unless this is expressly stated<sup>971</sup> and any inconsistency is presumably to be resolved in favour of the MIA where the construction of the IABA does not ‘expressly or by necessary intendment’ require the contrary. The words of the legislation are perhaps unclear and their effect subject to debate as it is uncertain when the necessary intendment to override existing legislation arises.

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970 IABA s 6.

971 IABA s 5.

13.4 Submissions have noted that the provisions of the MIA dealing with brokers are not consistent with the IABA.<sup>972</sup> Submissions suggest that practitioners and the industry infer that the MIA prevails where there is inconsistency. Problems include conflict between insurers and brokers where some policies fall under the ICA (and therefore the IABA) and others under the MIA.<sup>973</sup> Furthermore, the MIA makes the broker liable to the insurer for the premium whether or not this has been paid whereas the IABA does not when appropriate notice has been given.<sup>974</sup> One submission suggests the MIA provisions dealing with brokers should remain unaltered because of the degree of integration with the UK market.<sup>975</sup> Others believe the situation needs rationalising and that the MIA should follow the IABA.<sup>976</sup>

13.5 The Commission sees no reason in principle why the conduct of the business of marine insurance (as distinct from the content of the contract) should be different from that of non-marine general insurance. The IABA provides a detailed, considered regime for the regulation of the insurance intermediaries whereas MIA s 58–60 do not. The Commission considers that the IABA (and its successor legislation) should apply to marine insurance.

## CLERP 6 and the IABA

13.6 The federal government is currently undertaking reform of the regulation of financial services, known as the Corporate Law Economic Reform Program 6 (CLERP 6). The proposed changes will be implemented by the Financial Services Reform Bill (FSRB).<sup>977</sup> Key aspects of the FSRB include the uniform regulation of all financial products and a single licensing framework for all financial service providers.<sup>978</sup> A ‘financial product’ is specifically defined to include a contract of insurance.<sup>979</sup> The FSRB will replace the current licensing requirements in the IABA and will require insurance agents and brokers to be licensed as financial service providers.<sup>980</sup>

972 P Grieve *Submission 6*, Insurance Council of Australia *Submission 11*, MLAANZ *Submission 12*, Gault Armstrong & Kemble *Submission 16*.

973 P Grieve *Submission 6*, Insurance Council of Australia *Submission 11*.

974 MIA s 59(1). Although MIA s 59(2) provides a lien for the broker against the policy, this is only of assistance to the broker if a claim is lodged: Gault Armstrong & Kemble *Submission 16*.

975 MLAANZ *Submission 12*.

976 P Grieve *Submission 6*.

977 The government had intended to enact the legislation by 1 January 2001. However, it has been delayed as a consequence of lack of agreement between the states and the Commonwealth on the referral of power to the Commonwealth Parliament to enact the proposed FSRB: J Hockey ‘Financial Services Reform Bill Update’ *Press Releases* 27 June 2000, 29 November 2000 and 21 December 2000.

978 Other key aspects of the draft legislation are minimum standards of conduct for financial service providers, uniform disclosure obligations, and flexibility for authorisation of market operators: J Hockey ‘Revolution in Financial Services’ *Press Release* 11 February 2000.

979 Financial Services Reform Bill cl 764A(1)(d).

980 Financial Services Reform Bill Part 7.5; The Treasury *Financial Services Reform Bill — Commentary on the Draft Provisions* Canberra February 2000, 79.



13.7 The FSRB will repeal the IABA. Although the FSRB defines a contract of insurance as a financial product, it specifically excludes certain types of insurance contracts from the definition of financial product because other regulatory regimes apply to them.<sup>981</sup> One of these specific exclusions is insurance in relation to which the MIA applies.<sup>982</sup> Although it is true to say that marine insurance is governed by its own statutory regime, that regime does not deal comprehensively with the matters covered by the IABA and the FSRB. The exclusion of marine insurance from the FSRB produces the anomalous result that, although the new licensing regulations will apply to brokers who deal in marine insurance, all other aspects of the new scheme will not.

13.8 The Insurance Council of Australia considers that the FSRB is the appropriate legislation for dealing with issues of payment and disclosure.<sup>983</sup> In order to remove the regulatory gap in the conduct of agents and brokers relating to marine insurance and non-marine insurance, the Commission recommends that the IABA be amended to make it clear that it governs the conduct of marine insurance brokers and agents and that MIA s 59 and 60 be repealed simultaneously. Given the anticipated enactment of the FSRB later in 2001, it might be easier and more efficient to amend the FSRB to remove the exclusion of marine insurance and to repeal MIA s 59 and 60 from the date on which the FSRB (or the relevant portions of it) takes effect.

13.9 If, however, that change is not made to the IABA or the FSRB, the MIA should be amended to introduce the same regulatory scheme into it as will be set out in the FSRB when it becomes law. It is, however, undesirable to have a lengthy set of provisions repeated in two pieces of legislation with the attendant risk that they may become inconsistent at some time in the future.

13.10 Section 58 of the MIA serves a different purpose. It provides that, unless otherwise agreed, the insured's duty to pay the premium and the insurer's duty to issue the policy are concurrent obligations but that the policy does not have to be issued until the premium has been paid or tendered. It is in some respects logically related to the provisions relating to the minimum requirements of the policy found in MIA s 28–30. After the repeal of s 59 and 60, it will be somewhat disconnected from the other portions of the Act to which it is related. However, consistently with the Commission's intention not to make drafting changes for their own sake and the Commission's recommended change to s 28, which will include an express reference to s 58, the Commission does not see any need to modify s 58 or its location within the MIA.

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981 The Treasury 'Financial Products, Service Providers, and Markets — An Integrated Framework Implementing CLERP 6' *Consultation Paper* Canberra March 1999, 119.

982 Financial Services Reform Bill cl 965A(h).

983 Insurance Council of Australia *Submission 11*.

## Payments

13.11 Both the IABA and the MIA contain provisions relating to payments.<sup>984</sup> Clauses 945A to 945C of the FSRB carry across the effect of IABA s 14, under which the insurer rather than the insured bears the risk of the loss of funds held by an insolvent insurance broker. Clause 945B of the FSRB deems funds paid by the insured to a licensed financial services provider who is not an insurer (ie a broker) to be a discharge of the insured's liability to the insurer. However, payments by an insurer to a licensed broker of money payable to an insured is not a discharge of the insurer's liability to the insured.

13.12 IABA s 27 sets out in detail a broker's duties in relation to premiums. These duties include payment of premiums to the insurer within set times, notification to the insurer of non-payment of premium by the insured, and the return of premium to the insured within set times where the risk has not been accepted. The duties of insurance brokers in relation to premiums currently contained in IABA s 27 will be carried across to the new regime by way of regulations.<sup>985</sup>

13.13 MIA s 58–60 do not deal with the details of the payment of premium. If the Commission's recommendation that marine insurance be included in the FSRB is not implemented, the MIA should be amended to replicate within that Act the regulatory scheme that will be found in the FSRB.

## Disclosure and representations

13.14 Both the MIA and the IABA contain provisions relating to disclosure and representations by agents and brokers.<sup>986</sup> Under s 24–26 of the MIA, a material non-disclosure or misrepresentation by an insured or its agent entitles an insurer to avoid the contract. Section 13 of the IABA provides for the imprisonment of intermediaries who make false or misleading statements with intent to deceive an insurer.

13.15 The FSRB does not yet contain market misconduct provisions, offences, and penalties.<sup>987</sup> Part 7.8 of the FSRB sets out a financial product disclosure regime. The disclosure regime will replace a range of existing disclosure regimes for

984 MIA s 58–60; IABA s 14. See ALRC DP 63 para 8.55 and 8.56.

985 The Treasury *Financial Services Reform Bill — Commentary on the Draft Provisions* Canberra February 2000, 123.

986 See ALRC DP 63 para 8.57 and 8.58. The 'disclosure' sections of the MIA (s 24–6) deal with the duty of utmost good faith which requires the parties to disclose every material circumstance. This is different from the 'disclosure' sections of the IABA (s 16–17), which relate to the obligations of insurance intermediaries and brokers to inform insureds when they are acting under the authority of the insurer.

987 The Treasury *Financial Services Reform Bill — Commentary on the Draft Provisions* Canberra February 2000, 3.

financial products, and will supplement disclosure requirements for insurance under the ICA.<sup>988</sup> However, as the FSRB will repeal the IABA, and ‘insurance to or in relation to which the *Marine Insurance Act 1909* applies’ is excluded from the FSRB,<sup>989</sup> the only sanctions for non-disclosure or misrepresentation would rest with the MIA, or an untested blend of other statutory and common law remedies.

13.16 As stated above, the Commission is of the view the IABA should apply to marine insurance. If the enactment of the FSRB proceeds and repeals the IABA, there is no reason for the FSRB to distinguish between marine and non-marine insurance. The Commission recommends that the FSRB be amended to remove the provisions which exclude insurance in relation to which the MIA applies.

Recommendation 34. **The *Insurance (Agents and Brokers) Act 1984* (IABA) and its successor provisions in the Financial Services Reform Bill should be amended to remove the provisions which exclude from their operation insurance in relation to which the MIA applies. As a consequence, MIA s 59 and 60 should be repealed with effect from the date on which the changes to the IABA, or the relevant portions of the Financial Services Reform Bill, take effect.**

988 The Treasury *Financial Services Reform Bill — Commentary on the Draft Provisions* Canberra February 2000, 129–130.

989 See para 13.7.



## 14. Choice of law and jurisdiction

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### Introduction

14.1 This chapter examines issues relating to freedom of contract and contractual choice of law and jurisdiction in the context of reform of the MIA. The MIA applies to all contracts of marine insurance but the parties are free in most respects to contract on different terms. The tradition in relation to marine insurance contracts has been to treat ‘flexibility as more important than uniformity’.<sup>990</sup> One key issue in considering reform of the MIA is the extent to which this flexibility should be retained or modified.

14.2 Jurisdiction and choice of law rules are also relevant factors in considering reform of the MIA. By choosing a foreign forum or a foreign law, the parties to contracts of marine insurance may be able to evade the remedial effect of any reforms to the MIA. In particular, by specifying that the law of another country will apply to the interpretation of the contract, an Australian insurer may be able to avoid the effect of reforms broadly favourable to insureds in areas such as breach of warranties and the duty of disclosure.

### A flexible insurance regime

14.3 Much of the MIA is concerned simply with the ‘interpretation of the contract contained in the common form of marine policy’.<sup>991</sup> The MIA codified the

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990 D Taylor ‘The Need for Reform of Marine Insurance’ *Paper MLAANZ–BIMCO Conference Brisbane* 17–19 March 1999.

991 M Mustill and J Gilman *Arnould’s Law of Marine Insurance and Average* 16th ed vol I Stevens & Sons London 1981, 41 referring to *Kulukundis v Norwich Union Fire Insurance Society* [1937] 1 KB 1, 34. Scott LJ continued ‘we have all got into the mental habit of thinking of it as substantive law; particularly since its codification in statutory shape ... the act simply fixes the interpretation which it requires the court to put on the old form of policy unless the special terms of the particular contract vary it’.

scattered common law relating to the circumstances in which extrinsic evidence of the

‘usages of trade’ might be led to add to, fill out or explain the terms of the policy. *Arnould’s Law of Marine Insurance and Average* observes that usage is of special importance in commercial contracts, nowhere more so than in marine insurance, for it has always been accepted that such usages need not be set out in the policy.<sup>992</sup> In consequence, many provisions of the MIA apply ‘unless the policy otherwise provides’; ‘subject to any express provision in the policy’; ‘unless the contrary be expressed’; ‘unless otherwise agreed’ or similar.<sup>993</sup> In addition, s 93 of the MIA states

93(1) Where any right, duty or liability would arise under a contract of marine insurance by implication of law, it may be negated or varied by express agreement, or by usage, if the usage be such as to bind both parties to the contract.

14.4 The Commission observes in passing that usage may be a much less valuable guide to practice, law and contractual intention in Australia than might be the case in London, for example. Consultations have indicated that knowledge of the operation and effect of the MIA varies significantly. In any event, insureds could not be expected to have knowledge of the Act and usages to the same extent as those who work in the insurance industry, though brokers advising them might be. The general understanding of shorthand terms is far from universal and perfect. This can lead to unexpected results when a policy is interpreted by a court, which must try to give the contractual terms a natural meaning, and does so in a way that was not intended by the insurance professionals involved.<sup>994</sup> All other things being equal, in the Commission’s view it is preferable that the terms of any contract of insurance be set out clearly on or attached to the policy document or referred to in other contractual documents in a way that makes it quite clear what is included.

14.5 The MIA also provides that the insurer may waive the application of certain provisions of the MIA.<sup>995</sup> An example is s 61, which provides that the insurer is liable for any loss proximately caused by a peril insured against. A number of exclusions are stated but the parties are free to add or subtract from them. For example, s 61(2) excludes, unless the policy otherwise provides, ‘inherent vice or nature of the subject matter insured’. In practice, even before the enactment of the MIA, marine insurance contracts often included Inchmaree clauses<sup>996</sup> which cover breakage of machinery on ships, and a range of other risks that otherwise would

992 M Mustill and J Gilman *Arnould’s Law of Marine Insurance and Average* 16th ed vol I Stevens & Sons London 1981, 41.

993 MIA s 8, 15, 21–22, 30, 33, 35, 38, 51, 56, 58–59, 61–62, 66, 71–72, 74–77, 79–80, 82–83, 93. Many of these provisions imply terms, where the policy is otherwise silent, which are broadly favourable to the insurer, eg s 21, 51, 58–59, 61.

994 See para 11.36.

995 MIA s 24, 48, 61, 68.

996 *Thames & Mersey Marine Insurance Co Ltd v Hamilton, Fraser & Co (The Inchmaree)* (1887) 12 AC 484.

not be covered.<sup>997</sup> Even in relation to the provisions relating to insurable interest, the duty of disclosure and warranties, there is room for the parties to agree on terms that diverge from the basic principles of the MIA.<sup>998</sup>

14.6 Some of the harsh consequences of breach may be modified by contract. For example, where a policy covers a fleet of ships, a material non-disclosure or breach of warranty in respect of one ship may lead to the insurer avoiding liability for claims in respect to all other ships in the fleet. For this reason clauses may be inserted in fleet policies moderating this position so that the only claims avoided are those related to the relevant ship.<sup>999</sup>

14.7 The flexibility of the MIA is said by many to be the key to its continuing relevance and its importance was emphasised in submissions.<sup>1000</sup> The importance of retaining this flexibility and freedom of contract has been consistently emphasised and is one reason marine insurers prefer the separate MIA regime. In contrast, s 52 of the ICA declares void any provision in a contract of insurance that purports to exclude, restrict or modify the operation of the Act to the prejudice of any person other than the insurer.<sup>1001</sup>

14.8 The prescriptive approach of the ICA may not be appropriate for the particular circumstances of marine insurance, especially given the need for flexibility in meeting the varying demands of clients in an international market. The distinctions between the MIA and ICA and some of the reasons for retaining the MIA with measured amendment only, including those relating to the international market, are discussed in chapter 3.

## **The MIA and standard contractual terms**

14.9 As noted above, many provisions of the MIA are in effect ‘default’ contractual terms that apply only where the contract is otherwise silent. In its Discussion Paper the Commission asked how often contracts of marine insurance are, in practice, silent on terms otherwise implied by the MIA and whether there is a continuing justification for the MIA to imply such contractual terms.<sup>1002</sup>

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997 ITC Hulls cl 6.2; IVC Hulls cl 4.2; ITC Freight cl 7.2; IVC Freight 4.2.

998 See ALRC DP 63 para 2.50–2.53.

999 *Marine insurance seminar* Phillips Fox Sydney 20 February 2001.

1000 eg P Grieve *Submission 6*; Law Society of WA *Submission 7*; K Carruthers *Submission 9*; Law Council of Australia *Submission 10*; Insurance Council of Australia *Submission 11*; MLAANZ *Submission 12*.

1001 Contingency cover is an example of where the prescriptive approach of the ICA may not be appropriate to marine insurance: See ALRC DP 63 para 2.55.

1002 ALRC DP 63 question 7.



14.10 In many ways the MIA, a reflection of UK marine insurance law and industry practice a century ago, may not reflect current marine insurance practice. If contracts expressly deal with matters otherwise implied by the MIA, these statutory provisions may be seen to have no purpose apart from reflecting a superseded norm, and as appropriate for repeal or amendment. However, the Maritime Law Association of Australia & New Zealand (MLAANZ) noted that contracts are in fact often silent on the matters dealt with by the MIA. It submitted that

Certain terms which are considered to be of general public importance, such as seaworthiness, legality etc should continue to be provided for in legislation.<sup>1003</sup>

14.11 Where provisions of the MIA implying contractual terms serve no useful modern purpose, the reform options include deleting these provisions or amending them to reflect current standard terms.

14.12 In its Discussion Paper, the Commission asked whether, assuming that such provisions of the MIA were deleted, it might be appropriate for the standard terms of marine insurance contracts to be governed solely by the marine insurance industry within a self-regulatory scheme. The Commission noted that one model for such a scheme is the Norwegian Marine Insurance Plan, which is developed by an insurance industry committee.<sup>1004</sup> The Plan provides for key contractual terms and practical commercial details relating to Norwegian marine insurance policies.<sup>1005</sup>

14.13 The Commission has not attempted to identify any comprehensive list of the provisions of the MIA that might be deleted or amended on the basis that they imply terms no longer usual in marine insurance policies. No submissions suggested that this would be a desirable approach to reform of the MIA. Furthermore, submissions opposed the suggestion that options for enhanced industry self-regulation and standard contractual terms should be examined in more detail.<sup>1006</sup>

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1003 MLAANZ *Submission 12*. Justice Carruthers stated that there is justification for the MIA to prescribe 'default' contractual terms: K Carruthers *Submission 9*.

1004 A committee set up under the aegis of Det Norske Veritas conducted the last major revision of the Plan. The committee convened included representatives of the Norwegian Shipowners' Association; the Central Union of Underwriters; the Mutual Hull Clubs Committee; the protection and indemnity (P&I) insurers; the Norwegian Shipowners Mutual War Risks Insurance Association; the Federation of Norwegian Engineering Industries and Det Norske Veritas. There is a standing committee responsible for ongoing revision of the Plan: Norwegian Marine Insurance Plan <http://exchange.dnv.com/nmip/books/plan/preface.htm> (29 March 2000).

1005 See ALRC DP 63 para 2.57–2.59.

1006 K Carruthers *Submission 9*; MLAANZ *Submission 12*.

14.14 For a range of reasons, discussed in chapter 15 below, the Commission has rejected comprehensive modernisation of the MIA for its own sake, including any attempt to delete or amend provisions simply because they may no longer reflect current marine insurance practice unless that is part of more comprehensive amendments to those or related provisions.

### Institute clauses

14.15 The Institute clauses form the basis of most marine insurance policies written in Australia.<sup>1007</sup> These clauses were drafted under the aegis of the Institute of London Underwriters.<sup>1008</sup> The Institute issued various sets of model clauses since its establishment in 1884. These clauses have been the subject of numerous revisions. Most recently, the Joint Hull Committee<sup>1009</sup> has undertaken to comprehensively review the Institute hull clauses and issue new policy wordings by the end of 2002.

14.16 Cargo cover in Australia is generally based on one of three sets of policy clauses: the Institute Cargo Clauses (ICC) (A), (B), and (C).<sup>1010</sup> The ICC(A) provide ‘all risks’ cover, subject to specified exclusions. The ICC(B) and ICC(C) provide cover for named risks, subject to the same exclusions. The list of risks covered in ICC(C) is a sub-set of those in ICC(B).

14.17 The exclusions in the Institute cargo clauses are often modified by the parties. For example, while the clauses exclude loss caused by ‘inherent vice’ or delay where the cargo consists of perishable goods, cover may be extended to include inherent vice, delay and rejection by the government authority of the importing country.<sup>1011</sup> Separate sets of Institute clauses exist for particular cargoes such as coal, oil, rubber and frozen meat, and for particular types of transport, such as container transport.<sup>1012</sup>

14.18 In the Australian market, hull insurance cover is also based on Institute clauses. There are two sets of Institute hull clauses, distinguishing between time and voyage policies respectively — the Institute Time Clauses (ITC) Hulls and the Institute Voyage Clauses (IVC) Hulls. Both sets of hull clauses provide named

1007 The clauses discussed here are still known as the ‘Institute clauses’.

1008 The Institute of London Underwriters has been subsumed by the International Underwriters Association (IUA).

1009 The Joint Hull Committee is comprised of representatives of Lloyd’s and company insurers engaged in the London market. See para 7.31.

1010 Freight is the subject of a separate set of Institute clauses.

1011 B Turner and T Bunn ‘Placing a Risk — Cargo Insurance’ *Paper* MLAANZ Conference Brisbane 7-11 September 1996.

1012 H Bennett *The Law of Marine Insurance* Clarendon Oxford 1996, 105.

risks cover, subject to various exclusions. Again, these clauses may be significantly varied by the parties.

14.19 The Institute clauses are, according to MLAANZ, ‘built on the foundation stone of the MIA — or its UK equivalent’.<sup>1013</sup> Clearly, the changes to the MIA recommended by the Commission will necessitate fresh attention to the terms of Australian marine insurance policies. However, this can only be beneficial overall and lead to a greater general understanding in the industry of the current and proposed operation of the MIA and the way in which standard and other contractual terms interact with it.

### Choice of law rules and jurisdiction

14.20 The Discussion Paper noted that the international workings of the marine insurance market and the fact that most contracts are made between ostensibly well informed commercial interests suggest that the parties’ freedom to contract should be preserved. On the other hand, the benefit of reforms to the MIA may be lost, especially to those insured parties who may have most need of such reforms, if contracts of marine insurance written in Australia come to be routinely governed by UK or other foreign law.

14.21 For this reason the Commission gave detailed consideration to issues surrounding choice of law and jurisdiction in the Discussion Paper<sup>1014</sup> and examined whether party choice of law should be constrained by legislative provisions such as those found in the ICA and the *Carriage of Goods by Sea Act 1991* (Cth) (COGSA).

#### *Insurance Contracts Act 1984*

14.22 ICA s 52 forbids parties contracting out of the ICA where this would prejudice a person other than the insurer. Section 8 of the ICA also prevents the parties from avoiding the ICA by choosing the law of another jurisdiction as the governing law of the contract.<sup>1015</sup> It provides that the ICA extends to contracts of insurance the proper law of which is, or would be apart from any choice of law in the contract, the law of an Australian state or territory.<sup>1016</sup> Where the parties have expressly nominated another law to govern the contract then, notwithstanding that contractual term, the ICA will apply if the objective proper law is that of a state or

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1013 Law Council of Australia and Maritime Law Association of Australia and New Zealand *Submission to AG’s Dept* 1997.

1014 ALRC DP 63 para 2.60-2.85.

1015 *Akai Pty Ltd v The People’s Insurance Co Ltd* (1996) 188 CLR 417, 433; 141 ALR 374, 384.

1016 ICA s 8(1).

territory.<sup>1017</sup> Similar provisions are found in the *Insurance (Agents and Brokers) Act 1984* (Cth) (IABA).<sup>1018</sup>

### ***Carriage of Goods by Sea Act 1991***

14.23 COGSA enacted into Australian law new rules governing the conditions upon which goods are to be carried in international shipping.<sup>1019</sup> To ensure that these rules are applied to all contracts for the shipment of goods out of Australia, s 11(1) provides that all parties to a sea carriage document relating to the carriage of goods from any place in Australia to any place outside Australia are taken to have intended to contract according to the laws in force at the place of shipment (that is, the relevant Australian jurisdiction).<sup>1020</sup>

14.24 Section 11(2) provides that an agreement to preclude or limit the effect of s 11(1) or the jurisdiction of Australian courts has no effect.<sup>1021</sup> This means, for example, that an Australian court, when dealing with a bill of lading for the shipment of goods from Sydney to France in which it is stipulated that French law shall govern the contract, must nevertheless apply the law of New South Wales, including the terms and conditions laid down in COGSA, as the proper law of the bill of lading.<sup>1022</sup>

14.25 The restrictions on choice of law in COGSA go further than those in the ICA. Section 11 of COGSA displaces the choice of law itself whereas the ICA provides that the ICA's provisions are to apply to contracts the proper law of which is that of an Australian state or territory objectively ascertained, notwithstanding the express choice of a foreign legal system.<sup>1023</sup>

### **Implications for reform of the MIA**

14.26 While there may be a national interest in maintaining and promoting Australian courts and arbitration as dispute resolution forums in marine insurance and other international commercial matters, restricting the scope for parties to exercise choice of law may adversely affect the availability and competitiveness of insurance in Australia.

14.27 Some Australian insureds choose to insure with both Australian insurers and co-insurers in London or other overseas markets. By maintaining contact with more

<sup>1017</sup> ICA s 8(2).

<sup>1018</sup> IABA s 6.

<sup>1019</sup> Replacing the Hague Rules implemented in the *Sea-Carriage of Goods Act 1924* (Cth).

<sup>1020</sup> COGSA s 11, which is similar in effect to its predecessor: *Sea-Carriage of Goods Act 1924* (Cth) s 9.

<sup>1021</sup> Section 11(3) provides that an agreement for the resolution of a dispute by arbitration is not made ineffective by s 11(2) if the agreement provides for that arbitration to be conducted in Australia.

<sup>1022</sup> See P Nygh *Conflict of Laws* 6th ed Butterworths Sydney 1995, 35.

<sup>1023</sup> *Ibid* 297. The *Trade Practices Act 1974* (Cth) s 67 uses a mechanism similar to the ICA s 8.

than one market, the insured may be able to obtain more competitive rates. If party choice of law is constrained, this may have some adverse effect on the availability of overseas insurance for Australian risks if some overseas insurers prefer that English law, for example, govern their contract.

14.28 Australian insurers may be commercially disadvantaged in the international marine insurance market if they are not able to offer insurance subject to English law (or Dutch or Norwegian or other law, if that is the preference of a prospective insured). In addition, if marine insurance contracts were subject to a provision similar to s 8 of the ICA, there may be uncertainty as to the proper law of the contract entered by the Australian company where Australian insurers are co-insurers of insurance contracts entered into by leading underwriters overseas. Such uncertainty might also disadvantage Australian insurers.<sup>1024</sup>

14.29 For these reasons the Commission proposed in its Discussion Paper that the law of marine insurance in Australia should not restrict the right of parties to choose some other body of law as the governing law of the contract or to decide that disputes be resolved by a foreign court or other forum.<sup>1025</sup> However, the Commission was prepared to consider alternative approaches that might provide a 'middle road' between the provisions found in the ICA or COGSA and full freedom of contract in choice of law and jurisdiction. In this context, the Commission asked whether the MIA should provide that, where both parties to a contract of marine insurance are domiciled in Australia, the application of Australian law and the jurisdiction of Australian courts may not be circumvented contractually.<sup>1026</sup>

14.30 Submissions expressed divergent opinions on this issue. Most submissions agreed with the draft proposal.<sup>1027</sup> For example, the Law Society of Western Australia rejected suggestions that the MIA include any provision restricting choice of law or jurisdiction and stated

While this approach would encourage and promote dispute resolution in Australia, in our view it would be unnecessarily restrictive, particularly on international corporations. Further, it may ultimately reduce the availability of foreign insurance for Australian risks. The absence of such a section may encourage competition for Australian insurers in international markets.<sup>1028</sup>

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1024 See ALRC DP 63 para 2.69–2.71 discussing the High Court's consideration of the ICA choice of law provisions in *Akai Pty Ltd v The People's Insurance Co Ltd* 188 CLR 418; (1996) 141 ALR 374.

1025 ALRC DP 63 draft proposal 1.

1026 ALRC DP 63 question 9.

1027 D Chaplin *Submission 3*; P Grieve *Submission 6*; Law Society of WA *Submission 7*; K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*; National Bulk Commodities Group *Submission 14*.

1028 Law Society of WA *Submission 7*.

14.31 Part of the Law Society of WA's reason for rejecting restrictions on choice of law was that parties to most marine insurance contracts are commercial entities with some degree of bargaining power. This factor was echoed by the National Bulk Commodities Group, which stated that its member companies are

well able to make their own decisions, whether on the basis of in house or external advice, as to the desirability of choosing the law of a country other than Australia as the governing law of the contract of insurance.<sup>1029</sup>

14.32 Justice Carruthers agreed that, in general, an amended MIA should not restrict choice of law or jurisdiction where overseas interests are involved but stated that

there are persuasive grounds, looking at the overall picture, to consider the MIA providing that, where both parties to a contract of marine insurance are domiciled in Australia, the application of Australian law and the jurisdiction of Australian courts may not be circumvented contractually. In fact this may be too good an opportunity to be missed.<sup>1030</sup>

14.33 However, one submission considered that Australian law should always govern marine insurance written in Australia. Alexander Street SC stated that

it would defeat beneficial changes intended to be achieved by this Commission if parties are free to contract out of MIA so as to adopt some other law of marine insurance. ... A provision that purports to exclude, modify or restrict Australian jurisdiction or application of Australian law should be of no force or effect. Once a dispute has been crystallised the parties are free to resolve by agreement that it be determined at any place and by any forum they like if able to agree upon the same.<sup>1031</sup>

14.34 The Commission recognises concerns that, by allowing parties the freedom to contract that foreign law will apply, reforms to the MIA may be circumvented. However, as noted in the Discussion Paper, it is difficult to predict whether or to what extent insurers might enter contracts subject, for example, to UK law in order to circumvent changes to the MIA. On one hand, brokers may argue against contractual choice of law clauses that might work against the interest of the insured parties they advise. On the other, in practice, the level of premiums and terms of the cover, rather than the choice of law, are possibly of more concern to insureds and their brokers.

14.35 The effect of reform in this area on the position of Australian marine insurance in the international market is equally hard to predict. There may also be international competition policy ramifications.

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1029 National Bulk Commodities Group *Submission 14*.

1030 K Carruthers *Submission 9*.

1031 A Street *Submission 15*.

14.36 On balance, the Commission has concluded that there should be no change to the MIA in respect of party choice of law and jurisdiction.

**Recommendation 35. The law of marine insurance in Australia should not restrict the right of parties to choose some other body of law as the governing law of the contract or to decide that disputes be resolved by a foreign court or other forum.**

### Jurisdiction of the Federal Court of Australia

14.37 The Discussion Paper raised the issue of the Federal Court's jurisdiction over marine insurance matters.

14.38 Section 39B(1A)(c) of the *Judiciary Act 1903* (Cth) confers jurisdiction on the Federal Court in any matter 'arising under any laws' made by the federal parliament other than criminal matters. This covers matters arising 'under' the MIA. However, there is some uncertainty concerning contractual disputes that might arise in relation to a marine insurance policy but which do not arise 'under' the MIA. The Discussion Paper proposed that the MIA should expressly invest the Federal Court with jurisdiction in marine insurance matters, to be exercised concurrently with state and territory courts. There was support for this proposal in submissions<sup>1032</sup> although one submission argued that the existing jurisdiction under the *Judiciary Act 1903* s 39B(1A)(c) was sufficient.<sup>1033</sup>

14.39 With one qualification, the Commission would agree with the latter position. The vast majority of marine insurance disputes would raise for consideration one or more provisions of the MIA, or one or more terms of the contract on which the MIA has some impact. Most such disputes could then be said to arise 'under' the Act and would therefore be matters in respect of which the Federal Court currently has jurisdiction. However, the mere fact that a claim might involve the interpretation of the MIA does not mean that it is a matter arising 'under' a law made by the federal parliament. The claim must rely on a right that owes its existence to the Act or depends on the Act for its enforcement.<sup>1034</sup>

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1032 Law Society of WA *Submission 7*; K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*.

1033 A Street *Submission 15*.

1034 *Felton v Mulligan* (1971) 24 CLR 367, 416 (Gibbs J). In that case the claim was held to arise from the deed between a husband and wife and not from the relevant legislation, the *Matrimonial Causes Act 1959* (Cth). See also Australian Law Reform Commission Discussion Paper 64, *The Judicial Power of the*

14.40 If the federal parliament had no power to legislate generally in the area of marine insurance, s 39B(1A)(c) would seem to go as far as the parliament can within the Constitution and, therefore, there would be no need to repeat the terms



and effect of that section in the MIA. Indeed, there would be strong policy reasons for not doing so as s 39B(1A)(c) is clearly intended to be of general application.<sup>1035</sup> There are many good reasons why there should not be a plethora of statutory provisions in a large number of Acts all saying the same thing unless there is some particular reason why this is necessary. The Commission understands that it is the current practice of the Office of Parliamentary Counsel not to provide expressly for the Federal Court's jurisdiction in new legislation on the basis that s 39B(1A)(c) covers the position, presumably unless the general position stated there needs to be qualified.

14.41 The only reason to consider a wider conferral of jurisdiction is to cover the relatively unlikely situation where a matter arises under a contract of marine insurance that does not arise 'under' the MIA. In such a case, the Federal Court would not have jurisdiction under s 39B(1A)(c) and no similar provision in the MIA itself would alter that position. Such cases could only be brought in the state court system. However, if the issues that do not arise under the MIA are 'part of the same controversy' as other issues in the case that do arise under the MIA (or any other federal Act), the Federal Court would have accrued jurisdiction to determine the issues not arising under the Act.

14.42 If, on the other hand, a provision with scope broader than s 39B(1A)(c) could legitimately be enacted by the federal parliament and included in the MIA, the rare cases that do not arise 'under' the Act could also be accommodated. Such a provision would have the benefit of removing any doubt about the Federal Court's jurisdiction that might be created by the limitation identified in *Felton v Mulligan*<sup>1036</sup> on the range of matters that arise 'under' an Act and are therefore caught by s 39B(1A)(c).

14.43 The Commonwealth has a range of powers under the Constitution which allow it to grant jurisdiction over admiralty and maritime matters.<sup>1037</sup> In particular, s 76(iii) and 77 of the Constitution allow parliament to make laws defining the jurisdiction of any federal court or state court with respect to 'Admiralty and maritime jurisdiction'. The extent of this jurisdiction was discussed in *Owners of the Ship 'Shin Kobe Maru' v Empire Shipping Co Inc.*<sup>1038</sup> The High Court held that s 76(iii) extended to 'matters of the kind generally accepted by maritime nations as falling within a special jurisdiction, sometimes called Admiralty and sometimes

1035 However, s 39B(1A)(c) may be held not to apply where pre-existing legislation expressly prohibits the Federal Court from exercising jurisdiction, or may be subsequently restricted where appropriate in particular pieces of legislation.

1036 (1971) 24 CLR 367.

1037 Australian Law Reform Commission Report 33 *Civil Admiralty Jurisdiction* AGPS Canberra 1986 (ALRC 33), 49.

1038 (1994) 181 CLR 404.

called maritime jurisdiction, concerned with the resolution of controversies relating to marine commerce and navigation'.<sup>1039</sup> This extends the definition beyond the English division of admiralty to a wide traditional base<sup>1040</sup> and would appear to allow the grant of jurisdiction to the Federal Court over marine insurance matters not confined to matters arising under the MIA.

14.44 In addition to the jurisdictional provisions of s 76 and 77, s 51(xiv) of the Constitution provides the Commonwealth parliament with power to legislate for 'insurance, other than State insurance; also State insurance extending beyond the limits of the State concerned'. The parliament may also legislate on incidental matters under s 51(xxxix) of the Constitution. An amendment to the MIA to expressly invest the Federal Court with jurisdiction in marine insurance matters generally could be founded on either of these bases or under s 76(iii) and 77 of the Constitution.

14.45 To overcome the uncertainty in this area, the Commission recommends that the MIA be amended to expressly invest the Federal Court with jurisdiction in marine insurance matters generally (other than state insurance), to be exercised concurrently with state and territory courts.

**Recommendation 36. The MIA should expressly invest the Federal Court with jurisdiction in marine insurance matters (other than state insurance) as an incident of admiralty and maritime jurisdiction, to be exercised concurrently with state and territory courts.**

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1039 (1994) 181 CLR 404, 424.

1040 See M White *Australian Maritime Law* 2nd ed The Federation Press Sydney 2000, 16–18.

## 15. Policies and contracts

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### Introduction

15.1 This chapter considers the requirements under the MIA for marine insurance contracts and policies. It examines the status of the slip, formation of the contract, content requirement for marine insurance policies, evidential requirement for marine insurance contracts and different types of policies. This chapter also considers the impact of electronic transactions on marine insurance contracts and policies. Finally, the chapter reviews those areas of the MIA which require amendment in order to modernise the Act.

### Marine insurance contracts and policies

15.2 The MIA distinguishes in a number of respects between contracts and policies. In short, policies are the formal embodiment of the contract. Under s 27 a contract of marine insurance is deemed to be concluded when the insured's proposal is accepted by the insurer. The policy can be issued at a later time.<sup>1041</sup> Unless otherwise agreed, the insurer is under a duty to issue the policy but, as this is concurrent with the insured's duty to pay the premium, the policy does not have to be issued until the premium has been paid or tendered.<sup>1042</sup> In order to show when

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1041 MIA s 28.

1042 MIA s 58.

the contract was in fact concluded, the parties and the courts may refer to the slip, covering note or any other customary memorandum.<sup>1043</sup>

15.3 The policy itself must contain certain minimum information,<sup>1044</sup> it must be signed by the insurer<sup>1045</sup> and the subject matter insured must be designated in the policy with reasonable certainty.<sup>1046</sup>

### Status of the slip

15.4 In marine insurance practice, contracts are often based on the use of a slip.<sup>1047</sup> A slip is a memorandum of agreement prepared by the broker, acting as the agent of the insured, who approaches underwriters seeking subscriptions to the cover. Beginning with the leading underwriter, each underwriter initials the slip with the percentage of the risk underwritten. Generally, negotiations about the terms of the insurance and the rate of premium are carried on between the broker and the leading underwriter alone.

### Use of the slip in Australia

15.5 The market understanding is that the initialling of the slip by an underwriter creates a binding contract with that underwriter and that a formal policy may not be prepared until some months after the slip is closed. The underwriter is considered bound from the moment the slip is initialled, even in the absence of a policy,<sup>1048</sup> and is obliged to issue a policy at the request of the insured.

15.6 In practice, Australian courts are reluctant to allow insurers to escape liability on the technical point that no policy has been issued<sup>1049</sup> and MIA s 58 provides that once the insurer has received premium it has a duty to issue the policy, which can be specifically enforced if necessary.

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1043 MIA s 27.

1044 Under MIA s 29, a marine policy must specify  
 (a) the name of the assured, or of some person who effects the insurance on his behalf  
 (b) the subject-matter insured and the risk insured against  
 (c) the voyage, or period of time, or both, as the case may be, covered by the insurance  
 (d) the sum or sums insured  
 (e) the name or names of the insurers.

1045 MIA s 30.

1046 MIA s 32.

1047 Slips are commonly used in the London market where coinsurance is widespread. The use of slips in the Australian market is limited and reducing as more business is placed with one underwriter and submitted and agreed by fax or email: Associated Marine Insurers Agents Pty Ltd *Correspondence* 17 April 2000.

1048 H Bennett 'The Role of the Slip in Marine Insurance Law' [1994] *Lloyd's Maritime and Commercial Law Quarterly* 94.

1049 D Luxford 'The Marine Insurance Act: Chronologically Challenged Legislation?' *Paper MLAANZ Annual Conference Wellington New Zealand 5–8 November 1995*, 26.

## Overseas

15.7 In New Zealand, s 26 of the MIA (NZ) provides that it is an offence if an insurer or an insurer's agent does not execute, or procure the execution of, a policy complying with the Act within 30 days of receiving or taking credit for the premium or other consideration, and provides for a NZ\$200 fine.

15.8 Case law in the United Kingdom has established that the slip can be used as evidence in an action for rectification if there is a discrepancy between the wording of the slip and the policy.<sup>1050</sup> Furthermore, the parole evidence rule, which prevented extrinsic evidence from being allowed to vary the written contract, is no longer strictly adhered to and the slip may constitute useful evidence of the terms of the contract.<sup>1051</sup>

15.9 In the early 1800s, the status of the slip in English common law was that of a mere proposal, not amounting to a contract of marine insurance. Since the 1871 case of *Ionides*,<sup>1052</sup> however, the slip has been recognised as amounting to a contract and is admissible as evidence of it.

## Evidential requirements

15.10 The real limitation on the use of a slip is found in MIA s 28, which provides that

28 Subject to the provisions of any Act, a contract of marine insurance is inadmissible in evidence in any action for the recovery of a loss under the contract unless it is embodied in a marine policy in accordance with this Act.

15.11 The equivalent provision was repealed in New Zealand by the Marine Insurance Amendment Act 1975 (NZ). However, the MIA (Can) contains a requirement similar to that in the MIA (UK).<sup>1053</sup>

15.12 Section 28 of the MIA represents the one departure in substance between the Australian MIA and the original MIA (UK) 1906. The difference is the insertion of the words 'in an action for the recovery of a loss under the contract'. In the UK, contractual documents are not admissible in evidence for any purpose unless a policy has been issued.<sup>1054</sup> In Australia the prohibition relates only to the critical

1050 *Symington & Co v Union Insurance Society of Canton Ltd (No 2)* (1928) 34 CC 189.

1051 *Youell v Bland Welch* [1992] 2 Lloyd's Rep 127. It was acknowledged that extrinsic evidence could be admissible as an aid to interpretation of wording not possessed on its face of a clear and unequivocal meaning.

1052 *Ionides v Pacific & Marine Insurance Co* (1871) LR 6 QB 674.

1053 MIA (Can) s 25(1) A contract is inadmissible in evidence, unless it is evidenced by a marine policy in accordance with this Act.

1054 MIA (UK) s 22.

function of evidence in a claim seeking recovery of a loss under the contract. MIA s 95 confirms that once a policy in accordance with the Act has been issued, however, nothing prevents reference being made in legal proceedings to the slip, covering note or other customary memorandum of the contract.

15.13 The purpose of s 28 and 95 was to protect stamp duty revenue. The MIA (UK) tellingly uses the words ‘duly stamped policy’ in its equivalent of s 95.<sup>1055</sup> The equivalent provision in New Zealand Act, s 90, was repealed by the Stamp Duties Amendment Act 1960 (NZ). The Commission’s enquiries have revealed that no stamp duty is currently payable on marine insurance policies in any Australian state or territory. Accordingly, there is no revenue to protect and s 28 has become simply a formal hindrance to the proof of a contract in legal proceedings for the recovery of a loss under the policy.

15.14 The words ‘in an action for the recovery of a loss under the contract’ were inserted into the MIA as a result of discussion during the second reading of the Marine Insurance Bill. The second reading speech referred to s 27, 28 and 95 of the MIA and noted the difference between the English and Australian position in relation to stamp duty. While in England stamp duty was an important factor behind some of the drafting, in Australia there was no Commonwealth Stamp Act and it was considered ‘not for us to expressly recognise or protect the stamping laws of the States’.<sup>1056</sup> The discussion noted that, in the absence of a policy, nothing in the Bill shall be deemed to take away the right of a litigant to sue the company for a policy.<sup>1057</sup>

15.15 The second reading speech also referred to MIA s 95, which states

Where a policy in accordance with this Act has been issued nothing in this Act shall prevent reference being made in legal proceedings to the slip or covering note or other customary memorandum of a contract of marine insurance.

15.16 This differs from MIA (UK) s 89, which states

Where there is a duly stamped policy, reference may be made, as heretofore, to the slip or covering note, in any legal proceeding.

15.17 The aim of this change in wording was to keep as close to the MIA (UK) as possible while refraining from a direct reference to stamp duty as this was a matter for the states, not the Commonwealth.<sup>1058</sup>

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1055 MIA (UK) s 89.

1056 P Glynn, Attorney-General, *Hansard* (H of R) 6 October 1909, 4190.

1057 *Ibid*, 4192.

1058 *Ibid*, 5436.

15.18 The requirement for a marine insurance policy as evidence of the contract dates back to the Stamp Act 1795 (UK). This legislation introduced a special stamp duty regime for marine insurance contracts and stipulated certain matters that were to be contained in the marine insurance policy. The Finance Act 1959 (UK) repealed certain stamp duty provisions relating to marine insurance and the Finance Act 1970 (UK) abolished stamp duty on marine insurance contracts.

15.19 In order to clarify the legal status of the slip, the Discussion Paper suggested that the provisions of the MIA should be amended to allow a slip or any other document recording or evidencing the contract of marine insurance to be treated as prima facie evidence of the contract in the absence of any other document.<sup>1059</sup>

15.20 Some insurers have warned against relying on the slip as against the policy<sup>1060</sup> but this perhaps loses sight of the fact that the principal point of any reform in this area is to allow a slip to be admissible in evidence when there is no policy document, so there is no question of there being a contest between the two in the circumstances where reform is envisaged. The MIA already contemplates the use of a slip to challenge the accuracy of the policy document in setting out the agreed contractual terms, and its admissibility into evidence for this purpose. In this respect, a possible contest between the two documents, for example in a claim for rectification, is nothing new.

15.21 On the other hand, several submissions supported this proposal.<sup>1061</sup> However, there were some provisos. It was suggested that all documents evidencing the contract should be considered, especially where one party disputes the content of one document as against another.<sup>1062</sup> Another submission supported the Commission's draft proposal provided that the slip contains the same information as that specified for a marine policy in MIA s 29, 30 and 32.<sup>1063</sup> The Insurance Council of Australia supported the proposal provided that the amendment included adequate provision for the treatment of documents in the event of non-payment of premium<sup>1064</sup> although the precise nature of the Council's concerns was not identified.

15.22 It is not the Commission's intention to give the slip or other contractual document any greater status or evidentiary value than it would normally bear if used to show the true contractual intention of the parties. It is quite possible that one party would wish to show that the policy does not properly record the

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1059 ALRC DP 63 Draft proposal 14.

1060 Insurers *Consultation* Melbourne 6 June 2000.

1061 E Laryea *Submission 4*; K Carruthers *Submission 9*; MLAANZ *Submission 12*; National Bulk Commodities Group *Submission 14*.

1062 D Chaplin *Submission 3*.

1063 P Grieve *Submission 6*.

1064 Insurance Council of Australia *Submission 11*.

agreement if it differs from the slip; this has always been contemplated by the MIA. Rather, the Commission's intention is simply to permit the parties (in reality, the insured) to introduce into evidence whatever contractual documents are available to it in the absence of a duly issued policy in order to advance its case. The court will then determine the existence and content of the contract on the basis of the whole of the evidence available to it.

15.23 Accordingly, the Commission recommends that the first sentence of s 28 be repealed. Section 95 of the MIA perhaps becomes redundant as a result but should be retained to preserve the admissibility of the slip and other contractual documents.

15.24 The MIA already provides that the insurer is duty-bound to issue a policy once the premium has been paid or tendered and that should remain. However, it appears to be necessary to re-state the obligation in s 28 in order to put the second sentence of that section into context. For various reasons set out in chapter 14, the Commission prefers to leave s 58 as and where it is although it is logically and physically removed from s 28–30, and will be more so if the Commission's recommendations in relation to the repeal of s 59 and 60 are adopted.<sup>1065</sup>

## Contract formation

15.25 A related issue raised in the Discussion Paper is whether the risk placed through subscription to a slip is covered by one contract of insurance or whether each subscription gives rise to a separate contract.<sup>1066</sup> MIA s 31(2) states that

31(2) Where a policy is subscribed by or on behalf of two or more insurers, each subscription, unless the contrary be expressed, constitutes a distinct contract with the assured.

15.26 The distinction between a slip and a policy drawn in various places in the MIA is blurred to some extent in this instance. The law is said to be clear that each signature on a slip gives rise to a distinct, binding contract and each underwriter is bound by the terms as agreed at the time of the underwriter's subscription.<sup>1067</sup>

15.27 While the law allows following underwriters ample scope to vary or amend the terms of the insurance contract, 'the expertise of the leading underwriter and the market dislike of policies embodying contracts on different terms are powerful constraints on its practical operation'.<sup>1068</sup>

1065 See ch 13.

1066 H Bennett 'The Role of the Slip in Marine Insurance Law' [1994] *Lloyd's Maritime and Commercial Law Quarterly* 94, 105–6.

1067 *Ibid* 103–7.

1068 *Ibid* 106.



15.28 The Discussion Paper asked whether there were any issues in relation to the formation of contracts of marine insurance that should be clarified by amendments to the MIA but there was no comment on this issue in submissions.<sup>1069</sup> In view of the Commission's recommendations concerning reform of the requirements for marine insurance contracts and policies, the Commission does not consider that any further change needs to be made to the MIA on this issue.

### **Composite policies**

15.29 A similar point was raised with the Commission in its discussions with representatives of the London insurance market in February 2001. The Commission had not previously raised the issue of whether a contract with multiple insureds constitutes a distinct and separate contract with each of them or a joint or composite contract with them all. The MIA is silent on this issue. It was not raised in the Discussion Paper and was not the subject of any submission.

15.30 If there is a joint contract with all insureds, the breach of the contract by any one of them will taint the cover held by all other insureds, who will suffer accordingly if the breach entitles the insurer to avoid or reduce its liability to the innocent insureds. According to *Arnould's Law of Marine Insurance and Average*, there can only be a joint insurance in the strict sense when the insureds have a joint interest in the property insured.<sup>1070</sup> The question whether an insurance policy is joint or composite is a matter of construction but, generally, a policy insuring two or more interests will be construed as composite insurance with each party insured in respect of its own interest.<sup>1071</sup>

15.31 In the absence of any submission or other comment suggesting that there are substantial problems in this area, the Commission does not propose any statutory change.

### **The contents of the policy**

15.32 In both the UK and Australia the marine insurance policy must be signed by or on behalf of the insurer<sup>1072</sup> and the subject matter insured must be designated with reasonable certainty.<sup>1073</sup> However, there are differences in the required content of marine insurance policies. The requirements for a marine insurance policy in Australia are set out in MIA s 29, which states

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1069 ALRC DP 63 Question 39.

1070 M Mustill & J Gilman *Arnould's Law of Marine Insurance and Average* 16th ed Vol I Stevens & Sons London 1981, 224.

1071 *Ibid.*

1072 MIA (UK) s 24(1); MIA s 30(1).

1073 MIA (UK) s 26(1); MIA s 32(1).

A marine policy must specify:

- (a) the name of the assured, or of some person who effects the insurance on his behalf;
- (b) the subject-matter insured and the risk insured against;
- (c) the voyage, or period of time, or both, as the case may be, covered by the insurance;
- (d) the sum or sums insured;
- (e) the name or names of the insurers.

15.33 In the UK, the Finance Act 1959 (UK) repealed s 23(2)–(5) of the MIA (UK), which were equivalent to MIA s 29(b)–(e), so that only the requirement that the policy specify the name of the insured or of some person who effects the insurance on its behalf remains, apart from the designation of the subject matter with reasonable certainty.<sup>1074</sup> The same position applies in New Zealand.<sup>1075</sup> In Canada, the full requirements have been retained.<sup>1076</sup>

15.34 The Discussion Paper suggested that s 29(b)–(e) of the MIA be repealed to bring the MIA in line with the MIA (UK).<sup>1077</sup> Submissions were generally in favour of this proposal<sup>1078</sup> although one submission opposed it.<sup>1079</sup> The Insurance Council expressed concern that the slip should contain minimum information to detail the risk with some certainty.<sup>1080</sup> One submission did not support repeal of these clauses on the basis that, if a slip is to be accepted as evidence, it should detail the risk with some certainty and also state who the insurers are.<sup>1081</sup> Section 29, however, does not deal with the slip.

15.35 Being a contract in some ways like all others, a contract of marine insurance is bound by the general rule of contract law that requires the terms of the contract to be sufficiently certain.<sup>1082</sup> How this common law principle would interact with a reduced s 29 is unclear. In principle, the common law would still apply by virtue of s 4 unless s 29, in whatever form it appears, can be regarded as inconsistent with and overriding the common law.

1074 MIA (UK) s 26(1), equivalent to MIA s 32(1).

1075 MIA (NZ) s 23.

1076 MIA (Can) s 26.

1077 ALRC DP 63 Draft proposal 16.

1078 E Laryea *Submission 4*; K Carruthers *Submission 9*; MLAANZ *Submission 12*.

1079 A Street *Submission 15*.

1080 Insurance Council of Australia *Submission 11*.

1081 P Grieve *Submission 6*.

1082 N Seddon & M Ellinghaus *Cheshire & Fifoot's Law of Contract* 7th Aust ed Butterworths Sydney 1997, 210; see *Upper Hunter County District Council v Australian Chilling & Freezing Co* (1968) 118 CLR 429, 436, 437 (Barwick CJ); see also *G Scammell & Nephew Ltd v H C & J G Ouston* [1941] AC 251, 255 (Viscount Maugham).

15.36 Concerns were raised in consultation that reform in this area should not encourage poor practices in terms of issuing policies.<sup>1083</sup> One option which would prevent this would be for the MIA to contain a provision along the lines of s 74 of the ICA, which states that, upon a written request from the insured, the insurer must supply a document setting out the provisions of the contract, that is, the policy document. This suggestion was raised in the Discussion Paper<sup>1084</sup> and received support in submissions.<sup>1085</sup> In particular, the Insurance Council of Australia commented that this requirement was fundamental to the interests of international trade and in recognising the interests of banks and mortgagors.<sup>1086</sup> However, MIA s 58 already largely accomplishes this.

15.37 On balance, the Commission does not feel that any further restatement of the insurer's obligation in this regard is required. It should be noted that the insurer's obligation to issue the policy under s 58 only arises once the premium has been paid or tendered but no time period within which this must be done is stipulated. Section 26 of the MIA (NZ)<sup>1087</sup> is more strongly worded in that it covers insurers' agents as well as insurers and triggers the obligation once the insurer has taken credit for the premium or other consideration. MIA s 58 could be expanded in this way although that is unlikely to be of great importance. However, the existing requirement that premium must be paid or tendered before the policy has to be issued should deal with the Insurance Council's concern that insurers have the ability to handle circumstances where premium is not paid. This concern no doubt arises in part from MIA s 60, which provides that in the absence of fraud a policy issued by a broker acknowledging receipt of the premium is conclusive as between the insurer and insured, though the insurer retains its rights against the broker.

15.38 Throughout this report the Commission has endeavoured to move the law of marine insurance to a point where all the terms of the contract are to be found on the face of the contractual documents (ideally, the policy itself) or incorporated into them. There is a focus on the insertion of express terms to define the parties' obligations rather than reliance on the Act to interpret or imply those obligations. It would be contrary to this general approach to suggest that the basic requirements relating to the content of the fundamental contractual document should be loosened unless there is good reason to do so. The Commission is not aware of such reason and considers that the minimum requirements set out in MIA s 29, which in any event are quite modest, should be retained.

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1083 Legal practitioners *Consultation* Perth 22 November 2000.

1084 ALRC DP 63 Question 40.

1085 K Carruthers *Submission 9*; MLAANZ *Submission 12*; Insurance Council of Australia *Submission 11*.

1086 Insurance Council of Australia *Submission 11*.

1087 See para 15.7.

## Types of marine insurance policies

15.39 In Australia, marine insurance policies generally provide either cargo or hull insurance. The MIA specifically distinguishes between voyage,<sup>1088</sup> time<sup>1089</sup> and floating policies<sup>1090</sup> and policies that are valued or unvalued.<sup>1091</sup> Some policies may combine both voyage and time<sup>1092</sup> and these are known as ‘mixed policies’.

15.40 Voyage policies relate to a specific voyage and are generally used to insure cargo rather than hull and machinery. The duration of the period of insurance is governed by the relevant policy clauses. Historically, cargo voyage cover related to the period from lifting of cargo to unloading from the ship.<sup>1093</sup> Modern voyage policies generally cover the goods on a ‘warehouse to warehouse’ basis, for example, as defined in the Institute Cargo Clauses transit clause<sup>1094</sup> or by reference to the passing of risk under the terms of international contracts for sale of goods.<sup>1095</sup>

15.41 Most hull and freight insurance is placed under time policies, which are self-evidently policies for a fixed period of time. Time policies are usually annual and may be renewable. They may be restricted in the type of adventure insured or by geography.<sup>1096</sup>

## Limitation on time policies

15.42 The MIA states that a time policy made for a period over 12 months is invalid, except that an extension of up to 30 days may be made for a ship to reach its destination or complete a voyage.<sup>1097</sup> This provision, a legacy of UK stamp duty legislation, has been criticised for being unnecessarily restrictive and no longer serving any real purpose.<sup>1098</sup> The equivalent provision of the MIA (UK), s 25(2),

1088 A voyage policy is a contract to insure the subject matter from one specific place to another specific place or places: MIA s 31(1).

1089 A time policy is a contract to insure the subject matter for a definite period of time: MIA s 31(2).

1090 Floating policies describe the insurance and general terms and leave the name of ships and other particulars to be defined by subsequent declaration: MIA s 35.

1091 MIA s 33, 34.

1092 Section 31(1) of the MIA states that a contract for both time and voyage may be included in the same policy.

1093 R Thomas ‘Cargo Insurance: Issues Arising from the Standard Cover Provided by the London Institute Cargo Clauses’ in M Huybrechts E Van Hooydonk & C Dieryck (eds) *Marine Insurance at the Turn of the Millennium* vol I Intersentia Antwerp 1999, 325, 328.

1094 See Institute Cargo Clauses (A) cl 8.1.

1095 eg see International Chamber of Commerce *Incoterms 2000* ICC Publishing SA Paris 1999.

1096 H Bennett *The Law of Marine Insurance* Clarendon Press Oxford 1996, 260.

1097 MIA s 31(2).

1098 D Luxford ‘The Marine Insurance Act: Chronologically Challenged Legislation?’ *Paper Maritime Law Association of Australia and New Zealand Annual Conference Wellington New Zealand November 1995*, 38; M Thompson ‘Reform of the Law of Marine Insurance’ (1993) 5 *Insurance Law Journal* 195, 204.

was repealed by the Finance Act 1959 (UK).<sup>1099</sup> The equivalent provision in New Zealand<sup>1100</sup> was repealed by the Marine Insurance Amendment Act 1975 (NZ). Section 29(3) of the Marine Insurance Act 1993 (Can) states that a marine policy is a time policy if the contract insures the subject matter for a definite period. No restriction is placed on the duration of a time policy.

15.43 Stamp duty is no longer payable on time policies in any Australian state or territory. Accordingly, the *raison d'être* of this provision has disappeared. If the Commission's recommendations in relation to the implied warranty of unseaworthiness and commencement of risk are accepted, this would remove the only other places where the distinction between time and voyage policies is of importance in the Act itself. In the other hand, the distinction is important in business and there is no reason for it not to be retained in that context.

15.44 The Discussion Paper proposed that MIA s 31(2), which restricts time policies to 12 months, be repealed.<sup>1101</sup> This proposal received support in submissions and the Commission recommends the removal of this restriction as an unnecessary hindrance to current marine insurance practice.

15.45 The distinction between time and voyage policies is set out in MIA s 31(1). Apart from the time restriction in s 31(2), which the Commission recommends be repealed, the only other functions of this distinction within the Act is in relation to the warranty of seaworthiness in s 45 and the implied condition as to the commencement of the risk in s 48(1), which applies only to voyage policies. The warranty of seaworthiness in relation to voyage policies is found in s 45(1); by contrast, s 45(5) states that there is no such warranty implied in time policies but that in certain circumstances the insurer is not liable for a loss attributable to unseaworthiness. If the Commission's recommendations in relation to the warranty of seaworthiness are adopted, this distinction will be lost. Similarly, the Commission's proposal that s 48 be repealed in favour of express terms does away with the point of distinction in this regard as well. As a result, the statutory distinction between voyage and time policies will have no further purpose in the Act except for the rather banal statement in s 31(1) that contracts for voyage and time insurance can be included in the same policy.

15.46 The distinction remains in general use, however, and will no doubt condition the minds of insurers and insurance intermediaries in their day-to-day business. Accordingly, even if the distinction between time and voyage policies has no ramification within the Act itself, the Commission proposes that s 31(1) be retained

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1099 The equivalent provision of the Marine Insurance Act 1908 (NZ), s 27(2), was repealed by s 4(1) of the Marine Insurance Amendment Act 1975 (NZ).

1100 MIA (NZ) s 27(2).

1101 ALRC DP 63 Draft proposal 18.

even if only to prevent any argument that the distinction itself has been abolished or that contracts of both sorts cannot be embodied in one combined policy.

### **Floating, open and annual policies**

15.47 Section 35 of the MIA refers to ‘floating policies’ which ‘describe the insurance in general terms, and leave the name of the ship or ships and other particulars to be defined by subsequent declaration’.<sup>1102</sup> This form of policy has largely become obsolete.<sup>1103</sup> In practice, cargo is generally insured under open or annual cover, which, unlike a floating policy, does not require the maximum amount of insurance to be stated.

15.48 Cargo open cover involves an agreement to provide insurance for all shipments of goods as agreed, subject to declaration by the insured at or about the time of shipment. Premium is payable per shipment or series of shipments and premiums are only paid when cargo is transported. Open cover is not usually restricted by time, continuing until cancelled by either party. Monthly declarations are made and debits for premiums are made monthly in arrears.<sup>1104</sup>

15.49 Annual cargo cover is more common than open cover. An annual policy provides cover for all shipments of goods, as agreed, which commence during the annual period specified in the policy. Premium is payable by deposit based on the estimated value of shipments at the beginning of the period and adjusted later based on the actual value of the shipments. Debits for premiums are taken twice a year.<sup>1105</sup>

15.50 Open and annual policies offer more flexibility than floating policies as they are not restricted to any sum insured although the value of any one shipment, or of cargo stored at any one place, may be limited. However, while floating policies are ‘policies’ in terms of s 29 and 32 of the MIA, it is doubtful whether open and annual cover would amount to a policy because of the lack of certainty of their subject matter.<sup>1106</sup> In practice, parties using such cover may agree that a certificate of insurance, sometimes issued electronically by the insurer, will represent a

1102 Thompson notes that floating policies that are arranged on an annual turnover basis do not seem to be caught by the wording of this section and there is no obligation on the insured to ‘honestly state’ the value for adjustment purposes: M Thompson ‘Reform of the Law of Marine Insurance’ (1993) 5 *Insurance Law Journal* 195, 204.

1103 D Luxford ‘The Marine Insurance Act: Chronologically Challenged Legislation?’ *Paper MLAANZ Annual Conference Wellington New Zealand 5–8 November 1995*, 27.

1104 Insurers *Consultation* Melbourne 6 June 2000.

1105 *Ibid.*

1106 See R Thomas ‘Cargo Insurance: Issues Arising from the Standard Cover Provided by the London Institute Cargo Clauses’ in M Huybrechts E Van Hooydonk & C Dieryck (eds) *Marine Insurance at the Turn of the Millennium* vol I Intersentia Antwerp 1999, 325, 334.

sufficient insurance document.<sup>1107</sup> In principle, however, the requirements of s 29 are mandatory as this is one provision which the MIA does not permit the parties to modify by agreement. This strict position is modified somewhat by s 32(4), which permits usage to be considered in determining if the subject matter has been designated with reasonable certainty. As usage permits open and annual policies with a degree of vagueness about the precise subject matter insured, s 32(4) it seems will overcome this part of the problem. The lack of a precise sum insured because no value is declared until after loss or arrival is accommodated by s 35(4), which deems the policy to be unvalued, in which case s 34 and 22 apply. The remaining requirements of s 29 would, it seems, be easily met in any event. The recommended repeal of the first sentence of s 28, which prevents the admission into evidence of contractual documents if no policy is issued, probably also assists. Accordingly the Commission suggests that there is probably little risk that open or annual policies will be held not to be policies. Even so, that conclusion is untested. To avoid uncertainty, there are a number of options.

15.51 The first option, contrary to the conclusion in paragraph 15.38, is to repeal some or all of s 29(b), (c) and (d). The Commission sees no reason on this or any other basis to repeal s 29(e). Although the Commission can find no evidence to support this hypothesis, it queries whether the indeterminate position of annual and open cover influenced the UK and New Zealand amendments to their equivalents to s 29. The second option is to declare open and annual policies to be policies in s 35, as floating policies are, and, either in addition or alternatively, provide that all such policies (or indeed, all policies of any type) are not invalid by reason only that they do not comply fully with the formal requirements of s 29.

15.52 The Commission recommends that s 29 be amended to include a new subsection stating that no marine policy is invalid by reason only that it does not comply with the existing formal requirements in what will become s 29(1).

15.53 Secondly, s 35(1) should be expanded to include open and annual policies, thus declaring them to be 'policies' for the purposes of the MIA and making other necessary changes to the description of the subject matter in that subsection. The heading to s 35 should be amended to reflect these changes.

15.54 Finally, s 35(3) should be re-worded to make it clear that the opening words, 'unless the policy otherwise provides,' extend to the opening clause of the second sentence of that subsection.

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1107 Ibid 335.

15.55 The Discussion Paper suggested that the MIA could be amended to remove definitions of types of cover with the aim of giving open and annual cover full recognition as evidence of the contract of insurance and to allow them to be treated as a policy.<sup>1108</sup> This proposal was supported in submissions.<sup>1109</sup> In light of the Commission's recommendations in the three preceding paragraphs, it is not necessary to pursue this suggestion. Since valued, unvalued, time and voyage policies are used elsewhere in the Act and are still relevant to marine insurance practice, the Commission recommends that these definitions remain.

15.56 Even if open and annual cover were not be recognised as marine insurance policies because of failure to comply with MIA s 29 and 32, recommendation 37, which removes the requirement for the contract of marine insurance to be embodied in a policy before being admissible in evidence in an action for recovery of a loss under the contract, will allow open and annual cover to be given as evidence of the contract of insurance.

### **Assignment of open and annual cover**

15.57 Assignment of the policy is dealt with in s 56 and 57. Assignment of the contract is not mentioned at all in the Act. A contract is a chose in action assignable at common law. The fact that it is not included in s 56 or 57 suggests that a contract not yet embodied in a policy is unassignable. This seems to be unnecessarily restrictive unless the contract provides specifically for that outcome. The Commission's policy expressed in recommendation 37 and elsewhere is to eliminate unnecessary formality and any distinction between the policy and contract. Accordingly the Commission recommends that s 56 and 57 be expanded to include a reference to a contract whenever a policy is mentioned with appropriate changes to the headings.

### **Electronic transactions**

15.58 Although the MIA is flexible and in many areas allows for changing market practice, electronic transactions were not envisaged at the time of drafting but must be accommodated by the Act.

15.59 Various international efforts have been made to set up legal frameworks for electronic transactions. For example, the UNCITRAL (United Nations Commission

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1108 ALRC DP 63 Draft proposal 19.

1109 D Chaplin *Submission 3*; P Grieve *Submission 6*; K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*; National Bulk Commodities Group *Submission 14*; A Street *Submission 15*. Alexander Street SC supported the proposal provided that there was a clear distinction between an open cover policy requiring declarations and an open offer to issue policies.



on International Trade Law) Model Law on Electronic Commerce 1996 covers issues such as the meaning of writing, signature and originality in the context of electronic documents.<sup>1110</sup> The European Model EDI (electronic data interchange) Agreement also deals with the issue of electronic transactions.<sup>1111</sup>

15.60 In Australia, changes have been made to the laws governing carriage of goods by sea to allow for electronic transactions. A Sea-Carriage Documents Act has been passed in each state and in the Northern Territory to replace old bills of lading legislation.<sup>1112</sup> Each specifically permits the use of electronic equivalents to bills of lading. The *Carriage of Goods by Sea Act 1991* (Cth) was amended in 1997 to cover documents in electronic form.<sup>1113</sup> However, the legal implications of electronic transactions involving marine insurance have not yet been addressed.

15.61 *The Sea-Carriage Documents Act 1997* (NSW) contains the following definition of the term 'data message'.<sup>1114</sup>

Data message means information generated, stored or communicated by electronic, optical or analogous means including, but not limited to, electronic data interchange, electronic mail, telegram, telex and telecopy.

15.62 Section 6 of the Act sets out its application to electronic and computerised sea-carriage documents and gives definitions of certain terms.<sup>1115</sup>

- (1) Subject to this section, this Act applies:
- (a) in relation to a sea-carriage document in the form of a data message in the same way as it applies in relation to a written sea-carriage document, and
  - (b) in relation to the communication of a sea-carriage document by means of a data message in the same way as it applies in relation to the communication of a sea-carriage document by other means.

1110 G Zekos 'The use of Electronic Technology in Maritime Transport: The Economic Necessity and the Legal Framework in European Union Law' (1998) 3 *Web Journal of Current Legal Issues* <http://webjcli.ncl.ac.uk/1998/issue3/zekos3.html> (11 December 2000).

1111 Ibid.

1112 *Sea-Carriage Documents Act 1997* (NSW); *Sea-Carriage Documents Act 1998* (Vic); *Sea-Carriage Documents Act 1996* (Qld); *Sea-Carriage Documents Act 1998* (SA); *Sea-Carriage Documents Act 1997* (Tas); *Sea-Carriage Documents Act 1997* (WA); *Sea-Carriage Documents Act 1998* (NT); see E Laryea 'Dematerialisation of Insurance Documents in International Trade Transactions: A Need for Legislative Reform' (2000) 23 *UNSW Law Journal* 78, 80.

1113 COGSA s 7 was amended in 1997 to allow for regulations to add a schedule to provide inter alia for 'the coverage of a wider range of sea carriage documents (including documents in electronic form)'.

1114 *Sea-Carriage Documents Act 1997* (NSW) s 5. A similar definition is contained in *Sea-Carriage Documents Act 1996* (Qld) s 3; *Sea-Carriage Documents Act 1998* (Vic) s 5; *Sea-Carriage Documents Act 1998* (SA) s 4; *Sea-Carriage Documents Act 1997* (Tas) s 4; *Sea-Carriage Documents Act 1997* (WA) s 5; *Sea-Carriage Documents Act 1998* (NT) s 5.

1115 Similar definitions are contained in *Sea-Carriage Documents Act 1996* (Qld) s 4; *Sea-Carriage Documents Act 1998* (Vic) s 6; *Sea-Carriage Documents Act 1998* (SA) s 5; *Sea-Carriage Documents Act 1997* (Tas) s 5; *Sea-Carriage Documents Act 1997* (WA) s 6; *Sea-Carriage Documents Act 1998* (NT) s 6.

(2) This Act applies under subsection (1) with necessary changes and in accordance with procedures agreed between the parties to the contract of carriage.

(3) Without limiting the generality of subsection (2), in this Act, in the application of the following terms to a sea-carriage document in the form of a data message, or to the communication of a sea-carriage document by means of a data message:

**delivery** includes any form of communication which constitutes delivery under the terms of the contract of carriage.

**endorsement** includes any form of authorisation which constitutes endorsement under the terms of the contract of carriage.

**possession**, in relation to the document, includes being in receipt of the document in any manner which constitutes possession under the terms of the contract of carriage.

**signed** includes authentication in any manner which constitutes signing under the terms of the contract of carriage.

15.63 While the definition of ‘data message’ is broad and appears to cover all types of electronic messages, the definitions in s 6 refer directly to the terms of the sea-carriage document in the form of, or communicated as, a data message without any closer definition of those terms. Various aspects of the communication of the document are defined by the terms of the contract. This prevents the Act being confined to any particular form of electronic document or transmission, which is important in a world where technology changes rapidly, and leaves it to the parties to determine what system they wish to use.

15.64 The *Electronic Transactions Act 1999* (Cth) (‘ETA’) and the Electronic Transactions Regulations 2000 (Cth) were introduced to deal with the legal issues arising from the use of electronic commerce and to form the basis of a uniform national legislation.<sup>1116</sup> The ETA was based on the UNCITRAL Model Law on Electronic Commerce. The ETA and the regulations came into effect on 15 March 2000 but apply only to certain legislation listed in the regulations. After 1 July 2001 the ETA will apply to all Commonwealth laws (such as the MIA) except those that are specifically excluded.

15.65 Even if the ETA is to cover contracts covered by the MIA there is support for the view that the MIA should in any event be amended to deal expressly with electronic transactions.<sup>1117</sup> The Law Council of Australia in its submission recommended that the MIA not exclude the operation of the ETA.<sup>1118</sup> There does not appear to be any need to do that expressly as the ETA will automatically apply to contracts governed by the MIA and the ICA without further elaboration from 1 July 2001.

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1116 D Williams Attorney-General ‘Australia at the forefront of the information economy’ *News release* 14 March 2000. [http://law.gov.au/aghome/agnews/2000newsag/711\\_00.htm](http://law.gov.au/aghome/agnews/2000newsag/711_00.htm) (11 May 2000).

1117 E Laryea ‘Dematerialisation of Insurance Documents in International Trade Transactions: A Need for Legislative Reform’ (2000) 23 *UNSW Law Journal* 78, 104.

1118 Law Council of Australia *Submission 10*.

15.66 The admissibility of the slip into evidence is not affected by the electronic nature of the slip whether or not the Commission's recommendations in this regard are adopted.<sup>1119</sup> However, MIA s 30(1) requires that a contract of marine insurance be signed by or on behalf of the insurer, presumably meaning each insurer. A corporate seal is a sufficient but not mandatory form of signature on behalf of a corporation.<sup>1120</sup>

15.67 The Discussion Paper suggested amendment of MIA s 30 to allow a marine insurance policy to be issued by an insurer electronically without the requirement for a physical or manual signature. This draft proposal received support in submissions.<sup>1121</sup> One submission suggested that the policy should contain the secure name and address of the insurer to avoid fraud.<sup>1122</sup> If authentication is a concern, it may be more advisable to prescribe regulations for electronic signature.

15.68 Section 10 of the ETA sets out the requirements for electronic signature as follows

- 10(1) If, under a law of the Commonwealth, the signature of a person is required, that requirement is taken to have been met in relation to an electronic communication if:
- (a) in all cases — a method is used to identify the person and to indicate the person's approval of the information communicated; and
  - (b) in all cases — having regard to all the relevant circumstances at the time the method was used, the method was as reliable as was appropriate for the purposes for which the information was communicated; and
  - (c) if the signature is required to be given to a Commonwealth entity, or to a person acting on behalf of a Commonwealth entity, and the entity requires that the method used as mentioned in paragraph (a) be in accordance with particular information technology requirements — the entity's requirement has been met; and
  - (d) if the signature is required to be given to a person who is neither a Commonwealth entity nor a person acting on behalf of a Commonwealth entity — the person to whom the signature is required to be given consents to that requirement being met by way of the use of the method mentioned in paragraph (a).

15.69 The ETA prescribes broad requirements to be satisfied before an electronic signature may be accepted. Other electronic transactions legislation is more specific. For example, some American states have adopted a statutory system that refers to a particular form of technology by which electronic signatures may be

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1119 See para 15.10–15.24.

1120 MIA s 30(1).

1121 K Carruthers *Submission 9*, Insurance Council of Australia *Submission 11*, MLAANZ *Submission 12*.

1122 D Chaplin *Submission 3*.

made.<sup>1123</sup> While it is argued that adopting particular technologies allows a detailed regulatory system to be developed, legislation that is technologically neutral has greater flexibility and is able to adapt to changing methods of electronic transactions. This broad approach is also more in keeping with the existing style of the MIA, which is one of the reasons that the MIA has largely kept pace with changes in the marine insurance industry.

15.70 The Commission considers that it is sufficient to rely on the ETA in this regard. This will allow consistency with similar requirements under other federal legislation. If that is done, there does not appear to be any need for particular amendment to MIA s 30(1). Such amendment might put the position beyond dispute (if there is room for any) but a similar argument would apply to all such provisions in all federal legislation. The ETA was no doubt designed in part to obviate the need to trawl through all federal legislation with a view to making detailed and particular amendments unless they were warranted by particular circumstances. For this reason and for the sake of consistency, the Commission recommends that amendment to the law of marine insurance in this regard should be based on the ETA and that no further amendment to s 30(1) is warranted.

15.71 Another area of the MIA that may need updating in view of the increasing use of electronic communications is assignment of the marine insurance policy. Section 56(3) of the MIA states that a marine policy may be assigned 'by indorsement thereon or in other customary manner'. Although it could be argued that indorsement upon an electronic document by electronic means could well in due course fall within the meaning of a 'customary manner',<sup>1124</sup> the MIA assumes a physical document. Therefore, this section could be amended to permit assignment by electronic means or otherwise as agreed by the parties. However, section 8(1) of the ETA states that

For the purposes of a law of the Commonwealth, a transaction is not invalid because it took place wholly or partly by means of one or more electronic communications.

15.72 Therefore, the Commission considers that it is sufficient to rely on the ETA in this regard.

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1123 Electronic Commerce Expert Group *Electronic Commerce: building the legal framework* Report of the Electronic Commerce Expert Group to the Attorney-General 31 March 1998, 120, <http://www.law.gov.au/aghome/advisory/eceg/single.htm> (12 December 2000).

1124 For further discussion see E Laryea 'Dematerialisation of Insurance Documents in International Trade Transactions: A Need for Legislative Reform' (2000) 23 *UNSW Law Journal* 78, 94.

Recommendation 37. **MIA s 28 should be amended to permit a contract of marine insurance to be admissible in evidence in legal proceedings as evidence of the contract.**

Recommendation 38. **MIA s 31(2), which restricts time policies to 12 months in duration, should be repealed as unnecessarily restrictive.**

Recommendation 39. **The existing MIA s 29 should become s 29(1) and a new subsection 29(2) should be inserted stating that no marine policy is invalid by reason only that it does not comply with the existing formal requirements in s 29(1).**

Recommendation 40. **MIA s 35(1) should be amended to include open and annual policies and to make all necessary changes to the description of the subject matter in s 35(1) and to the heading to s 35.**

Recommendation 41. **MIA s 35(3) should be amended to make it clear that the words ‘Unless the policy otherwise provides’ extend to the opening clause of the second sentence so that they apply to the requirement that all declarations under floating, open or annual policies must comprise all consignments within the terms of the policy.**

Recommendation 42. **MIA s 56 should be amended to include assignment of contracts as well as policies. If, contrary to recommendation 29, MIA s 57 is not repealed, it should also be amended to include assignment of contracts as well as policies. The words ‘or contract’ should be inserted into these sections and the heading wherever reference is made to a policy.**

## **Modernising the MIA**

15.73 The MIA has been virtually unchanged since it codified the common law in 1909. Since that time some of its provisions have become obsolete or outdated due to changes in shipping, technology and insurance industry practice. Some of these provisions are discussed in this chapter.

15.74 It should be appreciated that some provisions, while appearing outdated, may still be relevant today or have a precise and appropriate meaning as interpreted by the courts. ‘Modernisation’ of such settled terminology could result in unnecessary litigation or lead to uncertainty. The amendment of established wordings should be approached with reserve unless brought about by the need for substantive amendment, and even then care should be taken to preserve valuable

expressions supported or explained by extensive case law even if they are perhaps quaint or somewhat out of touch with the contemporary vernacular.

15.75 The Department of Transport and Regional Services has noted that

the experience of this Department in recent changes to the Carriage of Goods by Sea legislation, suggests a cautious approach to changing legislation only for the purpose of modernising language ... the modernisation of language can introduce significant change in the meaning the legislation and significant uncertainty in the community most directly affected by such changes. Such changes require extensive community consultation to ensure that, in modernising, we do not effect any fundamental changes in the rights that are intended to be conferred by the legislation.<sup>1125</sup>

15.76 Such changes also have the effect of reducing the value of existing case law in settling claims, which can lead to increased litigation costs in the short to medium term.

### Form of policy and definitions

15.77 Section 36 of the MIA states that a policy may be in the form set out in the Second Schedule, which incorporates the Lloyd's SG Policy. This wording contains archaic terms and concepts and has long been subject to criticism. The form has been described as

a strange, very peculiar, absurd, incoherent, clumsy, imperfect, obscure, incomprehensible, tortuous document, drawn up with much laxity, by a lunatic with a very private sense of humour, in a form which is past praying for.<sup>1126</sup>

15.78 In practice, this form of policy is used only extremely rarely<sup>1127</sup> and the Commission was surprised to learn during consultations that it is sometimes invoked in contemporary policies. Although the Second Schedule wording resonates with legal history, it is generally agreed that it should be deleted. However, the Second Schedule also contains 17 rules of interpretation not appearing elsewhere in the Act and which may remain of importance.

To the extent that the defined terms remain in current usage, the rules of interpretation retain their value as expressions of the market's understanding and are given statutory force by [section 36(2) of the MIA].<sup>1128</sup>

1125 Department of Transport and Regional Services *Submission 2*.

1126 D O'May *Marine Insurance — Law and Policy* Sweet & Maxwell London 1993, 8, amalgamating epithets drawn from English case law.

1127 Although it is conceivable that the Lloyd's Ships and Goods Policy might be used where an insurer is using the superseded pre-1983 Institute cargo clauses.

1128 S Derrington 'The Law Relating to Non-Disclosure, Misrepresentation and Breach of Warranty in Contracts of Marine Insurance: A Case for Reform' *Ph D thesis* University of Queensland November 1998, 59.

15.79 They are entitled Rules for Construction of Policy and are said to be used for the construction of a policy in the SG “or other like form” where the context does not otherwise require.

15.80 The Commission considers that the form of policy should be removed from the Second Schedule but, in view of the fact that the Rules for Construction of Policy may still be relevant to the interpretation of policy terms, these should be retained and re-enacted in a new interpretation section, s 3A. The only changes that should be made to these definitions is the gender neutralisation of references to ships and the removal of the subjunctive. Section 36 of the MIA, which refers to the policy form, would become redundant and should also be repealed.

15.81 The Canadian Marine Insurance Act 1993, based on the United Kingdom Act, contains more extensive definition and interpretation sections than the Australian and United Kingdom Acts.<sup>1129</sup> This is a feature of modern legislative drafting that assists in statutory interpretation. The Discussion Paper suggested that s 36 and the Second Schedule of the MIA be repealed but that definitions worthy of retention should be moved into the body of the MIA.<sup>1130</sup> This proposal was supported in submissions<sup>1131</sup> although one submission considered that the terms in the Second Schedule remained relevant<sup>1132</sup> and another warned against discarding seemingly redundant terms that might later become important again, such as piracy.<sup>1133</sup>

15.82 The Discussion Paper asked if the MIA should contain a more extensive definitions section, such as that found in the Canadian Marine Insurance Act 1993.<sup>1134</sup> There was support for this idea in submissions.<sup>1135</sup> However, the Commission believes that the existing definitions in MIA s 3 and the Second Schedule are clearly understood and do not require the introduction of new terms. Some additional terms have been inserted into the MIA by the Commission’s other recommendations but the Commission does not see the need to create a new, extensive dictionary section.

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1129 The Canadian Act includes definitions of action, contract, freight, goods, insurable property, marine adventure, marine policy, maritime perils, movable, ship, as well as other definitions contained throughout the Act.

1130 ALRC DP 63 Draft proposal 20.

1131 D Chaplin *Submission 3*; P Grieve *Submission 6*; K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*; National Bulk Commodities Group *Submission 14*; A Street *Submission 15*.

1132 Law Society of WA *Submission 7*.

1133 P Grieve *Submission 6*.

1134 ALRC DP 63 Question 46.

1135 K Carruthers *Submission 9*; Insurance Council of Australia *Submission 11*; MLAANZ *Submission 12*.

### Measure of indemnity

15.83 It has been suggested that there is a case for updating the language in those parts of the MIA that deal with the measure of average, salvage, and other liability of insurers for loss.<sup>1136</sup> In particular, the provisions on general average<sup>1137</sup> may need to be updated to take into account the fact that the law of general average is now subject to its own international regime, the York-Antwerp Rules. The Discussion Paper asked whether there was a need to update the language of the MIA or amend or repeal any of the provisions dealing with the measure of average, salvage, and other liability of insurers for loss.<sup>1138</sup>

15.84 Only one submission commented on this matter and was not in favour of any change.<sup>1139</sup> One submission noted that the MIA should reflect the fact that general average is now subject to its own international regime in the York-Antwerp rules but that caution should be exercised as changes might reduce the value of existing case law in settling claims and could lead to increased litigation.<sup>1140</sup>

15.85 In view of these concerns, the Commission does not recommend any change to the MIA in these areas.

### Mutual insurance

15.86 Section 91 of the MIA provides

91(1) Where two or more persons mutually agree to insure each other against marine losses there is said to be a mutual insurance.

(2) The provisions of this Act relating to the premium do not apply to mutual insurance, but a guarantee, or such other arrangement as may be agreed upon, may be substituted for the premium.

(3) The provisions of this Act, in so far as they may be modified by the agreement of the parties, may in the case of mutual insurance be modified by the terms of the policies issued by the association, or by the rules and regulations of the association.

(4) Subject to the exceptions mentioned in this section, the provisions of this Act apply to a mutual insurance.

1136 D Luxford 'The Marine Insurance Act: Chronologically Challenged Legislation?' *Paper* MLAANZ Annual Conference Wellington 5–8 November 1995.

1137 General average is the principle that losses sustained or expenditure incurred in time of peril and for the common good should be shared among those interested in the adventure according to their shares in the adventure. For example, if a ship is threatened with total loss by being dashed on a reef, the master might jettison part of the cargo to save the ship and the remainder of the cargo. The loss is not borne solely by those whose cargo is jettisoned but shared among all parties involved.

1138 ALRC DP 63 Question 47.

1139 MLAANZ *Submission 12*.

1140 Dept of Transport and Regional Services *Submission 2*.



15.87 As discussed in the Discussion Paper, P & I clubs provide mutual insurance.<sup>1141</sup> Historically, shipowners formed together in unincorporated associations in which they each entered their ships for a certain sum and each undertook to contribute to any loss that their fellow members might incur. However, following the enactment of the Companies Act 1862 (UK) and the decision in *Re Padstow Total Loss and Collision Assurance Association*,<sup>1142</sup> those associations were registered under the Companies Act. As a result it is the association that is the insurer — the members do not directly provide insurance for each other.<sup>1143</sup>

15.88 It has been suggested that, in the light of this, the definition of mutual insurance in s 91(1) of the MIA is not strictly accurate as its wording implies that the member is insured by other individual members rather than by an incorporated association.<sup>1144</sup> The Discussion Paper asked how often were the provisions in the MIA relating to mutual insurance relied on and was any modification required.<sup>1145</sup> The Discussion Paper also asked if the definition of mutual insurance in s 91(1) should be amended to remove any implication that the member is insured by other individual members, rather than by an incorporated association.<sup>1146</sup>

15.89 Those few submissions that commented on this area were not in favour of change<sup>1147</sup> except for one submission that supported updating the definition of ‘mutual insurance’ in the light of the registration of associations under the Companies Act 1862 (UK).<sup>1148</sup>

15.90 However, s 91(3) oddly refers to an ‘association’ which is nowhere else described or defined. It is presumably the group of mutual insurers referred to in s 91(1). To remove uncertainty, s 91(1) could be expanded to refer expressly to an association formed by two or more persons in order to insure each other. The Commission recommends that that amendment be made.

### **Other obsolete or outdated provisions**

15.91 It has been suggested that particular average warranties (s 82) and provisions relating to rats and vermin (s 61(2)(c)) may have no modern application.<sup>1149</sup> There

1141 ALRC DP 63 para 1.23–1.26.

1142 (1882) LR 20 Ch. 137.

1143 M Tilley ‘The Origin and Development of the Mutual Shipowners’ Protection & Indemnity Associations’ (1986) *Journal of Maritime Law and Commerce* 261, 267.

1144 *Ibid* 269–70.

1145 ALRC DP 63 Question 48.

1146 ALRC DP 63 Question 49.

1147 MLAANZ *Submission 12*.

1148 Law Society of WA *Submission 7*.

1149 D Luxford ‘The Marine Insurance Act: Chronologically Challenged Legislation?’ *Paper* MLAANZ Annual Conference Wellington 5–8 November 1995, 33.

may also be other provisions that no longer apply in practice or could be amended to reflect current practice but this has not been discussed elsewhere in the available literature. For example, s 5 (Application of certain Imperial and State Acts) is no longer applicable.

15.92 The Discussion Paper asked if s 5, s 61(2)(c) and s 82 of the MIA or any other provisions of the MIA should be amended or repealed.<sup>1150</sup> Only one submission commented on these questions and was not in favour of any change.<sup>1151</sup> In view of this response the Commission does not recommend changes to any other obsolete provisions.

### **Gender**

15.93 Another aspect in which the MIA is out of date in terms of language is the reference to the insurer and insured in the masculine only and to vessels in the feminine. This may well have reflected the reality of commerce at the beginning of the 20th century but it is unacceptable now.

15.94 No submissions were received on this question and, it must be conceded, it is relatively peripheral. The options are to make changes towards gender neutrality in those portions of the MIA that are otherwise to be amended, or to systematically go through the Act to make those changes even in provisions that are not otherwise touched.

15.95 On balance, the Commission does not recommend the latter course. The Commission's recommended alterations to the MIA include the gender neutralisation of those portions that are the subject of other changes but do not include proposed amendments where the only proposed change would relate to gender.

**Recommendation 43. MIA s 36 and the Form of Policy contained in the Second Schedule of the MIA should be repealed. The Rules for Construction of Policy in the Second Schedule should be re-enacted in a new s 3A in the MIA.**

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1150 ALRC DP 63 Questions 50, 51.

1151 MLAANZ *Submission 12*.

**Recommendation 44. MIA s 91(1) should be amended to refer expressly to an association formed by two or more persons in order to insure each other.**



## **Appendix A**

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<b>Name</b>	<i>Submission number</i>
The Law Society of Western Australia	7
Chaplin D, Associated Marine Insurers	3
Clarke R, Gault Armstrong & Kemble (WA) Pty Ltd	16 and 18
Carruthers K, The Hon Justice, NSW Court of Appeal	9
Department of Transport and Regional Services	2
Derrington S	13
Grieve P	6
Laryea E	4
Law Council of Australia	10
Levingstons	1
Lewins K	8
National Bulk Commodities Group	14
Maritime Law Association of Australia & New Zealand	12
McAlpine R, Australian Chamber of Shipping Ltd	5
The Insurance Council of Australia Ltd	11
Street A, SC	15
Wise A, Panama Maritime Documentation Services Inc	17



# Appendix B

## Amended *Marine Insurance Act*

This appendix sets out the text of the *Marine Insurance Act 1909* as amended if the Commission's recommendations set out in this report were adopted in full, annotated in the following style.

- Words to be deleted are struck through
- New sections and new words are in bold type and are underlined
- Notes in square brackets are for guidance only.

The recommended amendment to the *Insurance Contracts Act 1984* is not included in this appendix but is set out in schedule 2 of the draft Marine Insurance Amendment Bill found in appendix C.

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## PART I—PRELIMINARY

**Short title and commencement**

1. This Act may be cited as the Marine Insurance Act 1909 and shall commence on a day to be fixed by proclamation.

[No change]

**Interpretation**

3 In this Act, unless the contrary intention appears:

“**Action**” includes counterclaim and set-off:

“**Freight**” includes the profit derivable by a ship-owner from the employment of his ship to carry his own goods or movables, as well as freight payable by a third party, but does not include passage money:

“**Movables**” means any movable tangible property, other than the ship, and includes money, valuable securities, and other documents:

“**Policy**” means a marine policy.

[No change]

**Construction of terms in policy**

**3A** ~~The following are the rules referred to by this Act for~~ are to be applied in the construction of a policy in the above or other like form, where the context does not otherwise require:

**(1)** Lost or not lost Where the subject-matter is insured “lost or not lost”, and the loss has occurred before the contract is concluded, the risk attaches unless, at such time, the assured was aware of the loss, and the insurer was not.

**(2)** From Where the subject-matter is insured “from” a particular place, the risk does not attach until the ship starts on the voyage insured.

**(3)** At and from (a) Where a ship is insured “at and from” a particular place, and it is at that place in good safety when the contract is concluded, the risk attaches immediately.

**(b)** If it is not at that place when the contract is concluded the risk attaches as soon as it arrives there in good safety, and, unless the policy otherwise provides, it is immaterial that it is covered by another policy for a specified time after arrival.

**(c)** Where chartered freight is insured “at and from” a particular place and the ship is at that place in good safety, when the contract is concluded the risk attaches immediately. If it is not there when the contract is concluded, the risk attaches as soon as it arrives there in good safety.

**(d)** Where freight, other than chartered freight, is payable without special conditions and is insured “at and from” a particular place, the risk attaches pro rata as the goods or merchandise are shipped; provided that if there is cargo in readiness which belongs to the ship-owner, or which some other person has contracted with him to ship, the risk attaches as soon as the ship is ready to receive such cargo.

**(4)** From the loading thereof Where goods or other movables are insured “from the loading thereof,” the risk does not attach until such goods or movables are actually on board, and the insurer is not liable for them while in transit from the shore to the ship.

- (5) *Safely landed* Where the risk on goods or other movables continues until they are “safely landed”, they must be landed in the customary manner and within a reasonable time after arrival at the port of discharge, and if they are not so landed the risk ceases.
- (6) *Touch and stay* In the absence of any further licence or usage, the liberty to touch and stay “at any port or place whatsoever” does not authorize the ship to depart from the course of its voyage from the port of departure to the port of destination.
- (7) *Perils of the seas* The term “perils of the seas” refers only to fortuitous accidents or casualties of the seas. It does not include the ordinary action of the winds and waves.
- (8) *Pirates* The term “pirates” includes passengers who mutiny and rioters who attack the ship from the shore.
- (9) *Thieves* The term “thieves” does not cover clandestine theft or a theft committed by any one of the ship’s company, whether crew or passengers.
- (10) *Restraint of princes* The term “arrest, &c., of kings, princes, and people” refers to political or executive acts, and does not include a loss caused by riot or by ordinary judicial process.
- (11) *Barratry* The term “barratry” includes every wrongful act wilfully committed by the master or crew to the prejudice of the owner, or, as the case may be, the charterer.
- (12) *All other perils* The term “all other perils” includes only perils similar in kind to the perils specifically mentioned in the policy.
- (13) *Average unless general* The term “average unless general” means a partial loss of the subject-matter insured other than a general average loss, and does not include “particular charges.”
- (14) *Stranded* Where the ship has stranded, the insurer is liable for the excepted losses, although the loss is not attributable to the stranding, provided that when the stranding takes place the risk has attached and, if the policy is on goods, that the damaged goods are on board.
- (15) *Ship* The term “ship” includes the hull, materials and outfit, stores and provisions for the officers and crew, and, in the case of vessels engaged in a special trade, the ordinary fittings requisite for the trade, and also, in the case of a steamship, the machinery, boilers, and coals and engine stores, if owned by the assured.
- (16) *Freight* The term “freight” includes the profit derivable by a ship-owner from the employment of his ship to carry his own goods or movables, as well as freight payable by a third party, but does not include passage money.
- (17) *Goods* The term “goods” means goods in the nature of merchandise, and does not include personal effects or provisions and stores for use on board. In the absence of any usage to the contrary, deck cargo and living animals must be insured specifically, and not under the general denomination of goods.

[From MIA Second Schedule]

**Saving of rules of common law**

4. The rules of the common law, including the law merchant, save in so far as they are inconsistent with the express provisions of this Act, shall apply to contracts of marine insurance.

[No change]

**Application of certain Imperial and State Acts**

5. The Imperial Acts and State Acts set out in the First Schedule shall not to the extent therein specified apply to any contract or policy of marine insurance to which this Act applies.

[No change]

**Application of Act**

6(1) This Act shall apply to marine insurance other than State marine insurance and to State marine insurance extending beyond the limits of the State concerned.

[No change]

(2) This Act does not apply to contracts of marine insurance made before the commencement of this Act.

[No change]

**PART II—MARINE INSURANCE****Division 1—Limits of Marine Insurance****Marine insurance defined**

7. Subject to sections 9A and 9B of the Insurance Contracts Act 1984, A contract of marine insurance is a contract whereby the insurer undertakes to indemnify the assured, in manner and to the extent thereby agreed, against marine losses, that is to say, the losses incident to marine adventure.

**Mixed land and sea risks Scope of marine insurance**

8(1) A contract of marine insurance may, by its express terms, or by usage of trade, be extended so as to protect the assured against losses ~~on inland waters or~~ on any land or air risk which may be incidental to any sea voyage.

(2) Unless the contract otherwise provides, ~~Where~~ a ship in course of building or repairs, ~~or~~ the launch of a ship, or any adventure analogous to a marine adventure, is covered by a policy ~~in the form of a marine policy,~~ the provisions of this Act, in so far as applicable, ~~shall apply thereto;~~ but, except as by this section provided, nothing in this Act shall alter or affect any rule of law applicable to any contract of insurance other than a contract of marine insurance as by this Act defined.

(3) Unless it expressly provides otherwise, a contract of marine insurance protects the assured against losses on all inland waters.

(4) Unless the contract expressly provides otherwise or the context requires otherwise, all references in this Act and in a contract of marine insurance to the “sea” and the “seas” include references to inland waters.

**Marine adventure and maritime perils defined**

9(1) Subject to the provisions of this Act, every lawful marine adventure may be the subject of a contract of marine insurance.

[No change]

- (2) In particular there is a marine adventure where:
- (a) any ship, goods, or other movables are exposed to maritime perils. Such property is in this Act referred to as “insurable property”;  
[No change]
- (b) the earning or acquisition of any freight, passage money, commission, profit, or other pecuniary benefit, or the security for any advances, loan, or disbursements, is endangered by the exposure of insurable property to maritime perils;  
[No change]
- (c) any liability to a third party may be incurred by the owner of, or other person interested in or responsible for, insurable property, by reason of maritime perils. “Maritime perils” means the perils consequent on, or incidental to, the navigation of the sea, that is to say, perils of the seas, fire, war perils, pirates, rovers, thieves, captures, seizures, restraints, and detentions of princes and peoples, jettisons, barratry, and any other perils, either of the like kind, or which may be designated by the policy.  
[No change]

#### Division 2—Insurable Interest

##### **Avoidance of wagering or gaming contracts Insurable interest not required**

10(1) Every contract of marine insurance by way of gaming or wagering is void.

##### **A contract of marine insurance is not void by reason only that the assured did not have, at the time when the contract was entered into, an interest in the subject matter of the contract.**

[Cf ICA s 16]

(2) — A contract of marine insurance is deemed to be a gaming or wagering contract:

[Repealed]

(a) — where the assured has not an insurable interest as defined by this Act, and the contract is entered into with no expectation of acquiring such an interest; or  
[Repealed]

(b) — where the policy is made “interest or no interest,” or “without further proof of interest than the policy itself,” or “without benefit of salvage to the insurer,” or subject to any other like term: Provided that, where there is no possibility of salvage, a policy may be effected without benefit of salvage to the insurer.  
[Repealed]

##### **Insurable interest defined Legal or equitable interest not required at time of loss**

11(1) Subject to the provisions of this Act, every person has an insurable interest who is interested in a marine adventure.

##### **Where the assured under a contract of marine insurance has suffered a pecuniary or economic loss by reason that property the subject matter of the contract has been damaged or destroyed, the insurer is not relieved of liability under the contract by reason only that, at the time of the loss, the assured did not have an interest at law or in equity in the property.**

[Cf ICA s 17]

(2) — In particular, a person is interested in a marine adventure where he stands in any legal or equitable relation to the adventure, or to any insurable property at risk therein, in consequence of which he may benefit by the safety or due arrival of insurable property, or



may be prejudiced by its loss, or by damage thereto, or by the detention thereof, or may incur liability in respect thereof.

[Repealed]

**~~When interest must attach~~**

~~12(1) The assured must be interested in the subject matter insured at the time of the loss, though he need not be interested when the insurance is effected. Provided that where the subject matter is insured “lost or not lost,” the assured may recover although he may not have acquired his interest until after the loss, unless at the time of effecting the contract of insurance the assured was aware of the loss, and the insurer was not.~~

[Repealed]

~~(2) — Where the assured has no interest at the time of the loss, he cannot acquire interest by any act or election after he is aware of the loss.~~

[Repealed]

**~~Defeasible or contingent interest~~**

~~13(1) A defeasible interest is insurable, as also is a contingent interest.~~

[Repealed]

~~(2) — In particular, where the buyer of goods has insured them, he has an insurable interest, notwithstanding that he might, at his election, have rejected the goods, or have treated them as at the seller’s risk, by reason of the latter’s delay in making delivery or otherwise.~~

[Repealed]

**~~Partial interest~~**

~~14. — A partial interest of any nature is insurable.~~

[Repealed]

**~~Re-insurance~~**

~~15(1) The insurer under a contract of marine insurance has an insurable interest in his risk, and may re-insure in respect of it.~~

[Repealed]

~~(2) — Unless the policy otherwise provides, the original assured has no right or interest in respect of such re-insurance.~~

**~~Bottomry~~**

~~16. — The lender of money on bottomry or respondentia has an insurable interest in respect of the loan.~~

[Repealed]<sup>1152</sup>

**~~Master’s and seamen’s wages~~**

~~17. — The master or any member of the crew of a ship has an insurable interest in respect of his wages.~~

[Repealed]

**~~Advance freight~~**

~~18. — In the case of advance freight, the person advancing the freight has an insurable interest, in so far as such freight is not repayable in case of loss.~~

[Repealed]

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1152 If the Commission’s recommendation to abolish the requirement for an insurable interest is not adopted, the Commission has recommended an alternative amendment to s 16 so that it reads as follows.

A lender of money on the security of a ship or ship’s cargo or other insurable property has an insurable interest in respect of the loan.

**Charges of insurance**

~~19.—The assured has an insurable interest in the charges of any insurance which he may effect.~~

[Repealed]<sup>1153</sup>

**Quantum of interest**

~~20(1) Where the subject matter insured is mortgaged, the mortgagor has an insurable interest in the full value thereof, and the mortgagee has an insurable interest in respect of any sum due or to become due under the mortgage.~~

[Repealed]

~~(2) A mortgagee, consignee, or other person having an interest in the subject matter insured may insure on behalf and for the benefit of other persons interested as well as for his own benefit.~~

[Repealed]

~~(3) The owner of insurable property has an insurable interest in respect of the full value thereof, notwithstanding that some third person may have agreed, or be liable, to indemnify him in case of loss.~~

[Repealed]

**Assignment of interest**

~~21.—Where the assured assigns or otherwise parts with his interest in the subject matter insured, he does not thereby transfer to the assignee his rights under the contract of insurance, unless there be an express or implied agreement with the assignee to that effect. But the provisions of this section do not affect a transmission of interest by operation of law.~~

[Repealed]

**Division 3—Insurable Value****Measure of insurable value**

22. Subject to any express provision or valuation in the policy, the insurable value of the subject-matter insured must be ascertained as follows:

[No change]

- (a) In insurance on a ship, the insurable value is the value, at the commencement of the risk, of the ship, including her outfit, provisions and stores for the officers and crew, money advanced for seamen's wages, and other disbursements (if any) incurred to make the ship fit for the voyage or adventure contemplated by the policy, plus the charges of insurance upon the whole: The insurable value, in the case of a steam-ship, includes also the machinery, boilers, and coals and engine stores if owned by the assured, and, in the case of a ship engaged in a special trade, the ordinary fittings requisite for that trade:

[No change]

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1153 If the Commission's recommendation to abolish the requirement for an insurable interest is not adopted, the Commission has recommended the insertion of a new s 19A to read as follows.

A purchaser of insurable property acquires an insurable interest in the property, any profit that may be derived from it and any liability that may be incurred in relation to it, if it has not already done so, when it pays for the property, or when it becomes bound to pay for the property provided that it subsequently pays for the property.

- (b) In insurance on freight, whether paid in advance or otherwise, the insurable value is the gross amount of the freight at the risk of the assured, plus the charges of insurance:  
[No change]
- (c) In insurance on goods or merchandise, the insurable value is the prime cost of the property insured, plus the expenses of and incidental to shipping and the charges of insurance upon the whole:  
[No change]
- (d) In insurance on any other subject-matter, the insurable value is the amount at the risk of the assured when the policy attaches, plus the charges of insurance.  
[No change]

#### Division 4—Disclosure and Representations

##### ~~Insurance is *uberrimae fidei*~~ **Duty of utmost good faith**

23 ~~A contract of marine insurance is a contract based upon the utmost good faith, and, if the utmost good faith be not observed by either party, the contract may be avoided by the other party.~~

**(1) A contract of marine insurance is a contract based on the utmost good faith and there is implied in such a contract a provision requiring each party to it to act towards the other party, in respect of any matter arising under or in relation to it, with the utmost good faith.**

**(2) If reliance by a party to a contract of marine insurance on a provision of the contract would be to fail to act with the utmost good faith, the party may not rely on the provision.**

**(3) Subsection (2) does not limit the operation of subsection (1).**

**(4) In deciding whether reliance by an insurer on a provision of a contract of marine insurance would be to fail to act with the utmost good faith, the court shall have regard to any notification of the provision that was given to the assured, whether a notification of a kind mentioned in this Act or otherwise.**

[Cf ICA s 13 and 14]

**(5) The requirement that each party act towards the other party with the utmost good faith extends for the duration of the relationship between the parties set out in the contract of marine insurance except in relation to any claim or other aspect of the relationship which becomes the subject of litigation between the parties, in which case the requirement ceases when the litigation is commenced but only in relation to the claim or other aspect that is the subject of that litigation.**

##### **Disclosure by assured**

24(1) Subject to the provisions of this section, the assured must disclose to the insurer, before the contract is concluded, every ~~material~~ circumstance which is known to the assured, **or which a reasonable person in the circumstances could be expected to know, to be material.** and the assured is deemed to know every circumstance which, in the ordinary course of business, ought to be known by him. If the assured fails to make such disclosure, the insurer may avoid the contract.

[Cf ICA s 21]

(2) Every circumstance is material which would influence the judgment of a prudent insurer in fixing the premium, or determining whether it will take the risk.

[No change]

(3) In the absence of inquiry the following circumstances need not be disclosed, namely:

(a) Any circumstance which diminishes the risk;

[No change]

(b) Any circumstance which is known or presumed to be known to the insurer. The insurer is presumed to know matters of common notoriety or knowledge, and matters which an insurer in the ordinary course of his business, as such, ought to know;

[No change]

(c) Any circumstance as to which information is waived by the insurer;

[No change]

(d) Any circumstance which it is superfluous to disclose by reason of any express ~~or implied warranty~~ **term of the contract.**

(4) Whether any particular circumstance, which is not disclosed, be material or not is, in each case, a question of fact.

[No change]

(5) The term "circumstance" includes any communication made to, or information received by, the assured.

[No change]

#### **Disclosure by agent effecting insurance**

25. Subject to the provisions of the preceding section as to circumstances which need not be disclosed, where an insurance is effected for the assured by an agent, the agent must disclose to the insurer:

[No change]

(a) every ~~material~~ circumstance which is known to ~~himself, and an agent to insure is deemed to know every circumstance which in the ordinary course of business ought to be known by, or to have been communicated to, him~~ **the agent, or which a reasonable person in the circumstances could be expected to know, to be material;** and

(b) every material circumstance which the assured is bound to disclose, unless it come to his knowledge too late to communicate it to the agent.

[No change]

#### **Representations pending negotiation of contract**

26(1) Every material representation made by the assured or his agent to the insurer during the negotiations for the contract, and before the contract is concluded, must be true. ~~If it be untrue the insurer may avoid the contract.~~

(2) A representation is material which would influence the judgment of a prudent insurer in fixing the premium, or determining whether it will take the risk.

[No change]

(3) A representation may be either as to a matter of fact, or as to a matter of expectation or belief.

[No change]

(4) A representation as to a matter of fact is true, if it be substantially correct, that is to say, if the difference between what is represented and what is actually correct would not be considered material by a prudent insurer.

[No change]

(5) A representation as to a matter of expectation or belief is true if it be made in good faith.

[No change]

(6) A representation may be withdrawn or corrected before the contract is concluded.

[No change]

(7) Whether a particular representation be material or not is, in each case, a question of fact.

[No change]

#### **No other duty of disclosure**

**26A(1) Without otherwise limiting or restricting section 23 of this Act, this Act does not, and a contract of marine insurance may not, impose on an assured a duty of disclosure before the contract is concluded greater than that provided for by this Act.**

[Cf ICA s 12]

**(2) A contract of marine insurance may include an express term providing for a duty of disclosure by the assured after the contract has been concluded.**

#### **Remedies for non-disclosure and misrepresentation**

**26B(1) Subject to any contrary term in the contract, if there is a breach by the assured or its agent of the obligations in sections 24, 25 or 26 the following subsections apply.**

**(2) If the breach is fraudulent the insurer is entitled to avoid the contract.**

**(3) If the breach is not fraudulent and the insurer proves that the non-disclosure or misrepresentation induced it to enter into the contract:**

**(a) if the insurer proves that it would not have entered into the contract if there had been no breach — the insurer is entitled to avoid the contract but must return the premium to the assured.**

**(b) if the insurer proves that it would have entered into the contract but on different terms — the insurer:**

**(i) is not entitled to avoid the contract; and**

**(ii) is not liable to indemnify the assured for any loss proximately caused by the undisclosed or misrepresented circumstance; and**

**(iii) is entitled to reduce any liability that it may have to the assured to reflect any variation in premium, deductible or excess that the insurer would have required if there had been no breach; and**

**(iv) is entitled to cancel the policy in accordance with section 47A.**

#### **No greater remedies**

**26C. A contract of marine insurance may not provide for any remedies for a breach by the assured or its agent of the obligations in sections 24, 25 or 26 more favourable to the insurer than those provided for by section 26B.**

**Following insurers**

**26D(1) This section applies if there is a breach by the assured or its agent of the obligations in sections 24, 25 or 26 and it is proved that an insurer (in this section called the “following insurer”) underwrote a proportion of a risk on a contract of marine insurance only because one or more other insurers (in this section called the “leading insurers”) had already underwritten a proportion of the risk.**

**(2) The following insurer is deemed to have been induced to enter into the contract by the breach only if all of the leading insurers were induced by the breach to enter into the contract.**

**When contract is deemed to be concluded**

27. A contract of marine insurance is deemed to be concluded when the proposal of the assured is accepted by the insurer, whether the policy be then issued or not; and for the purpose of showing when the proposal was accepted, reference may be made to the slip or covering note or other customary memorandum of the contract.

[No change]

**Division 5—The Policy****Contract must be embodied in policy**

28. ~~Subject to the provisions of any Act, a contract of marine insurance is inadmissible in evidence in an action for the recovery of a loss under the contract unless it is embodied in a marine policy in accordance with this Act.~~ **Subject to section 58, the insurer or its agent must issue a policy, or procure the issue of a policy, setting out expressly all the terms of the contract of marine insurance.** The policy may be executed and issued either at the time when the contract is concluded or afterwards.

**What policy must specify**

29**(1)** A marine policy must specify:

(a) the name of the assured, or of some person who effects the insurance on his behalf:

[No change]

(b) the subject-matter insured and the risk insured against:

[No change]

(c) the voyage, or period of time, or both, as the case may be, covered by the insurance:

[No change]

(d) the sum or sums insured:

[No change]

(e) the name or names of the insurers.

[No change]

**(2) No marine policy is invalid by reason only that it does not comply with subsection (1).**

**Signature of insurer**

30(1) A marine policy must be signed by or on behalf of the insurer, provided that in the case of a corporation the corporate seal may be sufficient, but nothing in this section shall be construed as requiring the subscription of a corporation to be under seal.

[No change]

(2) Where a policy is subscribed by or on behalf of two or more insurers, each subscription, unless the contrary be expressed, constitutes a distinct contract with the assured.

[No change]

#### **Voyage and time policies**

31(1) Where the contract is to insure the subject-matter “at and from,” or from one place to another place or to other places, the policy is called a “voyage policy”, and where the contract is to insure the subject-matter for a definite period of time the policy is called a “time policy.” A contract for both voyage and time may be included in the same policy.

[No change]

~~(2) — A time policy which is made for any time exceeding twelve months is invalid. Provided that a time policy may contain an agreement to the effect that, in the event of the ship being at sea or the voyage being otherwise not completed on the expiration of the policy, the subject matter of the insurance shall be held covered until the arrival of the ship at her destination, or for a reasonable time thereafter not exceeding thirty days; and the policy shall not be invalid on the ground only that by reason of such agreement it may become available for a period exceeding twelve months.~~

[Repealed].

#### **Designation of subject-matter**

32(1) The subject-matter insured must be designated in a marine policy with reasonable certainty.

[No change]

(2) The nature and extent of the interest of the assured in the subject-matter insured need not be specified in the policy.

[No change]

(3) Where the policy designates the subject-matter insured in general terms, it shall be construed to apply to the interest intended by the assured to be covered.

[No change]

(4) In the application of this section regard shall be had to any usage regulating the designation of the subject-matter insured.

[No change]

#### **Valued policy**

33(1) A policy may be either valued or unvalued.

[No change]

(2) A valued policy is a policy which specifies the agreed value of the subject-matter insured.

[No change]

(3) Subject to the provisions of this Act, and in the absence of fraud, the value fixed by the policy is, as between the insurer and assured, conclusive of the insurable value of the subject intended to be insured, whether the loss be total or partial.

[No change]

(4) Unless the policy otherwise provides, the value fixed by the policy is not conclusive for the purpose of determining whether there has been a constructive total loss.

[No change]

**Unvalued policy**

34. An unvalued policy is a policy which does not specify the value of the subject-matter insured, but, subject to the limit of the sum insured, leaves the insurable value to be subsequently ascertained, in the manner hereinbefore specified.

[No change]

**Floating, open and annual policies ~~policy by ship or ships~~**

35(1) A floating, **open or annual** policy is a policy which describes the insurance in general terms, and leaves the name of the ship or ships **or other insurable property** and other particulars to be defined by subsequent declaration.

(2) The subsequent declaration or declarations may be made by indorsement on the policy, or in other customary manner.

[No change]

(3) Unless the policy otherwise provides, the declarations must be made in the order of despatch or shipment **and** ~~they~~ must, in the case of goods, comprise all consignments within the terms of the policy, ~~and~~ ~~the~~ value of the goods or other property must be honestly stated, but an omission or erroneous declaration may be rectified even after loss or arrival, provided the omission or declaration was made in good faith.

(4) Unless the policy otherwise provides, where a declaration of value is not made until after notice of loss or arrival, the policy must be treated as an unvalued policy as regards the subject-matter of that declaration.

[No change]

**~~Construction of terms in policy~~**

~~36(1) A policy may be in the form in the Second Schedule.~~

~~[Repealed]~~

~~(2) Subject to the provisions of this Act, and unless the context of the policy otherwise requires, the terms and expressions mentioned in the Second Schedule shall be construed as having the scope and meaning in that Schedule assigned to them.~~

~~[Repealed]~~

**Premium to be arranged**

37(1) Where an insurance is effected at a premium to be arranged, and no arrangement is made, a reasonable premium is payable.

[No change]

(2) Where an insurance is effected on the terms that an additional premium is to be arranged in a given event, and that event happens but no arrangement is made, then a reasonable additional premium is payable.

[No change]

**Division 6—Double Insurance****Double insurance**

38(1) Where two or more policies are effected by or on behalf of the assured on the same adventure and interest or any part thereof, and the sums insured exceed the indemnity allowed by this Act, the assured is said to be over-insured by the double insurance.

[No change]

(2) Where the assured is over-insured by double insurance:

[No change]



- (a) the assured, unless the policy otherwise provides, may claim payment from the insurers in such order as he may think fit, provided that he is not entitled to receive any sum in excess of the indemnity allowed by this Act;  
[No change]
- (b) where the policy under which the assured claims is a valued policy, the assured must give credit, as against the valuation, for any sum received by him under any other policy, without regard to the actual value of the subject-matter insured;  
[No change]
- (c) where the policy under which the assured claims is an unvalued policy, he must give credit, as against the full insurable value, for any sum received by him under any other policy;  
[No change]
- (d) where the assured receives any sum in excess of the indemnity allowed by this Act, he is deemed to hold such sum in trust for the insurers, according to their right of contribution among themselves.  
[No change]

#### Division 7—Warranties Breach of contractual terms

##### Nature of warranty No warranties

39(1) ~~A warranty, in the following sections relating to warranties, means a promissory warranty, that is to say a warranty by which the assured undertakes that some particular thing shall or shall not be done, or that some conditions shall be fulfilled, or whereby he affirms or negatives the existence of a particular state of facts.~~

**Subject to this Act, no express or implied term in a contract of marine insurance is a warranty or otherwise has the effect that any breach of it by the assured entitles the insurer to be discharged from any liability under the contract.**

(2) ~~A warranty may be express or implied.~~

**Subject to this Act, an express term in a contract of marine insurance may provide that, if there is a breach by the assured of any express term in the contract, the insurer is discharged from all liability to indemnify the assured for any loss proximately caused by the breach.**

(3) ~~A warranty, as above defined, is a condition which must be exactly complied with, whether it be material to the risk or not. If it be not so complied with, then, subject to any express provision in the policy, the insurer is discharged from liability as from the date of the breach of warranty, but without prejudice to any liability incurred by him before that date.~~

**Without prejudice to any other burden of proof provided for by statute or common law, the insurer bears the burden of proving that there was a breach of a term of the contract and the assured bears the burden of proving that the loss for which it seeks to be indemnified was not proximately caused by or attributable to, as the case requires, the breach.**

##### When breach of warranty contractual term excused

40(1) Non-compliance with a ~~warranty~~ **term of a contract of marine insurance** is excused when, by reason of a change of circumstances, the ~~warranty~~ **term** ceases to be

applicable to the circumstances of the contract, or when compliance with the **warranty term** is rendered unlawful by any subsequent law.

~~(2) — Where a warranty is broken, the assured cannot avail himself of the defence that the breach has been remedied, and the warranty complied with, before loss.~~

[Repealed]

(3) A breach of warranty **by the assured of any term of a contract of marine insurance** may be waived by the insurer.

#### **Express warranties**

~~41(1) — An express warranty may be in any form of words from which the intention to warrant is to be inferred.~~

[Repealed]

~~(2) — An express warranty must be included in, or written upon, the policy, or must be contained in some document incorporated by reference into the policy.~~

[Repealed]

~~(3) — An express warranty does not exclude an implied warranty, unless it be inconsistent therewith.~~

[Repealed]

#### **Warranty of neutrality**

~~42(1) — Where insurable property, whether ship or goods, is expressly warranted neutral, there is an implied condition that the property shall have a neutral character at the commencement of the risk, and that, so far as the assured can control the matter, its neutral character shall be preserved during the risk.~~

[Repealed]

~~(2) — Where a ship is expressly warranted “neutral” there is also an implied condition that, so far as the assured can control the matter, she shall be properly documented, that is to say, that she shall carry the necessary papers to establish her neutrality, and that she shall not falsify or suppress her papers, or use simulated papers. If any loss occurs through breach of this condition, the insurer may avoid the contract.~~

[Repealed]

#### **No implied warranty of nationality**

~~43. — There is no implied warranty as to the nationality of a ship, or that her nationality shall not be changed during the risk.~~

[Repealed]

#### **Warranty of good safety**

~~44. — Where the subject matter insured is warranted “well” or “in good safety” on a particular day, it is sufficient if it be safe at any time during that day.~~

[Repealed]

#### **Warranty of Terms relating to seaworthiness of ship**

~~45(1) In a voyage policy there is an implied warranty that at the commencement of the voyage the ship shall be seaworthy for the purpose of the particular adventure insured.~~

**There is no warranty in any contract of marine insurance that any ship is seaworthy at any time during the insured adventure.**

~~(2) — Where the policy attaches while the ship is in port, there is also an implied warranty that she shall, at the commencement of the risk, be reasonably fit to encounter the ordinary perils of the port.~~

**A contract of marine insurance may contain an express term that a ship is seaworthy at any time or during any period within the period of cover of the contract and that the insurer is discharged from all liability to indemnify the assured for any loss attributable to any breach of this term if the assured:**

**(a) knew, or ought to have known, of the facts and circumstances that rendered the ship unseaworthy and that they rendered the ship unseaworthy; and**

**(b) failed to take such steps as were reasonably available to it to make the ship seaworthy.**

(3) ~~Where the policy relates to a voyage which is performed in different stages, during which the ship requires different kinds of or further preparation or equipment, there is an implied warranty that at the commencement of each stage the ship is seaworthy in respect of such preparation or equipment for the purposes of that stage.~~

**A contract of marine insurance may not contain a term that relates to the seaworthiness of a ship that is more favourable to the insurer than that provided for by this section.**

(4) A ship is deemed to be seaworthy when she is reasonably fit in all respects to encounter the ordinary perils of the seas of the adventure insured.

[No change]

(5) ~~— In a time policy there is no implied warranty that the ship shall be seaworthy at any stage of the adventure, but where, with the privity of the assured, the ship is sent to sea in an unseaworthy state, the insurer is not liable for any loss attributable to unseaworthiness.~~

[Repealed]

**No implied warranty that goods are seaworthy**

46(1) ~~In a policy on goods or other movables~~ **of marine insurance** there is no implied warranty that ~~the~~ **any** goods or movables are seaworthy.-

(2) ~~— In a voyage policy on goods or other movables there is an implied warranty that at the commencement of the voyage the ship is not only seaworthy as a ship, but also that she is reasonably fit to carry the goods or other movables to the destination contemplated by the policy.~~

[Repealed]

**Warranty of Terms relating to legality**

47. ~~There is an implied warranty that the adventure insured is a lawful one, and that, so far as the assured can control the matter, the adventure shall be carried out in a lawful manner.~~

**(1) There is no warranty in any contract of marine insurance that the adventure is lawful or that it shall be carried out in a lawful manner.**

**(2) A contract of marine insurance may include an express term to the effect that, so far as the assured can control the matter, the insured adventure shall have no unlawful purpose and that, if there is a breach of any such term, the insurer is discharged from all liability under the policy and is not required to return any part of the premium to the assured.**

**(3) A contract of marine insurance may include an express term to the effect that, so far as the assured can control the matter, the insured adventure shall be carried out in a lawful manner and that, if there is a breach of any such term, the insurer is**

**discharged from all liability to indemnify the assured for any loss attributable to that breach.**

**(4) A contract of marine insurance may not contain a term requiring the insured adventure to be lawful or that it be carried out in a lawful manner that is more favourable to the insurer than those provided for by this section.**

**Cancellation of contracts of marine insurance**

**47A(1) Subject to any express term in a contract of marine insurance, where:**

**(a) the assured has failed to comply with a provision of the contract; or**

**(b) the assured did not comply with the duty of utmost good faith; or**

**(c) the assured has made a fraudulent claim under the contract; or**

**(d) this Act otherwise permits;**

**the insurer may cancel the contract in accordance with this section.**

**(2) An insurer who wishes to exercise a right to cancel a contract of marine insurance, whether under this section or pursuant to an express term of the contract, shall give notice in writing of the proposed cancellation to the assured.**

**(3) Any notice of an insurer's intention to cancel a contract of marine insurance has effect to cancel the contract at any time specified in the notice after the earlier of the following times:**

**(a) the time when another contract of marine insurance between the assured and the insurer or some other insurer, being a contract that is intended by the assured to replace the first-mentioned contract, is entered into;**

**(b) 4 pm on the third business day after the day on which the notice was given to the insured.**

[Cf ICA s 59 and 60]

## Division 8—The Voyage

**Implied condition as to commencement of risk**

~~48(1) Where the subject matter is insured by a voyage policy "at and from" or "from" a particular place, it is not necessary that the ship should be at that place when the contract is concluded, but there is an implied condition that the adventure shall be commenced within a reasonable time, and that if the adventure be not so commenced the insurer may avoid the contract.~~

[Repealed]

~~(2) The implied condition may be negated by showing that the delay was caused by circumstances known to the insurer before the contract was concluded, or by showing that he waived the condition.~~

[Repealed]

**Alteration of port of departure**

49. Where the place of departure is specified by the policy, and the ship instead of sailing from that place sails from any other place, the risk does not attach.

[No change]

**Sailing for different destination**

50. Where the destination is specified in the policy, and the ship, instead of sailing for that destination, sails for any other destination, the risk does not attach.

[No change]

**Change of voyage**

~~51(1) Where, after the commencement of the risk, the destination of the ship is voluntarily changed from the destination contemplated by the policy, there is said to be a change of voyage.~~

[Repealed]

~~(2) Unless the policy otherwise provides, where there is a change of voyage, the insurer is discharged from liability as from the time of change, that is to say, as from the time when the determination to change it is manifested; and it is immaterial that the ship may not in fact have left the course of voyage contemplated by the policy when the loss occurs.~~

[Repealed]

**Deviation**

~~52(1) Where a ship, without lawful excuse, deviates from the voyage contemplated by the policy, the insurer is discharged from liability as from the time of deviation, and it is immaterial that the ship may have regained her route before any loss occurs.~~

[Repealed]

~~(2) There is a deviation from the voyage contemplated by the policy:~~

[Repealed]

~~(a) where the course of the voyage is specifically designated by the policy, and that course is departed from; or~~

[Repealed]

~~(b) where the course of the voyage is not specifically designated by the policy, but the usual and customary course is departed from.~~

[Repealed]

~~(3) The intention to deviate is immaterial; there must be a deviation in fact to discharge the insurer from his liability under the contract.~~

[Repealed]

**Several ports of discharge**

~~53(1) Where several ports of discharge are specified by the policy, the ship may proceed to all or any of them, but, in the absence of any usage or sufficient cause to the contrary, she must proceed to them, or such of them as she goes to, in the order designated by the policy. If she does not there is a deviation.~~

[Repealed]

~~(2) Where the policy is to "ports of discharge," within a given area, which are not named, the ship must, in the absence of any usage or sufficient cause to the contrary, proceed to them, or such of them as she goes to, in their geographical order. If she does not there is a deviation.~~

[Repealed]

**Delay in voyage**

~~54. In the case of a voyage policy, the adventure insured must be prosecuted throughout its course with reasonable despatch, and, if without lawful excuse it is not so prosecuted, the insurer is discharged from liability as from the time when the delay became~~

~~unreasonable.~~

[Repealed]

**Excuses for deviation or delay**

~~55(1) Deviation or delay in prosecuting the voyage contemplated by the policy is excused:~~

[Repealed]

~~(a) where authorized by any special term in the policy; or~~

[Repealed]

~~(b) where caused by circumstances beyond the control of the master and his employer; or~~

[Repealed]

~~(c) where reasonably necessary in order to comply with an express or implied warranty; or~~

[Repealed]

~~(d) where reasonably necessary for the safety of the ship or subject matter insured; or~~

[Repealed]

~~(e) for the purpose of saving human life, or aiding a ship in distress where human life may be in danger; or~~

[Repealed]

~~(f) where reasonably necessary for the purpose of obtaining medical or surgical aid for any person on board the ship; or~~

[Repealed]

~~(g) where caused by the barratrous conduct of the master or crew, if barratry be one of the perils insured against.~~

[Repealed]

~~(2) When the cause excusing the deviation or delay ceases to operate, the ship must resume her course, and prosecute her voyage, with reasonable despatch.~~

[Repealed]

**PART III—ASSIGNMENT OF POLICY OR CONTRACT**

**When and how policy or contract is assignable**

56(1) A marine policy **or contract of marine insurance** is assignable unless it contains terms expressly prohibiting assignment. It may be assigned either before or after loss.

(2) Where a marine policy **or contract of marine insurance** has been assigned so as to pass the beneficial interest in the policy **or contract**, the assignee of the policy **or contract** is entitled to sue thereon in **his its** own name; and the defendant is entitled to make any defence arising out of the **policy or** contract which ~~he~~ **it** would have been entitled to make if the action had been brought in the name of the person by or on behalf of whom the policy **or contract** was effected.

(3) A marine policy **or contract of marine insurance** may be assigned by indorsement thereon or in other customary manner.

**Assured who has no interest cannot assign**

~~57.—Where the assured has parted with or lost his interest in the subject matter insured, and has not, before or at the time of so doing, expressly or impliedly agreed to assign the policy, any subsequent assignment of the policy is inoperative: Provided that nothing in this section affects the assignment of a policy after loss.~~

[Repealed]

**PART IV—THE PREMIUM****When premium payable**

58. Unless otherwise agreed, the duty of the assured or his agent to pay the premium, and the duty of the insurer to issue the policy to the assured or his agent, are concurrent conditions, and the insurer is not bound to issue the policy until payment or tender of the premium.

[No change]

**Policy effected through broker**

~~59(1) Unless otherwise agreed, where a marine policy is effected on behalf of the assured by a broker, the broker is directly responsible to the insurer for the premium, and the insurer is directly responsible to the assured for the amount which may be payable in respect of losses, or in respect of returnable premium.~~

[To be repealed upon amendment of the *Insurance (Agents and Brokers) Act* or the enactment of the Financial Services Reform Bill]

~~(2) Unless otherwise agreed, the broker has, as against the assured, a lien upon the policy for the amount of the premium and his charges in respect of effecting the policy; and, where he has dealt with the person who employs him as a principal, he has also a lien on the policy in respect of any balance on any insurance account which may be due to him from such person, unless when the debt was incurred he had reason to believe that such person was only an agent.~~

[To be repealed upon amendment of the *Insurance (Agents and Brokers) Act* or the enactment of the Financial Services Reform Bill]

**Effect of receipt on policy**

60.—Where a marine policy effected on behalf of the assured by a broker acknowledges the receipt of the premium, such acknowledgment is, in the absence of fraud, conclusive as between the insurer and the assured, but not as between the insurer and broker.

[To be repealed upon amendment of the *Insurance (Agents and Brokers) Act* or the enactment of the Financial Services Reform Bill]

**PART V—LOSS AND ABANDONMENT****Division 1—General****Included and excluded losses**

61(1) Subject to the provisions of this Act, and unless the policy otherwise provides, the insurer is liable for any loss proximately caused by a peril insured against, but, subject as aforesaid, he is not liable for any loss which is not proximately caused by a peril insured

against.

[No change]

(2) In particular:

(a) the insurer is not liable for any loss attributable to the wilful misconduct of the assured, but, unless the policy otherwise provides, he is liable for any loss proximately caused by a peril insured against, even though the loss would not have happened but for the misconduct or negligence of the master or crew;

[No change]

(b) unless the policy otherwise provides, the insurer on ship or goods is not liable for any loss proximately caused by delay, although the delay be caused by a peril insured against;

[No change]

(c) unless the policy otherwise provides, the insurer is not liable for ordinary wear and tear, ordinary leakage and breakage, inherent vice or nature of the subject-matter insured, or for any loss proximately caused by rats or vermin, or for any injury to machinery not proximately caused by maritime perils.

[No change]

#### **Partial and total loss**

62(1) A loss may be either total or partial. Any loss other than a total loss, as hereinafter defined, is a partial loss.

[No change]

(2) A total loss may be either an actual total loss, or a constructive total loss.

[No change]

(3) Unless a different intention appears from the terms of the policy, an insurance against total loss includes a constructive, as well as an actual, total loss.

[No change]

(4) Where the assured brings an action for a total loss and the evidence proves only a partial loss, he may, unless the policy otherwise provides, recover for a partial loss.

[No change]

(5) Where goods reach their destination in specie, but, by reason of obliteration of marks, or otherwise, they are incapable of identification, the loss, if any, is partial, and not total.

[No change]

#### **Actual total loss**

63(1) Where the subject-matter insured is destroyed, or so damaged as to cease to be a thing of the kind insured, or where the assured is irretrievably deprived thereof, there is an actual total loss.

[No change]

(2) In the case of an actual total loss no notice of abandonment need be given.

[No change]

#### **Missing ship**

64. Where the ship concerned in the adventure is missing, and after the lapse of a reasonable time no news of her has been received, an actual total loss may be presumed.

[No change]



**Effect of transhipment etc.**

65. Where, by a peril insured against, the voyage is interrupted at an intermediate port or place, under such circumstances as, apart from any special stipulation in the contract of affreightment, to justify the master in landing and re-shipping the goods or other movables, or in transhipping them, and sending them on to their destination, the liability of the insurer continues, notwithstanding the landing or transhipment.

[No change]

**Constructive total loss defined**

66(1) Subject to any express provision in the policy, there is a constructive total loss where the subject-matter insured is reasonably abandoned on account of its actual total loss appearing to be unavoidable, or because it could not be preserved from actual total loss without an expenditure which would exceed its value when the expenditure had been incurred.

[No change]

(2) In particular, there is a constructive total loss:

(a) where the assured is deprived of the possession of his ship or goods by a peril insured against, and

[No change]

(i) it is unlikely that he can recover the ship or goods, as the case may be; or

[No change]

(ii) the cost of recovering the ship or goods, as the case may be, would exceed their value when recovered; or

[No change]

(b) in the case of damage to a ship, where she is so damaged by a peril insured against that the cost of repairing the damage would exceed the value of the ship when repaired. In estimating the cost of repairs, no deduction is to be made in respect of general average contributions to those repairs payable by other interests, but account is to be taken of the expense of future salvage operations and of any future general average contribution to which the ship would be liable if repaired; or

[No change]

(c) in the case of damage to goods, where the cost of repairing the damage and forwarding the goods to their destination would exceed their value on arrival.

[No change]

**Effect of constructive total loss**

67. Where there is a constructive total loss, the assured may either treat the loss as a partial loss, or abandon the subject-matter insured to the insurer and treat the loss as if it were an actual total loss.

[No change]

**Notice of abandonment**

68(1) Subject to the provisions of this section, where the assured elects to abandon the subject-matter insured to the insurer, he must give notice of abandonment. If he fails to do so the loss can only be treated as a partial loss.

[No change]

(2) Notice of abandonment may be given in writing, or by word of mouth, or partly in writing and partly by word of mouth, and may be given in any terms which indicate the

intention of the assured to abandon his insured interest in the subject-matter insured unconditionally to the insurer.

[No change]

(3) Notice of abandonment must be given with reasonable diligence after the receipt of reliable information of the loss, but where the information is of a doubtful character the assured is entitled to a reasonable time to make inquiry.

[No change]

(4) Where notice of abandonment is properly given, the rights of the assured are not prejudiced by the fact that the insurer refuses to accept the abandonment.

[No change]

(5) The acceptance of an abandonment may be either express or implied from the conduct of the insurer. The mere silence of the insurer after notice is not an acceptance.

[No change]

(6) Where notice of abandonment is accepted the abandonment is irrevocable. The acceptance of the notice conclusively admits liability for the loss and the sufficiency of the notice.

[No change]

(7) Notice of abandonment is unnecessary where, at the time when the assured receives information of the loss, there would be no possibility of benefit to the insurer if notice were given to him.

[No change]

(8) Notice of abandonment may be waived by the insurer.

[No change]

(9) Where an insurer has re-insured his risk, no notice of abandonment need be given by him.

[No change]

#### **Effect of abandonment**

69(1) Where there is a valid abandonment the insurer is entitled to take over the interest of the assured in whatever may remain of the subject-matter insured, and all proprietary rights incidental thereto.

[No change]

(2) Upon the abandonment of a ship, the insurer thereof is entitled to any freight in course of being earned, and which is earned by her subsequent to the casualty causing the loss, less the expenses of earning it incurred after the casualty; and, where the ship is carrying the owner's goods, the insurer is entitled to a reasonable remuneration for the carriage of them subsequent to the casualty causing the loss.

[No change]

### **Division 2—Partial Losses (including Salvage, General Average, and Particular Charges)**

#### **Particular average loss**

70(1) A particular average loss is a partial loss of the subject-matter insured, caused by a peril insured against, and which is not a general average loss.

[No change]

(2) Expenses incurred by or on behalf of the assured for the safety or preservation of the subject-matter insured, other than general average and salvage charges, are called particular charges. Particular charges are not included in particular average.

[No change]

**Salvage charges**

71(1) Subject to any express provision in the policy, salvage charges incurred in preventing a loss by perils insured against may be recovered as a loss by those perils.

[No change]

(2) "Salvage charges" means the charges recoverable under maritime law by a salvor independently of contract. They do not include the expenses of services in the nature of salvage rendered by the assured or his agents, or any person employed for hire by them, for the purpose of averting a peril insured against. Such expenses, where properly incurred, may be recovered as particular charges or as a general average loss, according to the circumstances under which they were incurred.

[No change]

**General average loss**

72(1) A general average loss is a loss caused by or directly consequential on a general average act. It includes a general average expenditure as well as a general average sacrifice.

[No change]

(2) There is a general average act where any extraordinary sacrifice or expenditure is voluntarily and reasonably made or incurred in time of peril for the purpose of preserving the property imperilled in the common adventure.

[No change]

(3) Where there is a general average loss, the party on whom it falls is entitled, subject to the conditions imposed by maritime law, to a rateable contribution from the other parties interested, and such contribution is called a general average contribution.

[No change]

(4) Subject to any express provision in the policy, where the assured has incurred a general average expenditure, he may recover from the insurer in respect of the proportion of the loss which falls upon him; and, in the case of a general average sacrifice, he may recover from the insurer in respect of the whole loss without having enforced his right of contribution from the other parties liable to contribute.

[No change]

(5) Subject to any express provision in the policy, where the assured has paid, or is liable to pay, a general average contribution in respect of the subject insured he may recover therefor from the insurer.

[No change]

(6) In the absence of express stipulation, the insurer is not liable for any general average loss or contribution where the loss was not incurred for the purpose of avoiding, or in connexion with the avoidance of, a peril insured against.

[No change]

(7) Where ship, freight, and cargo, or any two of those interests, are owned by the same assured, the liability of the insurer in respect of general average losses or contributions is to be determined as if those subjects were owned by different persons.

[No change]

**PART VI—MEASURE OF INDEMNITY****Division 1—Liability of Insurer for Loss****Extent of liability of insurer for loss**

73(1) The sum which the assured can recover in respect of a loss on a policy by which he is insured, in the case of an unvalued policy to the full extent of the insurable value, or, in the case of a valued policy to the full extent of the value fixed by the policy, is called the measure of indemnity.

[No change]

(2) Where there is a loss recoverable under the policy, the insurer, or each insurer if there be more than one, is liable for such proportion of the measure of indemnity as the amount of his subscription bears to the value fixed by the policy in the case of a valued policy, or to the insurable value in the case of an unvalued policy.

[No change]

**Total loss**

74. Subject to the provisions of this Act and to any express provision in the policy, where there is a total loss of the subject-matter insured:

[No change]

(a) if the policy be a valued policy, the measure of indemnity is the sum fixed by the policy;

[No change]

(b) if the policy be an unvalued policy, the measure of indemnity is the insurable value of the subject-matter insured.

[No change]

**Partial loss of ship**

75. Where a ship is damaged, but is not totally lost, the measure of indemnity, subject to any express provision in the policy, is as follows:

[No change]

(a) Where the ship has been repaired, the assured is entitled to the reasonable cost of the repairs, less the customary deductions, but not exceeding the sum insured in respect of any one casualty:

[No change]

(b) Where the ship has been only partially repaired, the assured is entitled to the reasonable cost of such repairs, computed as above, and also to be indemnified for the reasonable depreciation, if any, arising from the unrepaired damage, provided that the aggregate amount shall not exceed the cost of repairing the whole damage, computed as above:

[No change]

(c) Where the ship has not been repaired, and has not been sold in her damaged state during the risk, the assured is entitled to be indemnified for the reasonable depreciation arising from the unrepaired damage, but not exceeding the reasonable cost of repairing such damage, computed as above.

[No change]

**Partial loss of freight**

76. Subject to any express provision in the policy, where there is a partial loss of freight, the measure of indemnity is such proportion of the sum fixed by the policy in the case of a valued policy, or of the insurable value in the case of an unvalued policy, as the proportion of freight lost by the assured bears to the whole freight at the risk of the assured under the policy.

[No change]

**Partial loss of goods, merchandise etc.**

77. Where there is a partial loss of goods, merchandise, or other movables, the measure of indemnity, subject to any express provision in the policy, is as follows:

[No change]

(a) Where part of the goods, merchandise, or other movables insured by a valued policy is totally lost, the measure of indemnity is such proportion of the sum fixed by the policy as the insurable value of the part lost bears to the insurable value of the whole, ascertained as in the case of an unvalued policy:

[No change]

(b) Where part of the goods, merchandise, or other movables insured by an unvalued policy is totally lost, the measure of indemnity is the insurable value of the part lost, ascertained as in case of total loss:

[No change]

(c) Where the whole or any part of the goods or merchandise insured has been delivered damaged at its destination, the measure of indemnity is such proportion of the sum fixed by the policy in the case of a valued policy, or of the insurable value in the case of an unvalued policy, as the difference between the gross sound and damaged values at the place of arrival bears to the gross sound value:

[No change]

(d) "Gross value" means the wholesale price or, if there be no such price, the estimated value, with, in either case, freight, landing charges, and duty paid beforehand; provided that, in the case of goods or merchandise customarily sold in bond, the bonded price is deemed to be the gross value. "Gross proceeds" means the actual price obtained at a sale where all charges on sale are paid by the sellers.

[No change]

**Apportionment of valuation**

78(1) Where different species of property are insured under a single valuation, the valuation must be apportioned over the different species in proportion to their respective insurable values, as in the case of an unvalued policy. The insured value of any part of a species is such proportion of the total insured value of the species as the insurable value of the part bears to the insurable value of the whole, ascertained in both cases as provided by this Act.

[No change]

(2) Where a valuation has to be apportioned, and particulars of the prime cost of each separate species, quality, or description of goods cannot be ascertained, the division of the valuation may be made over the net arrived sound values of the different species, qualities, or descriptions of goods.

[No change]

**General average contributions and salvage charges**

79(1) Subject to any express provision in the policy, where the assured has paid, or is liable for, any general average contribution, the measure of indemnity is the full amount of such contribution, if the subject-matter liable to contribution is insured for its full contributory value; but, if such subject-matter be not insured for its full contributory value, or if only part of it be insured, the indemnity payable by the insurer must be reduced in proportion to the under insurance, and where there has been a particular average loss which constitutes a deduction from the contributory value, and for which the insurer is liable, that amount must be deducted from the insured value in order to ascertain what the insurer is liable to contribute.

[No change]

(2) Where the insurer is liable for salvage charges the extent of his liability must be determined on the like principle.

[No change]

**Liabilities to third parties**

80. Where the assured has effected an insurance in express terms against any liability to a third party, the measure of indemnity, subject to any express provision in the policy, is the amount paid or payable by him to such third party in respect of such liability.

[No change]

**General provisions as to measure of indemnity**

81(1) Where there has been a loss in respect of any subject-matter not expressly provided for in the foregoing provisions of this Act, the measure of indemnity shall be ascertained, as nearly as may be, in accordance with those provisions, in so far as applicable to the particular case.

[No change]

(2) Nothing in the provisions of this Act relating to the measure of indemnity shall affect the rules relating to double insurance, or prohibit the insurer from disproving interest wholly or in part, or from showing that at the time of the loss the whole or any part of the subject-matter insured was not at risk under the policy.

[No change]

**Contractual terms relating to ~~P~~particular average warranties**

82(1) Where a contract of marine insurance contains an express term that the subject-matter insured is ~~warranted~~ free from particular average, the assured cannot recover for a loss of part, other than a loss incurred by a general average sacrifice, unless the contract contained in the policy be apportionable; but, if the contract be apportionable, the assured may recover for a total loss of any apportionable part.

(2) Where a contract of marine insurance contains an express term that the subject-matter insured is ~~warranted~~ free from particular average, either wholly or under a certain percentage, the insurer is nevertheless liable for salvage charges, and for particular charges and other expenses properly incurred pursuant to the provisions of the suing and labouring clause in order to avert a loss insured against.

(3) Unless the policy otherwise provides, where a contract of marine insurance contains an express term that the subject-matter insured is ~~warranted~~ free from particular average under a specified percentage, a general average loss cannot be added to a particular average loss to make up the specified percentage.

(4) For the purpose of ascertaining whether the specified percentage has been reached, regard shall be had only to the actual loss suffered by the subject-matter insured. Particular charges and the expenses of and incidental to ascertaining and proving the loss must be excluded.

[No change]

**Successive losses**

83(1) Unless the policy otherwise provides, and subject to the provisions of this Act, the insurer is liable for successive losses, even though the total amount of such losses may exceed the sum insured.

[No change]

(2) Where, under the same policy, a partial loss, which has not been repaired or otherwise made good, is followed by a total loss, the assured can only recover in respect of the total loss: Provided that nothing in this section shall affect the liability of the insurer under the suing and labouring clause.

[No change]

**Suing and labouring clause**

84(1) Where the policy contains a suing and labouring clause, the engagement thereby entered into is deemed to be supplementary to the contract of insurance, and the assured may recover from the insurer any expenses properly incurred pursuant to the clause, notwithstanding that the insurer may have paid for a total loss, or that **the contract of marine insurance may contain an express term that** the subject-matter ~~may have been warranted~~ **is** free from particular average, either wholly or under a certain percentage.

(2) General average losses and contributions and salvage charges, as defined by this Act, are not recoverable under the suing and labouring clause.

[No change]

(3) Expenses incurred for the purpose of averting or diminishing any loss not covered by the policy are not recoverable under the suing and labouring clause.

[No change]

(4) It is the duty of the assured and his agents, in all cases, to take such measures as may be reasonable for the purpose of averting or minimizing a loss.

[No change]

**Division 2—Rights of Insurer on Payment of Loss**

**Right of subrogation**

85(1) Where the insurer pays for a total loss, either of the whole, or in the case of goods of any apportionable part, of the subject-matter insured, he thereupon becomes entitled to take over the interest of the assured in whatever may remain of the subject-matter so paid for, and he is thereby subrogated to all the rights and remedies of the assured in and in respect of that subject-matter as from the time of the casualty causing the loss.

[No change]

(2) Subject to the foregoing provisions, where the insurer pays for a partial loss, he acquires no title to the subject-matter insured, or such part of it as may remain, but he is thereupon subrogated to all rights and remedies of the assured in and in respect of the subject-matter insured as from the time of the casualty causing the loss, in so far as the assured has been indemnified, according to this Act, by such payment for the loss.

[No change]

**Contracts affecting rights of subrogation**

**85A(1) Where a contract of marine insurance includes a provision that has the effect of excluding or limiting the insurer's liability in respect of a loss by reason that the assured is a party to an agreement that excludes or limits a right of the assured to recover damages from a person other than the insurer in respect of the loss, the insurer may not rely on the provision unless the insurer clearly informed the assured in writing, before the contract of marine insurance was entered into, of the effect of the provision**

**(2) The duty of disclosure does not require the assured to disclose the existence of a contract that so limits the assured's rights.**

[Cf ICA s 68]

**Right of contribution**

86(1) Where the assured is over-insured by double insurance, each insurer is bound, as between himself and the other insurers, to contribute rateably to the loss in proportion to the amount for which he is liable under his contract.

[No change]

(2) If any insurer pays more than his proportion of the loss, he is entitled to maintain an action for contribution against the other insurers, and is entitled to the like remedies as a surety who has paid more than his proportion of the debt.

[No change]

**Effect of under insurance**

87. Where the assured is insured for an amount less than the insurable value, or, in the case of a valued policy, for an amount less than the policy valuation, he is deemed to be his own insurer in respect of the uninsured balance.

[No change]

**Rights with respect to moneys recovered from third parties**

**87A(1) Where money is recovered from a third party in respect of a loss that is wholly or partly the subject of a contract of marine insurance, that money shall, subject to any contrary agreement between the insurer and the assured, be distributed in the following manner and order.**

**(2) The party or parties funding the recovery action shall be reimbursed for its or their administrative and legal costs incurred in connection with that action. If there is insufficient money recovered for full reimbursement, the parties shall be reimbursed pro rata.**

**(3) If:**

**(a) The insurer has funded the action under its rights of subrogation, it is entitled to retain an amount equal to the amount that it has paid to the assured under the contract of marine insurance. The assured is then entitled to be paid an amount that, together with any amount that it has received from the insurer under the contract of marine insurance, will indemnify it in full for its loss.**

**(b) The assured has funded the action, it is entitled to retain an amount that, together with any amount that it has received from the insurer under the contract of marine insurance, will indemnify it in full for its loss. The insurer is then entitled to be paid an amount equal to the amount that it has paid to the assured under the contract of marine insurance.**



**(c) The insurer and the assured have funded the action jointly, they are entitled to the amounts referred to in paragraphs (a) and (b). If there is insufficient money recovered for full reimbursement, the parties shall be reimbursed pro rata.**

**(4) Any further amount recovered from the third party is to be paid to the parties to the contract of marine insurance pro rata in accordance with the ratio in which they contributed to the administrative and legal costs of the recovery action.**

**(5) Notwithstanding anything else in this section, any separate or identifiable components in respect of interest are to be paid to the insurer and the assured in such proportions as fairly reflect the amounts that each has recovered from the third party and the periods of time for which each lost the use of its money.**

[Cf ICA s 67]

## PART VII—RETURN OF PREMIUM

### Enforcement of return

88. Where the premium, or a proportionate part thereof, is, by this Act, declared to be returnable:

[No change]

(a) if already paid, it may be recovered by the assured from the insurer; and

[No change]

(b) if unpaid, it may be retained by the assured or his agent.

[No change]

### Return by agreement

89. Where the policy contains a stipulation for the return of the premium, or a proportionate part thereof, on the happening of a certain event, and that event happens, the premium, or, as the case may be, the proportionate part thereof, is thereupon returnable to the assured.

[No change]

### Return for failure of consideration

90(1) Where the consideration for the payment of the premium totally fails, and there has been no fraud or illegality on the part of the assured or his agents, the premium is thereupon returnable to the assured.

[No change]

(2) Where the consideration for the payment of the premium is apportionable, and there is a total failure of any apportionable part of the consideration, a proportionate part of the premium is, under the like conditions, thereupon returnable to the assured.

[No change]

(3) In particular:

(a) where the policy is void, or is avoided by the insurer as from the commencement of the risk, the premium is returnable, provided that there has been no fraud or illegality on the part of the assured; but if the risk is not apportionable, and has once attached, the premium is not returnable;

[No change]

(b) where the subject-matter insured, or part thereof, has never been imperilled, the premium, or, as the case may be, a proportionate part thereof, is returnable: Provided that where the subject-matter has been insured “lost or not lost” and has arrived in safety at the time when the contract is concluded, the premium is not returnable unless, at such time, the insurer knew of the safe arrival;

[No change]

~~(c) where the assured has no insurable interest throughout the currency of the risk, the premium is returnable, provided that this rule does not apply to a policy effected by way of gaming or wagering;~~

[Repealed]

~~(d) where the assured has a defeasible interest which is terminated during the currency of the risk, the premium is not returnable;~~

[Repealed]

(e) where the assured has over-insured under an unvalued policy, a proportionate part of the premium is returnable;

[No change]

(f) subject to the foregoing provisions, where the assured has over-insured by double insurance, a proportionate part of the several premiums is returnable: Provided that, if the policies are effected at different times, and any earlier policy has at any time borne the entire risk, or if a claim has been paid on the policy in respect of the full sum insured thereby, no premium is returnable in respect of that policy, and when the double insurance is effected knowingly by the assured no premium is returnable.

[No change]

## PART VIII—MUTUAL INSURANCE

### **Modification of Act in case of mutual insurance**

91(1) Where two or more persons mutually agree to insure each other, **or agree to form an association to insure each other,** against marine losses there is said to be mutual insurance.

(2) The provisions of this Act relating to the premium do not apply to mutual insurance, but a guarantee, or such other arrangement as may be agreed upon, may be substituted for the premium.

[No change]

(3) The provisions of this Act, in so far as they may be modified by the agreement of the parties, may in the case of mutual insurance be modified by the terms of the policies issued by the association, or by the rules and regulations of the association.

[No change]

(4) Subject to the exceptions mentioned in this section, the provisions of this Act apply to a mutual insurance.

[No change]

## PART IX—SUPPLEMENTAL

**Ratification by assured**

92. Where a contract of marine insurance is in good faith effected by one person on behalf of another, the person on whose behalf it is effected may ratify the contract even after he is aware of a loss.

[No change]

**Implied obligations varied by agreement or usage**

93(1) Where any right, duty, or liability would arise under a contract of marine insurance by implication of law, it may be negatived or varied by express agreement, or by usage, if the usage be such as to bind both parties to the contract.

[No change]

(2) The provisions of this section extend to any right, duty, or liability declared by this Act which may be lawfully modified by agreement.

[No change]

**Reasonable time etc. a question of fact**

94. Where by this Act any reference is made to reasonable time, reasonable premium, or reasonable diligence, the question what is reasonable is a question of fact.

[No change]

**Reference to slip or cover note**

95. Where a policy in accordance with this Act has been issued nothing in this Act shall prevent reference being made in legal proceedings to the slip or covering note or other customary memorandum of a contract of marine insurance.

[No change]

**Jurisdiction of the Federal Court of Australia**

**96. Jurisdiction is conferred on the Federal Court of Australia to be exercised concurrently with the courts of the states and territories in any matter arising under or relating to any contract of marine insurance.**

## SCHEDULES

## THE FIRST SCHEDULE

[No change]

Section 5

## IMPERIAL ACTS

Session and Chapter	Title or Short Title	Extent
19 Geo. 2, ch. 37	An Act to regulate insurance on ships belonging to the subjects of Great Britain, and on merchandises or effects laden thereon.	The whole.

28 Geo. 3, ch. 56	An Act to repeal an Act made in the twenty-fifth year of the reign of His present Majesty, intituled "An Marine Insurance Act for regulating insurance on ships, and on goods, merchandises, or effects," and for substituting other provisions for the like purpose in lieu thereof.	The whole so far as it relates to Marine Insurance
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## STATE ACTS

Short Title and Number	State	Extent
<i>Life, Fire, and Marine Insurance Act, 1902, No. 49.</i>	New South Wales	Section 17.
<i>The Instruments Act, 1890, No. 1103</i>	Victoria	Part III, Division 1.
<i>Prohibition to Re-Assurances Repeal Act 1867, No. 4.</i>	South Australia	The whole.
<i>The Marine Insurance Act 1907, No. 33</i>	Western Australia	The whole.
<i>The Policies of Marine Assurance Act 1869, No. 10.</i>	Tasmania	The whole.

~~THE SECOND SCHEDULE~~

[Repealed]

Section 36

## FORM OF POLICY

~~Lloyd's S.G. policy-~~

~~BE IT KNOWN THAT \_\_\_\_\_ as well in \_\_\_\_\_ own name as for and in the name and names of all and every other person or persons to whom the same doth, may, or shall appertain, in part or in all doth make assurance and cause and them, and every of them, to be insured lost or not lost, at and from~~

~~Upon any kind of goods and merchandises, and also upon the body, tackle, apparel, ordnance, munition, artillery, boat, and other furniture, of and in the good ship or vessel called the \_\_\_\_\_ whereof is master under God, for this present voyage, \_\_\_\_\_ or whosoever else shall go for master in the said ship, or by whatsoever other name or names the said ship, or the master thereof, is or shall be named or called; beginning the adventure upon the said goods and merchandises from the loading thereof aboard the said ship, upon the said ship, &c.~~

~~and so shall continue and endure, during her abode there, upon the said ship, &c., and further, until the said ship, with all her ordnance, tackle, apparel, &c.,~~

~~and goods and merchandises whatsoever shall be arrived at~~

~~upon the said ship, &c., until she hath moored at anchor twenty four hours in good safety; and upon the goods and merchandises, until the same be there discharged and safely landed. And it shall be lawful for the said ship, &c., in this voyage, to proceed and sail to and touch and stay at any ports or places whatsoever \_\_\_\_\_ without prejudice to this insurance. The said ship, &c., goods and merchandises, &c., for so much as concerns the assured by agreement between the assured and assurers in this policy, are and shall be valued at~~

~~Touching the adventures and perils which we the assurers are contented to bear and do take upon us in this voyage: they are of the seas, men of war, fire, enemies, pirates, rovers, thieves, jettisons, letters of mart and countermart, surprisals, takings at sea, arrests, restraints, and detainments of all kings, princes, and people, of what nation, condition, or quality soever, barratry of the master and mariners, and of all other perils, losses, and misfortunes, that have or shall come to the hurt, detriment, or damage of the said goods, and merchandises, and ship, &c., or any part thereof(a) And in the case of any loss or misfortune it shall be lawful to the assured, their factors, servants and assigns, to sue, labour, and travel for, in and about the defence, safeguards, and recovery of the said goods and merchandises, and ship, &c., or any part thereof, without prejudice to this insurance; to the charges whereof we, the assurers, will contribute each one according to the rate and quantity of his sum herein assured(b) And it is especially declared and agreed that no acts of the insurer or insured in recovering, saving, or preserving the property insured shall be considered as a waiver, or acceptance of abandonment. And it is agreed by us, the insurers, that this writing or policy of assurance shall be of as much force and effect as the surest writing or policy of assurance heretofore made in Lombard street, or in the Royal Exchange, or elsewhere in London. And so we, the assurers, are contented, and do hereby promise and bind ourselves, each one for his own part, our heirs, executors, and goods to the assured, their executors, administrators, and assigns, for the true performance of the premises, confessing ourselves paid the consideration due unto us for this assurance by the assured, at and after the rate of~~

~~IN WITNESS whereof we, the assurers, have subscribed our names and sums assured in London.~~

~~*N.B.* Corn, fish, salt, fruit, flour, and seed are warranted free from average, unless general, or the ship be stranded sugar, tobacco, hemp, flax, hides and skins are warranted free from average, under five per centum, and all other goods also the ship and freight, are warranted free from average, under three per centum unless general, or the ship be stranded.~~

## RULES FOR CONSTRUCTION OF POLICY

[Re-enacted in MIA s 3A]

The following are the rules referred to by this Act for the construction of a policy in the above or other like form, where the context does not otherwise require:-

### **Lost or not lost**

1. — Where the subject matter is insured “lost or not lost”, and the loss has occurred before the contract is concluded, the risk attaches unless, at such time, the assured was aware of the loss, and the insurer was not—

**From**

2. — Where the subject matter is insured “from” a particular place, the risk does not attach until the ship starts on the voyage insured.

**At and from**

3. — (a) Where a ship is insured “at and from” a particular place, and she is at that place in good safety when the contract is concluded, the risk attaches immediately.

(b) — If she be not at that place when the contract is concluded the risk attaches as soon as she arrives there in good safety, and, unless the policy otherwise provides, it is immaterial that she is covered by another policy for a specified time after arrival.

(c) — Where chartered freight is insured “at and from” a particular place and the ship is at that place in good safety, when the contract is concluded the risk attaches immediately. If she be not there when the contract is concluded, the risk attaches as soon as she arrives there in good safety.

(d) — Where freight, other than chartered freight, is payable without special conditions and is insured “at and from” a particular place, the risk attaches pro rata as the goods or merchandise are shipped; provided that if there be cargo in readiness which belongs to the ship owner, or which some other person has contracted with him to ship, the risk attaches as soon as the ship is ready to receive such cargo.

**From the loading thereof**

4. — Where goods or other movables are insured “from the loading thereof,” the risk does not attach until such goods or movables are actually on board, and the insurer is not liable for them while in transit from the shore to the ship.

**Safely landed**

5. — Where the risk on goods or other movables continues until they are “safely landed,” they must be landed in the customary manner and within a reasonable time after arrival at the port of discharge, and if they are not so landed the risk ceases.

**Touch and stay**

6. — In the absence of any further licence or usage, the liberty to touch and stay “at any port or place whatsoever” does not authorize the ship to depart from the course of her voyage from the port of departure to the port of destination.

**Perils of the seas**

7. — The term “perils of the seas” refers only to fortuitous accidents or casualties of the seas. It does not include the ordinary action of the winds and waves.

**Pirates**

8. — The term “pirates” includes passengers who mutiny and rioters who attack the ship from the shore.

**Thieves**

9. — The term “thieves” does not cover clandestine theft or a theft committed by any one of the ship's company, whether crew or passengers.

**Restraint of princes**

10. — The term “arrest, &c., of kings, princes, and people” refers to political or executive acts, and does not include a loss caused by riot or by ordinary judicial process.

**Barratry**

11. — The term “barratry” includes every wrongful act wilfully committed by the master or crew to the prejudice of the owner, or, as the case may be, the charterer.

**All other perils**

12. — The term “all other perils” includes only perils similar in kind to the perils specifically mentioned in the policy.

**Average unless general**

13. — The term “average unless general” means a partial loss of the subject matter insured other than a general average loss, and does not include “particular charges.”

**Stranded**

14. — Where the ship has stranded, the insurer is liable for the excepted losses, although the loss is not attributable to the stranding, provided that when the stranding takes place the risk has attached and, if the policy be on goods, that the damaged goods are on board.

**Ship**

15. — The term “ship” includes the hull, materials and outfit, stores and provisions for the officers and crew, and, in the case of vessels engaged in a special trade, the ordinary fittings requisite for the trade, and also, in the case of a steam ship, the machinery, boilers, and coals and engine stores, if owned by the assured.

**Freight**

16. — The term “freight” includes the profit derivable by a ship owner from the employment of his ship to carry his own goods or movables, as well as freight payable by a third party, but does not include passage money.

**Goods**

17. — The term “goods” means goods in the nature of merchandise, and does not include personal effects or provisions and stores for use on board. In the absence of any usage to the contrary, deck cargo and living animals must be insured specifically, and not under the general denomination of goods.





## Appendix C

# Draft Marine Insurance Amendment Bill

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Under its terms of reference the Commission is required to prepare the appropriate legislation and explanatory memorandum to give effect to the recommendations in this report. The draft legislation is found in this appendix and the draft explanatory memorandum in appendix D.

The draft Bill is intended to produce an amended *Marine Insurance Act* in a form that reflects the consolidated text set out in appendix B to this report. It also inserts a new s 9B into the *Insurance Contracts Act 1984* (Cth) in accordance with recommendation 2.

The recommended changes to the *Insurance (Agents and Brokers) Act 1984* (Cth) and the Financial Services Reform Bill are not included in this appendix as the terms of the necessary amendments depend on the fate of legislation that is still under consideration by the government.

Schedule 1 of the draft Bill does not contain any items relating to alternative recommendations 30–31, which apply if the Commission’s primary recommendation that the requirement for an insurable interest be abolished (recommendation 28) is not adopted. Notes in the text indicate in general terms the changes that would be necessary to give effect to the alternative recommendations.

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2001

The Parliament of the  
Commonwealth of Australia

HOUSE OF REPRESENTATIVES/THE SENATE

*Presented and read a first time*

## **Marine Insurance Amendment Bill 2001**

**No.     , 2001**

*(Attorney-General)*

**A Bill for an Act to amend the *Marine Insurance Act 1909* and the *Insurance Contracts Act 1984* and for related purposes**

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**A Bill for an Act to amend the *Marine Insurance Act 1909* and the *Insurance Contracts Act 1984* and for related purposes**

The Parliament of Australia enacts:

**1 Short title**

This Act may be cited as the *Marine Insurance Amendment Act 2001*.

**2 Commencement**<sup>1154</sup>

- (1) Subject to subsection (2), this Act commences on a date to be proclaimed.
- (2) Items 61 and 62 of Schedule 1 commence on the day on which [relevant provisions] of the *Financial Services Reform Act 2001* commence.

**3 Application**

This Act applies to all contracts of marine insurance concluded or renewed on or after the day on which this Act commences.

**4 Schedules**

Subject to section 2, each Act that is specified in a Schedule to this Act is amended or repealed as set out in the applicable items in the

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<sup>1154</sup> The terms of this subsection will need to be varied to meet the actual circumstances of the passage of the Financial Services Reform Bill or to reflect the date on which the recommended changes to the *Insurance (Agents and Brokers) Act 1984* (Cth) come into effect.

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3

Schedule concerned, and any other item in a Schedule to this Act has effect according to its terms.

## Schedule 1—Amendment of the *Marine Insurance Act 1909*

### 1 After section 3

Insert:

#### 3A Construction of terms in policy

The following rules are to be applied in the construction of a policy where the context does not otherwise require:

- (1) **Lost or not lost** Where the subject-matter is insured “lost or not lost”, and the loss has occurred before the contract is concluded, the risk attaches unless, at such time, the assured was aware of the loss, and the insurer was not.
- (2) **From** Where the subject-matter is insured “from” a particular place, the risk does not attach until the ship starts on the voyage insured.
- (3) **At and from** (a) Where a ship is insured “at and from” a particular place, and it is at that place in good safety when the contract is concluded, the risk attaches immediately.
  - (b) If it is not at that place when the contract is concluded the risk attaches as soon as it arrives there in good safety, and, unless the policy otherwise provides, it is immaterial that it is covered by another policy for a specified time after arrival.
  - (c) Where chartered freight is insured “at and from” a particular place and the ship is at that place in good safety, when the contract is concluded the risk attaches immediately. If it is not there when the contract is concluded, the risk attaches as soon as it arrives there in good safety.
  - (d) Where freight, other than chartered freight, is payable without special conditions and is insured “at and from” a particular place, the risk attaches pro rata as the goods or merchandise are shipped; provided that if there is cargo in readiness which belongs to the ship-owner, or which some other person has contracted with him to ship,

- 1 the risk attaches as soon as the ship is ready to receive such  
2 cargo.
- 3 (4) **From the loading thereof** Where goods or other movables are  
4 insured “from the loading there of,” the risk does not attach until  
5 such goods or movables are actually on board, and the insurer is  
6 not liable for them while in transit from the shore to the ship.
- 7 (5) **Safely landed** Where the risk on goods or other movables  
8 continues until they are “safely landed”, they must be landed in  
9 the customary manner and within a reasonable time after arrival  
10 at the port of discharge, and if they are not so landed the risk  
11 ceases.
- 12 (6) **Touch and stay** In the absence of any further licence or usage,  
13 the liberty to touch and stay “at any port or place whatsoever”  
14 does not authorize the ship to depart from the course of its  
15 voyage from the port of departure to the port of destination.
- 16 (7) **Perils of the seas** The term “perils of the seas” refers only to  
17 fortuitous accidents or casualties of the seas. It does not include  
18 the ordinary action of the winds and waves.
- 19 (8) **Pirates** The term “pirates” includes passengers who mutiny and  
20 rioters who attack the ship from the shore.
- 21 (9) **Thieves** The term “thieves” does not cover clandestine theft or a  
22 theft committed by any one of the ship’s company, whether crew  
23 or passengers.
- 24 (10) **Restraint of princes** The term “arrest, &c., of kings, princes, and  
25 people” refers to political or executive acts, and does not include  
26 a loss caused by riot or by ordinary judicial process.
- 27 (11) **Barratry** The term “barratry” includes every wrongful act  
28 wilfully committed by the master or crew to the prejudice of the  
29 owner, or, as the case may be, the charterer.
- 30 (12) **All other perils** The term “all other perils” includes only perils  
31 similar in kind to the perils specifically mentioned in the policy.
- 32 (13) **Average unless general** The term “average unless general”  
33 means a partial loss of the subject-matter insured other than a  
34 general average loss, and does not include “particular charges.”
- 35 (14) **Stranded** Where the ship has stranded, the insurer is liable for  
36 the excepted losses, although the loss is not attributable to the  
37 stranding, provided that when the stranding takes place the risk  
38 has attached and, if the policy is on goods, that the damaged  
39 goods are on board.

- 1 (15) **Ship** The term “ship” includes the hull, materials and outfit,  
 2 stores and provisions for the officers and crew, and, in the case  
 3 of vessels engaged in a special trade, the ordinary fittings  
 4 requisite for the trade, and also, in the case of a steam-ship, the  
 5 machinery, boilers, and coals and engine stores, if owned by the  
 6 assured.
- 7 (16) **Freight** The term “freight” includes the profit derivable by a  
 8 ship-owner from the employment of his ship to carry his own  
 9 goods or movables, as well as freight payable by a third party,  
 10 but does not include passage money.
- 11 (17) **Goods** The term “goods” means goods in the nature of  
 12 merchandise, and does not include personal effects or provisions  
 13 and stores for use on board. In the absence of any usage to the  
 14 contrary, deck cargo and living animals must be insured  
 15 specifically, and not under the general denomination of goods.

## 16 2 Section 7

17 Omit “A”, substitute “Subject to sections 9A and 9B of the *Insurance*  
 18 *Contracts Act 1984*, a”.

## 19 3 Subsection 8(1)

20 Omit “on inland waters or”.

21 Note: The heading to section 8 is replaced by the heading “**Scope of marine insurance**”.

## 22 4 Subsection 8(1)

23 After “land”, insert “or air”.

## 24 5 Subsection 8(2)

25 Repeal the subsection, substitute:

- 26 (2) Unless the contract otherwise provides, a ship in course of building or  
 27 repairs, the launch of a ship, or any adventure analogous to a marine  
 28 adventure is covered by the provisions of this Act, in so far as  
 29 applicable; but, except as by this section provided, nothing in this Act  
 30 shall alter or affect any rule of law applicable to any contract of  
 31 insurance other than a contract of marine insurance as by this Act  
 32 defined.

## 33 6 At the end of section 8

34 Add:



1 (3) Unless it expressly provides otherwise, a contract of marine insurance  
2 protects the assured against losses on all inland waters.

3 (4) Unless the contract expressly provides otherwise or the context  
4 requires otherwise, all references in this Act and in a contract of  
5 marine insurance to the “sea” and the “seas” include references to  
6 inland waters.

7 **7 Section 10**<sup>1155</sup>

8 Repeal the section, substitute:

9 **10 Insurable interest not required**

10 A contract of marine insurance is not void by reason only that the  
11 assured did not have, at the time when the contract was entered into,  
12 an interest in the subject matter of the contract.

13 **8 Section 11**

14 Repeal the section, substitute:

15 **11 Legal or equitable interest not required at time of loss**

16 Where the assured under a contract of marine insurance has suffered a  
17 pecuniary or economic loss by reason that property the subject matter  
18 of the contract has been damaged or destroyed, the insurer is not  
19 relieved of liability under the contract by reason only that, at the time  
20 of loss, the assured did not have an interest at law or in equity in the  
21 property.

22 **9 Section 12**

23 Repeal the section.

24 **10 Section 13**

25 Repeal the section.

26 **11 Section 14**

27 Repeal the section.

---

1155 If the Commission’s recommendation that the requirement for an insurable interest be abolished is not adopted, items 7 to 18 in schedule 1 should be replaced by items amending MIA s 16 and inserting a new s 19A as recommended in alternative recommendations 30–31: see fn 1 and 2 in appendix B.

1     **12 Section 15**

2             Repeal the section.

3     **13 Section 16**

4             Repeal the section.

5     **14 Section 17**

6             Repeal the section.

7     **15 Section 18**

8             Repeal the section.

9     **16 Section 19**

10            Repeal the section.

11    **17 Section 20**

12            Repeal the section.

13    **18 Section 21**

14            Repeal the section.

15    **19 Section 23**

16            Repeal the section, substitute:

17    **23 Duty of utmost good faith**

18            (1) A contract of marine insurance is a contract based on the utmost good  
19            faith and there is implied in such a contract a provision requiring each  
20            party to it to act towards the other party, in respect of any matter  
21            arising under or in relation to it, with the utmost good faith.

22            (2) If reliance by a party to a contract of marine insurance on a provision  
23            of the contract would be to fail to act with the utmost good faith, the  
24            party may not rely on the provision.

25            (3) Subsection (2) does not limit the operation of subsection (1).

26            (4) In deciding whether reliance by an insurer on a provision of a contract  
27            of marine insurance would be to fail to act with the utmost good faith,  
28            the court shall have regard to any notification of the provision that was

1 given to the assured, whether a notification of a kind mentioned in this  
2 Act or otherwise.

- 3 (5) The requirement that each party act toward the other party with the  
4 utmost good faith extends for the duration of the relationship between  
5 the parties set out in the contract of marine insurance except in  
6 relation to any claim or other aspect of the relationship which  
7 becomes the subject of litigation between the parties, in which case  
8 the requirement ceases when the litigation is commenced but only in  
9 relation to the claim or other aspect that is the subject of that litigation.

## 10 **20 Subsection 24(1)**

11 Repeal the subsection, substitute:

- 12 (1) Subject to the provisions of this section, the assured must disclose to  
13 the insurer, before the contract is concluded, every circumstance  
14 which is known to the assured, or which a reasonable person in the  
15 circumstances could be expected to know, to be material.

## 16 **21 Paragraph 24(3)(d)**

17 Omit “or implied warranty”, substitute “term of the contract”.

## 18 **22 Subsection 25(a)**

19 Omit the subsection, substitute:

- 20 (a) every material circumstance which is known to the agent, or which a  
21 reasonable person in the circumstances could be expected to know, to  
22 be material; and

## 23 **23 Subsection 26(1)**

24 Omit the second sentence.

## 25 **24 After section 26**

26 Insert:

## 27 **26A No other duty of disclosure**

- 28 (1) Without otherwise limiting or restricting section 23 of this Act, this  
29 Act does not, and a contract of marine insurance may not, impose on  
30 an assured a duty of disclosure before the contract is concluded  
31 greater than that provided for by this Act.

- 1 (2) A contract of marine insurance may include an express term providing  
2 for a duty of disclosure by the assured after the contract has been  
3 concluded.

#### 4 **26B Remedies for non-disclosure and misrepresentation**

- 5 (1) Subject to any contrary term in the contract, if there is a breach by the  
6 assured or its agent of the obligations in sections 24, 25 or 26 the  
7 following subsections apply.
- 8 (2) If the breach is fraudulent the insurer is entitled to avoid the contract.
- 9 (3) If the breach is not fraudulent and the insurer proves that the non-  
10 disclosure or misrepresentation induced it to enter into the contract:
- 11 (a) if the insurer proves that it would not have entered into the  
12 contract if there had been no breach — the insurer is entitled to  
13 avoid the contract but must return the premium to the assured.
- 14 (b) if the insurer proves that it would have entered into the contract  
15 but on different terms — the insurer:
- 16 (i) is not entitled to avoid the contract; and  
17 (ii) is not liable to indemnify the assured for any loss  
18 proximately caused by the undisclosed or misrepresented  
19 circumstance; and  
20 (iii) is entitled to reduce any liability that it may have to the  
21 assured to reflect any variation in premium, deductible or  
22 excess that the insurer would have required if there had  
23 been no breach; and  
24 (iv) is entitled to cancel the policy in accordance with section  
25 47A.

#### 26 **26C No greater remedies**

27 A contract of marine insurance may not provide for any remedies for a  
28 breach by the assured or its agent of the obligations in sections 24, 25  
29 or 26 more favourable to the insurer than those provided for by section  
30 26B.

#### 31 **26D Following insurers**

- 32 (1) This section applies if there is a breach by the assured or its agent of  
33 the obligations in sections 24, 25 or 26 and it is proved that an insurer

(in this section called the “following insurer”) underwrote a proportion of a risk on a contract of marine insurance only because one or more other insurers (in this section called the “leading insurers”) had already underwritten a proportion of the risk.

- (2) The following insurer is deemed to have been induced to enter into the contract by the breach only if all of the leading insurers were induced by the breach to enter into the contract.

## **25 Section 28**

Omit the first sentence, substitute:

Subject to section 58, the insurer or its agent must issue a policy, or procure the issue of a policy, setting out expressly all the terms of the contract of marine insurance.

## **26 At the end of section 29**

Add:

- (2) No marine policy is invalid by reason only that it does not comply with subsection (1).

## **27 Subsection 31(2)**

Repeal the subsection.

## **28 Subsection 35(1)**

After “floating” insert “, open or annual”.

Note: The heading to section 35 is replaced by the heading “**Floating, open and annual policies**”.

## **29 Subsection 35(1)**

After “ships” insert “or other insurable property”.

## **30 Subsection 35(3)**

Omit “shipment. They”, substitute “shipment and they”.

## **31 Subsection 35(3)**

Omit “policy and the”, substitute “policy. The”.

## **32 Section 36**

Repeal the section.

1     **33 Division 7 of Part II (heading)**

2             Omit the heading, substitute:

3     **Division 7—Breach of contractual terms**

4     **34 Section 39**

5             Omit the section, substitute:

6     **39 No warranties**

7             (1) Subject to this Act, no express or implied term in a contract of marine  
8                 insurance is a warranty or otherwise has the effect that any breach of it  
9                 by the assured entitles the insurer to be discharged from any liability  
10                under the contract.

11            (2) Subject to this Act, an express term in a contract of marine insurance  
12                may provide that, if there is a breach by the assured of an express term  
13                in the contract, the insurer is discharged from all liability to indemnify  
14                the assured for any loss proximately caused by the breach.

15            (3) Without prejudice to any other burden of proof provided for by statute  
16                or common law, the insurer bears the burden of proving that there was  
17                a breach of a term of the contract and the assured bears the burden of  
18                proving that the loss for which it seeks to be indemnified was not  
19                proximately caused by or attributable to, as the case requires, the  
20                breach.

21     **35 Subsection 40(1)**

22             Repeal the subsection, substitute:

23             (1) Non-compliance with a term of a contract of marine insurance is  
24                 excused when, by reason of a change of circumstances, the term  
25                 ceases to be applicable to the circumstances of the contract, or when  
26                 compliance with the term is rendered unlawful by any subsequent law.

27     Note:    The heading to section 40 is replaced by the heading “**When breach of contractual term**  
28                **excused**”.

29     **36 Subsection 40(2)**

30             Repeal the subsection.

**37 Subsection 40(3)**

Omit “of warranty”, substitute “by the assured of any term of a contract of marine insurance”.

**38 Section 41**

Repeal the section.

**39 Section 42**

Repeal the section

**40 Section 43**

Repeal the section.

**41 Section 44**

Repeal the section.

**42 Subsection 45(1)**

Repeal the subsection, substitute:

- (1) There is no implied warranty in any contract of marine insurance that any ship is seaworthy at any time during the insured adventure.

Note: The heading to section 45 is replaced by the heading “**Terms relating to seaworthiness of ship**”.

**43 Subsection 45(2)**

Repeal the subsection, substitute:

- (2) A contract of marine insurance may contain an express term that a ship is seaworthy at any time or during any period within the period of cover of the contract and that the insurer is discharged from all liability to indemnify the assured for any loss attributable to any breach of this term if the assured:
- (a) knew, or ought to have known, of the facts and circumstances that rendered the ship unseaworthy and that they rendered the ship unseaworthy; and
  - (b) failed to take such steps as were reasonably available to it to make the ship seaworthy.

**44 Subsection 45(3)**

Repeal the section, substitute:

- (3) A contract of marine insurance may not contain a term that relates to the seaworthiness of a ship that is more favourable to the insurer than that provided for by this section.

**45 Subsection 45(5)**

Repeal the subsection.

**46 Subsection 46(1)**

Repeal the subsection, substitute:

- (1) In a policy of marine insurance there is no implied warranty that any goods or movables are seaworthy.

**47 Subsection 46(2)**

Repeal the subsection.

**48 Section 47**

Repeal the section, substitute:

**47 Terms relating to legality**

- (1) There is no warranty in any contract of marine insurance that the adventure is lawful or that it shall be carried out in a lawful manner.
- (2) A contract of marine insurance may include an express term to the effect that, so far as the assured can control the matter, the insured adventure shall have no unlawful purpose and that, if there is a breach of any such term, the insurer is discharged from all liability under the policy and is not required to return any part of the premium to the assured.
- (3) A contract of marine insurance may include an express term to the effect that, so far as the assured can control the matter, the insured adventure shall be carried out in a lawful manner and that, if there is a breach of any such term, the insurer is discharged from all liability to indemnify the assured for any loss attributable to that breach.



- 1 (4) A contract of marine insurance may not contain a term requiring the  
2 insured adventure to be lawful or that it be carried out in a lawful  
3 manner that is more favourable to the insurer than those provided for  
4 by this section.

5 **49 After section 47**

6 Insert:

7 **47A Cancellation of contracts of marine insurance**

- 8 (1) Subject to any express term in a contract of marine insurance, where:  
9 (a) the assured has failed to comply with a provision of the contract;  
10 or  
11 (b) the assured did not comply with the duty of utmost good faith;  
12 or  
13 (c) the assured has made a fraudulent claim under the contract; or  
14 (d) this Act otherwise permits;

15 the insurer may cancel the contract in accordance with this section.

- 16 (2) An insurer who wishes to exercise a right to cancel a contract of  
17 marine insurance, whether under this section or pursuant to an express  
18 term of the contract, shall give notice in writing of the proposed  
19 cancellation to the assured.

- 20 (3) Any notice of an insurer's intention to cancel a contract of marine  
21 insurance has effect to cancel the contract at any time specified in the  
22 notice after the earlier of the following times:  
23 (a) the time when another contract of marine insurance between the  
24 assured and the insurer or some other insurer, being a contract  
25 that is intended by the assured to replace the first-mentioned  
26 contract, is entered into;  
27 (b) 4 pm on the third business day after the day on which the notice  
28 was given to the insured.

29 **50 Section 48**

30 Repeal the section.

31 **51 Section 51**

32 Repeal the section.

1 **52 Section 52**

2 Repeal the section.

3 **53 Section 53**

4 Repeal the section.

5 **54 Section 54**

6 Repeal the section.

7 **55 Section 55**

8 Repeal the section.

9 **56 Part III (heading)**

10 Omit the heading, substitute:

11 **PART III—ASSIGNMENT OF POLICY OR**  
12 **CONTRACT**

13 **57 Subsection 56(1)**

14 After “policy” insert “or contract of marine insurance”.

15 Note: The heading to section 56 is replaced by the heading “**When and how policy or contract is**  
16 **assignable**”.

17 **58 Subsection 56(2)**

18 Repeal the subsection, substitute:

- 19 (2) Where a marine policy or contract of marine insurance has been  
20 assigned so as to pass the beneficial interest in the policy or contract,  
21 the assignee of the policy or contract is entitled to sue thereon in its  
22 own name; and the defendant is entitled to make any defence arising  
23 out of the policy or contract which it would have been entitled to  
24 make if the action had been brought in the name of the person by or  
25 on behalf of whom the policy or contract was effected.

26 **59 Subsection 56(3)**

27 After “policy” insert “or contract of marine insurance”.

28

1 **60 Section 57**

2 Repeal the section.

3 **61 Section 59**<sup>1156</sup>

4 Repeal the section.

5 **62 Section 60**<sup>1157</sup>

6 Repeal the section.

7 **63 Subsection 82(1)**

8 Omit “Where the subject-matter insured is warranted free”, substitute  
9 “Where a contract of marine insurance contains an express term that the  
10 subject matter is free”.

11 Note: The heading to section 82 is replaced by the heading “**Contractual terms relating to**  
12 **particular average**”.

13 **64 Subsection 82(2)**

14 Omit “Where the subject-matter insured is warranted free”, substitute  
15 “Where a contract of marine insurance contains an express term that the  
16 subject matter is free”.

17 **65 Subsection 82(3)**

18 Omit “where the subject-matter insured is warranted free”, substitute  
19 “where a contract of marine insurance contains an express term that the  
20 subject matter is free”.

21 **66 Subsection 84(1)**

22 Omit “or that the subject-matter may have been warranted free”, substitute  
23 “or that the contract of marine insurance may contain an express term that  
24 the subject matter is free”.

25 **67 After section 85**

26 Insert:

---

1156 The wording of this item will depend on how and when the *Insurance (Agents and Brokers) Act 1984* or the Financial Services Reform Bill 2000 is amended.

1157 The wording of this item will depend on how and when the *Insurance (Agents and Brokers) Act 1984* or the Financial Services Reform Bill 2000 is amended.

**85A Contracts affecting rights of subrogation**

- (1) Where a contract of marine insurance includes a provision that has the effect of excluding or limiting the insurer's liability in respect of a loss by reason that the assured is a party to an agreement that excludes or limits a right of the assured to recover damages from a person other than the insurer in respect of the loss, the insurer may not rely on the provision unless the insurer clearly informed the assured in writing, before the contract of marine insurance was entered into, of the effect of the provision.
- (2) The duty of disclosure does not require the assured to disclose the existence of a contract that so limits the assured's rights.

**68 After section 87**

Insert:

**87A Rights with respect to moneys recovered from third parties**

- (1) Where money is recovered from a third party in respect of a loss that is wholly or partly the subject of a contract of marine insurance, that money shall, subject to any contrary agreement between the insurer and the assured, be distributed in the following manner and order.
- (2) The party or parties funding the recovery action shall be reimbursed for its or their administrative and legal costs incurred in connection with that action. If there is insufficient money recovered for full reimbursement, the parties shall be reimbursed pro rata.
- (3) If:
- (a) The insurer has funded the action under its rights of subrogation, it is entitled to retain or be paid an amount equal to the amount that it has paid to the assured under the contract of marine insurance. The assured is then entitled to be paid an amount that, together with any amount that it has received from the insurer under the contract of marine insurance, will indemnify it in full for its loss.
- (b) The assured has funded the action, it is entitled to retain an amount that, together with any amount that it has received from the insurer under the contract of marine insurance, will indemnify it in full for its loss. The insurer is then entitled to be

- 1                   paid an amount equal to the amount that it has paid to the  
2                   assured under the contract of marine insurance.
- 3                   (c) The insurer and the assured have funded the action jointly, they  
4                   are entitled to the amounts referred to in paragraphs (a) and (b).  
5                   If there is insufficient money recovered for full reimbursement,  
6                   the parties shall be reimbursed pro rata.
- 7                   (4) Any further amount recovered from the third party is to be paid to the  
8                   parties to the contract of marine insurance pro rata in accordance with  
9                   the ratio in which they contributed to the administrative and legal  
10                  costs of the recovery action.
- 11                  (5) Notwithstanding anything else in this section, any separate or  
12                  identifiable components in respect of interest are to be paid to the  
13                  insurer and the assured in such proportions as fairly reflect the  
14                  amounts that each has recovered from the third party and the periods  
15                  of time for which each lost the use of its money.

16                  **69 Paragraph 90(3)(c)**

17                    Repeal the paragraph.

18                  **70 Paragraph 90(3)(d)**

19                    Repeal the paragraph.

20                  **71 Subsection 91(1)**

21                    After “other”, insert “, or agree to form an association to insure each  
22                    other,”.

23                  **72 After section 95**

24                    Insert:

25                  **96 Jurisdiction of the Federal Court of Australia**

26                    Jurisdiction is conferred on the Federal Court of Australia to be  
27                    exercised concurrently with the courts of the states and territories in  
28                    any matter arising under or relating to any contract of marine  
29                    insurance.

30                  **73 Schedule 2**

31                    Repeal the Schedule.

32

1  
2 **Schedule 2—Amendment of the *Insurance***  
3 ***Contracts Act 1984***

4 **1 After section 9A**

5 Insert:

6 **9B Exclusion of carriage of non-commercial goods for the *Marine***  
7 ***Insurance Act 1909***

8 The *Marine Insurance Act 1909* does not apply to a contract of  
9 insurance for the transportation of goods other than goods being  
10 transported for the purposes of a business, trade, profession or  
11 occupation carried on or engaged in by the insured.

# Appendix D

## Draft Explanatory Memorandum

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### Marine Insurance Amendment Bill 2001

#### Outline

This Bill is based on the recommendations found in the report of the Australian Law Reform Commission (the Commission) no 91 entitled *Review of the Marine Insurance Act 1909* (ALRC 91). That reports recommends a number of amendments to the *Marine Insurance Act 1909* (MIA) and one amendment to the *Insurance Contracts Act 1984* (ICA), which are dealt with by this Bill. The Commission also recommended amendments to the *Insurance (Agents and Brokers) Act 1984* (Cth) or the Financial Services Reform Bill 2000 and these are included in this Bill.<sup>1158</sup>

The recommendations in the Commission's report involve the retention of the MIA as a separate legislative regime governing marine insurance, distinct from the ICA, which governs non-marine general insurance not otherwise covered by separate statutory schemes. Although the amendments narrow the gap between the MIA and the ICA, the Commission considered that the familiarity of practitioners both within Australia and overseas with the basic structure of the MIA warranted its retention as a separate scheme as the amendments were more readily identifiable and accommodated by those practitioners. Furthermore, if all marine insurance contracts had been put under the ICA regime, a significant number of provisions of the MIA would have had to be re-enacted in the ICA to cover a large number of distinctive provisions that underpin marine insurance contracts both in Australia and in other countries whose legislation is based on the Marine Insurance Act 1906 of the United Kingdom. Accordingly, this Bill does not repeal the MIA.

The amendments to the MIA fall into four broad categories, with a series of smaller amendments in other, particular areas. The four principal areas are:

- the coverage of the MIA;
- warranties and in particular, the harshness of the remedies available to insurers in the event of breach by an assured;

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<sup>1158</sup> The inclusion and wording of the last sentence in this paragraph will depend on whether and when the changes recommended by the Commission to the *Insurance (Agents and Brokers) Act 1984* (Cth) and the Financial Services Reform Bill 2000 are made.

- the duty of good faith and its particular manifestation in the obligations on an assured for complete and accurate disclosure before the contract is concluded; and
- the requirement for an insurable interest, which has produced some difficulties in a particular range of cases.

### ***The coverage of the Marine Insurance Act***

The Commission made two recommendations in this area. The first is the removal from the MIA to the ICA of contracts for the transportation of goods for non-commercial purposes. This is consistent with the overall approach that consumer contracts of insurance should be covered by the ICA (although that Act also covers many forms of commercial insurance) and extends the refinement in this area commenced by the enactment in 1998 of section 9A of the ICA, pursuant to which the insurance of pleasure craft was moved from the MIA to the ICA. Consistently with that amendment, the Commission recommends that a new section 9B be inserted into the ICA rather than amending the MIA itself.

The second principal change is to extend the MIA to cover insurance of adventures on inland waters. At present, the Act's operation is confined to maritime adventures (that is, sea voyages) and incidental non-maritime risks. There is some difficulty in determining the point at which a contract covering numerous and varied insurance risks ceases to be covered by the MIA and is therefore covered by the ICA. Although the statute cannot be re-worded so as to avoid all further uncertainty, the modest expansion recommended in this regard removes some areas of uncertainty. It is also consistent with the overall philosophy that consumer insurance of a maritime nature should be covered by the ICA but commercial marine insurance should be covered by MIA. The distinction between insurance covered by the two Acts is based on the commercial or non-commercial nature of the insured activities.

### ***Warranties***

The Commission's recommendations in relations to warranties have two purposes. The first is to soften the often harsh and disproportionate impact on an assured of the remedies currently provided by the MIA in favour of insurers. Secondly, and consistently with certain other recommendations, the amendments will force warranties, especially implied warranties, onto the face of the contract so that both parties, and the assured in particular, can be under no misapprehension as to the content of the contract, the terms that they are required to comply with and the ramifications of any breaches.

To this end, the Commission has recommended the abolition of the concept of warranties. However, in place of express warranties, the Commission has proposed



a regime under which the insurer has a number of structured remedies available to it should there be a breach of any express term of the contract by the assured.

In place of express warranties, the MIA will permit contracts of marine insurance to include express terms that provide that, in the event of a breach by the assured of any express term (or any range of express terms) the insurer will be discharged from liability to indemnify the assured for all loss that is proximately caused by that breach. At present, the insurer is automatically discharged from all further liability under the contract irrespective of the scale of the assured's breach or whether it caused or contributed to the loss.

The Commission also recommended that the implied warranties of seaworthiness and legality be removed but that the Act should be amended to permit contracts of marine insurance to include express terms relating to the seaworthiness of a ship and in relation to the legality of the purpose of the insured voyage and the manner in which it is carried out. In order to obtain the protection that is currently available to them under the MIA (to the extent that it is preserved under the amendments), insurers will be required to reword their documentation so that all terms on which they wish to rely appear on the face of the contract. Modern insurance practice often includes express terms dealing with these matters, which, to the extent of any inconsistency, override the warranties implied by the MIA. Accordingly, the amendments may in fact force relatively few changes in practice.

The remedies for a breach of an express term relating to the seaworthiness of a ship are essentially the same as for a breach of any other express term except that the insurer is no longer liable to indemnify the assured for loss which is 'attributable' to the breach. The term 'attributable' has been used to better reflect the current position and in contrast to the stricter test of proximate causation. Therefore, a causal connection between the unseaworthiness of the ship and the loss that is looser than that required in relation to other express terms will entitle an insurer to relief. However, this applies only if the breach of a term relating to unseaworthiness arises where the assured was aware of the facts constituting the unseaworthiness, that those facts constituted unseaworthiness, and failed to take whatever steps might reasonably have been available to it to remedy the position. Thus, assureds who do not know of the unseaworthiness, or were in no position to do anything about it once it arose, will remain covered. This preserves some elements of the current position in relation to time policies.

As a matter of public policy, the Commission has recommended that an insurer be relieved of all liability under a contract of marine insurance if the insured voyage is carried out for an illegal purpose, at least to the extent that the assured was in the position to control the matter. In that event, the premium is not returnable as the breach can be regarded as serious as fraud. If, on the other hand, the voyage is not carried out in a legal manner, which may involve only a relatively slight technical

breach of regulation, the insurer is only relieved of liability to indemnify the assured for any loss attributable to the breach of warranty. Accordingly, trivial or purely technical breaches which do not lead to loss will not prejudice an assured if loss is caused by some other insured peril.

One major criticism of the operation of warranties in the MIA is that any breach, however trivial and unrelated to any loss, entitles the insurer to be relieved automatically of all liability under the policy from the date of the breach, although without prejudice to any liabilities that may have arisen prior to the breach. There is no capacity for the assured to remedy the breach, and the remedies available to the insurer are the same whether or not the breach was in any way causative of the loss, fraudulent, or negligent (with some qualifications). The proposed remedy for breach of an express term is that the insurer, although not discharged from liability under the policy as a whole, is discharged from all liability to indemnify the assured for any loss which was proximately caused by the breach. The policy otherwise remains on foot. In this way, the assured cannot benefit from its breach but retains the benefit of the policy as a whole. On the other hand, the insurer is not bound to indemnify the assured for a loss caused by the assured's own breach of contract.

Although not stated in the amended MIA, the assured acquires the ability to remedy a breach of a contractual term before loss as a logical consequence of these amendments.

The statutory provisions may be modified by the contract but the amended MIA prevents a term being included in a contract of marine insurance that provides for remedies more favourable to the insurer.

If there is any breach of an express term of any sort, the insurer will be entitled to avail itself of a new statutory right of cancellation of the policy, subject to anything to the contrary in its contract. At present, the MIA does not have any provision granting the insurer the right to terminate the contract if there is a breach by the assured although such provisions were introduced into the ICA. The Commission considers that the MIA and ICA should be parallel in this respect. The statutory right of cancellation allows an insurer to bring a contract to an end where there has been a significant breach by the assured. The statutory right of cancellation also applies (as with the parallel provision in the ICA) where the assured has breached its duty of disclosure, its duty of utmost good faith or has made a fraudulent claim.

### ***Utmost good faith***

The reforms in this area recommended by the Commission fall into two broad categories: reform of the basic nature of the obligations of utmost good faith and

reforms relating to the specific duties of the assured in relation to complete and accurate disclosure of material circumstances before the contract is concluded.

At present, the MIA provides that utmost good faith is the basis of every contract of marine insurance and that, if one party does not observe the utmost good faith in relation to the other, the other party may avoid the contract entirely. This remedy is, however, of almost no value to assureds, who in most cases would want the contract to remain on foot if there has been any breach by the insurer so that the assured gets the benefit of indemnity if there is any loss. The avoidance of the policy and return of the premium would often be of little, if any, assistance.

This concept was amended in relation to non-marine insurance by the ICA, which makes the duty of utmost good faith an implied term of the contract. As a result, if there is any breach of the duty of utmost good faith, a much wider range of remedies is available to a court than is currently provided by the MIA, most notably, an award of damages, which may much more effectively compensate the innocent party.

Under the amended MIA, a breach of the obligations of utmost good faith by the assured now entitles the insurer to cancel the policy under the new statutory right of cancellation, subject to anything to the contrary in the contract.

The amendments in relation to the obligations for complete and accurate disclosure (which require full disclosure of all material circumstances and prohibit misrepresentation) before the contract is concluded have been modified to accommodate two problematic areas. Firstly, the current regime requires an assured (or its agent) to disclose accurately all material circumstances. Circumstances are material if they would influence a prudent insurer in determining whether it will accept the risk and, if so, on what terms. They do not have to have a decisive influence on the prudent insurer. This imposes on the assured an obligation to understand what is material to a prudent insurer. Secondly, prior to the decisions of the House of Lords in *Pan Atlantic Insurance Co Ltd v Pine Top insurance Co Ltd*<sup>1159</sup> and the Supreme Court of Victoria in *Akedian Co Ltd v Royal Insurance Australia Ltd, Sun Alliance Australia Ltd*<sup>1160</sup> there was no requirement that the actual insurer be induced by the non-disclosure or misrepresentation to enter into the contract. Accordingly, an imprudent insurer could avoid the consequences of its imprudence by relying on the objective standard of a prudent insurer.

The Commission's recommendations modify the requirement of disclosure and prohibition of misrepresentation so that the assured is required only to disclose

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1159 [1995] 1 AC 501.

1160 (1997) 148 ALR 480.

those circumstances which it knows to be material or which a reasonable person in its position would know to be material. The test of materiality is itself unchanged.

However, except in the case of fraud, the insurer is no longer entitled to avoid any liability unless it was actually induced by the non-disclosure or misrepresentation to enter into the contract. If the misrepresentation or non-disclosure is fraudulent, the insurer is entitled to avoid the contract entirely and to keep the premium. If the breach is not fraudulent but the insurer proves that it would not have entered into the contract at all, the insurer is entitled to avoid the policy but must return the premium. If it proves that it would have entered into the contract but on different terms, the insurer is not relieved from liability under the contract as a whole. However, it does not have to indemnify the assured for any loss attributable to the matter which was the subject of the misrepresentation or non-disclosure, and can modify any liability it does have to the assured to take into account any additional premiums, deductible or excess that may have been imposed.

In the event of any breach of the obligations of non-disclosure and accurate representation, the insurer is also entitled to cancel the contract under the Act, subject to anything to the contrary in the contract.

### ***Insurable interest***

The MIA requires an assured to have an insurable interest in the insured property at the time of loss. Although this interest is not required when the contract is concluded, the assured must nonetheless have at that time an expectation of acquiring an insurable interest. Otherwise, the contract is regarded as a gaming or wagering contract and is void.

These requirements were abolished by the ICA in relation to non-marine insurance. It is sufficient for an assured to recover under a non-marine policy if it has suffered a pecuniary or economic loss as a result of loss of or damage to the insured property. Those changes do not appear to have resulted in any difficulty or problems since enactment over 15 years ago.

The requirement for an insurable interest appears to create problems in two sets of circumstances. The first is that assureds that purchase goods on FOB, C&F or CFR terms do not have an insurable and an insured interest in the goods prior to loading aboard a ship (even if they have paid for them before that time) unless that policy includes both a 'lost or not lost' clause and warehouse-to-warehouse cover. Secondly, the assignment of a policy of marine insurance can be ineffective if it is assigned when the assured has already parted with or lost its insurable interest.

However, the insurance industry has strongly advocated the retention of the requirement for an insurable interest as it is said to be an integral part of marine

insurance. The Commission was not convinced that the requirement for an insurable interest is necessary to preserve marine insurers' legitimate rights. Their position is protected by the fundamental principle that an assured can only be indemnified for loss that it has actually suffered and by the requirement that the assured have suffered an economic or pecuniary loss due to the loss of or damage to the insured property. The Commission recommended that the requirement for an insurable interest be abolished.

### ***Subrogation***

The Commission's recommendations propose changes on two topics. Firstly, the MIA is silent on the distribution between the insurer and assured of money recovered from third parties, whether by the insurer pursuing its rights of subrogation or by the assured itself. The common law provides only limited guidance and the ICA, although modifying the common law in relation to non-marine insurance, does not provide a comprehensive regime. The Commission's proposals set out a complete system for the distribution of money received from third parties, though this may be modified by agreement between the parties.

The second area of proposed change is the insertion into the MIA of a new section reflecting the provisions of section 68 of the ICA. This relates to the effect on an insurer's rights of subrogation of contracts entered into by the assured with third parties that limit or exclude the assured's rights of recovery from that third party in the event of loss of or damage to the insured property. Such contracts also limit or exclude the insurer's right to recover from the third party under the insurer's rights of subrogation. Section 68 of the ICA prevents an insurer from relying on a term of the policy that limits its liability to indemnify the assured by reason of the existence of such a third party contract unless that the insurer clearly informed the assured of that term in writing before the contract of marine insurance was concluded. Section 68 also stipulates that the existence of such third party contracts does not have to be disclosed by the assured before the contract of marine insurance is concluded.

### ***Intermediaries***<sup>1161</sup>

The MIA contains several provisions dealing with the role of agents and brokers. Sections 25–26 relate to an agent's obligations of pre-contractual non-disclosure and accurate representation. Section 58 deals with the obligation to issue a policy once premium has been paid or tendered. Sections 59–60 deal with the relationship between the intermediary and the insurer and insured in relation to the payment of

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<sup>1161</sup> *The inclusion of this section dealing with Intermediaries will depend on whether and when the changes recommended by the Commission to the Insurance (Agents and Brokers) Act 1984 (Cth) and the Financial Services Reform Bill 2000 are made.*

money. There is no comprehensive scheme covering the relationship between the intermediaries and the principal parties to the contract.

The ICA contains very little about intermediaries because the subject is covered comprehensively in relation to non-marine insurance in the *Insurance (Agents and Brokers) Act 1984* (Cth) (IABA). The IABA provides a thorough and considered scheme governing the relationship of the various parties whereas the MIA offers a partial scheme only. However, there is some doubt as to the extent to which the IABA also covers marine insurance.

The IABA is to be repealed when the Financial Services Reform Bill (FSRB) becomes law. The FSRB provides for a licensing regime for financial service providers, which will cover all insurance brokers. However, marine insurance is excluded from the operation of the portions of the FSRB which cover other aspects of the relationship between the parties to the insurance contract.

The Commission considered that there is no reason in principle why the regulation of the business of marine insurance in Australia should be different from that of non-marine insurance. Its recommendation was that the IABA or its successor legislation should cover marine insurance as well as non-marine insurance and should be amended accordingly.

#### ***Choice of law and jurisdiction***

The Commission recommended that the MIA be amended to give the Federal Court of Australia jurisdiction in all marine insurance matters, to be exercised concurrently with the courts of the states and territories.

#### ***Policies and contracts***

The Commission made a number of miscellaneous recommendations which deal with the formalities of the contracts and policies of marine insurance and the structure and language of the MIA.

Section 28(1) of the MIA prevents the admission into evidence of any contract of marine insurance unless a policy has been issued in an action for recovery under a policy. The policy is the physical embodiment of, but is distinct from, the contract, which is concluded as soon as the insurer accepts the assured's proposal. The origin of the restriction in section 28 lies in the protection of stamp duty revenue. That purpose no longer being necessary, the Commission recommended that the relevant portion of section 28 be repealed.

For similar reasons, the Commission recommended the repeal of the prohibition in MIA section 31 of time policies for periods over 12 months. This provision was also originally designed to protect stamp duty revenue and is also outdated.

The Commission also recommended changes to MIA section 35 to expand the statutory acceptance of floating policies to include annual and open cover in order to remove any uncertainty about their status as policies within the meaning of the MIA.

A small change to the provisions relating to mutual insurance in MIA section 91 was recommended to bring it more into line with contemporary practice.

The Commission recommended the repeal of the policy wording found in the Second Schedule to the MIA but the retention of the Rules for Construction which form part of it as they provide definitions for some commonly used terms in policies of marine insurance.

### **Financial Impact Statement**

It is not anticipated that this Bill will result in any significant financial impact. Although some of the recommendations involved the repeal of certain sections of the MIA that were originally enacted in order to preserve stamp duty revenue, no such revenue is payable to the Commonwealth and stamp duty on marine insurance policies is no longer payable in any of the states and territories. Accordingly, these amendments have no impact on revenue collected by either the Commonwealth or the states and territories.

### **Regulation Impact Statement<sup>1162</sup>**

The Marine Insurance Act 1909 *both in its original form and as amended by this Bill involves no element of regulation.*

However, the recommendations in the Commission's report involve bringing the regulation of insurance intermediaries in marine insurance into line with the same regulatory scheme as that covering intermediaries in non-marine insurance. That scheme is currently set out in the *Insurance (Agents and Broker) Act 1984*. That Act is, however, due to be repealed when the Financial Services Reform Bill 2000 (FSRB) comes into force. The Commission has recommended that the FSRB be

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<sup>1162</sup> Apart from the first sentence of the Regulation Impact Statement, the wording of the Statement will depend on whether and when the changes recommended by the Commission to the *Insurance (Agents and Brokers) Act 1984* (Cth) and the Financial Services Reform Bill 2000 are made.

amended so that marine insurance is not excluded from it, which is the case at the time that Commission's report was prepared. If that recommendation is adopted, the regulatory scheme contained in the FSRB would apply to marine insurance business in the same way that it applies to non-marine insurance.

The Commission has stated that, in its opinion, there is nothing in the nature or business of marine insurance business (as opposed to the content of marine insurance contracts) that warrants a different regulatory regime from that which governs the rest of the insurance industry.

## NOTES ON CLAUSES

### Clause 1 – Short Title

This is a formal provision that specifies the short title of the Act as the *Marine Insurance Amendment Act 2001*.

### Clause 2 – Commencement<sup>1163</sup>

This clause provides that, with the exception of items 61 and 62 of Schedule 1, the Act will commence on a day to be proclaimed. The timing of the commencement will depend to some extent on the period of time that might be reasonably necessary for the marine insurance industry to accommodate the amendments in its contractual terms and contracting practices.

Items 61 and 62 in Schedule 1 relate to the repeal of sections 59 and 60 of the *Marine Insurance Act*. That repeal takes effect on the same day that the relevant portions of the *Financial Services Reform Act* commence.

### Clause 3 – Application

The amendments to the *Marine Insurance Act* created by this Act should apply to contracts of marine insurance that are concluded or renewed on or after the day on which this Act commences. Pre-existing contracts will continue to be governed by the unamended *Marine Insurance Act*.

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<sup>1163</sup> The wording of these paragraphs will depend on whether and when the changes recommended by the Commission to the *Insurance (Agents and Brokers) Act 1984* (Cth) and the Financial Services Reform Bill 2000 are made.



**Clause 4 – Schedules**

This clause provides that the Acts specified in the two Schedules to this Bill are amended or repealed as set out in those Schedules. Schedule 1 sets out a number of amendments to the *Marine Insurance Act 1909* and Schedule 2 sets out one amendment to the *Insurance Contracts Act 1984*.

**SCHEDULE 1 – AMENDMENT OF THE MARINE INSURANCE ACT 1909**

Item 1 inserts a new section 3A which re-enacts in the body of the MIA the 17 Rules of Construction originally located at the end of the Lloyd’s SG policy wording in Schedule 2 of the MIA. These Rules interpret certain terms commonly found in contracts of marine insurance. Schedule 2 of the MIA is repealed by item 73 of Schedule 1 to this Bill. See also item 32.

Item 2 amends the opening words to section 7 to make it clear that the operation of the MIA to contracts of marine insurance is subject to sections 9A and 9B of the ICA, which provide for certain exceptions to the general rule that marine insurance is covered by the MIA. These exceptions relate to the insurance of pleasure craft and the insurance of non-commercial goods in transit. Section 9B is inserted by Item 1 of Schedule 2 to this Bill.

Item 3 amends subsection 8(1) to add the insurance of risks on inland waters to the scope of the MIA.

Item 4 adds a reference to incidental air risks with the effect that those risks are included within the scope of the MIA.

Item 5 replaces the existing subsection 8(2) with a similar provision that includes insurance relating to ship repairs to the scope of the MIA and removes a reference to policies in the form of marine policies to remove the possibility that the form, rather than the substance, of the contract might determine whether it is governed by the MIA or the ICA.

Item 6 expands any reference in the MIA or in a contract of marine insurance to “the sea” or “seas” to inland waters, consistently with the expansion of the MIA to cover inland waters risks by virtue of item 3 above.

Item 7 repeals section 10 and the prohibition on gaming and wagering contracts and replaces it with a statement that no contract of marine insurance is void simply

because the assured did not have an insurable interest when the contract was entered into. The new section 10 is modelled on section 16 of the ICA.<sup>1164</sup>

Item 8 repeals the definition of “insurable interest” as that concept is abolished by these amendments. A new section 11 is inserted which provides that an insurer is not relieved of liability to indemnify an assured because the assured did not have an insurable interest in the insured property if the assured suffered economic or pecuniary loss as a result of loss of or damage to the insured property. The new section 11 is modelled on section 17 of the ICA.

Item 9 repeals section 12 of the MIA and with it the requirement that the assured have an insurable interest in the insured property at the time of loss.

Item 10 repeals section 13, which relates to insurable interests, as a result of the repeal of section 12.

Item 11 repeals section 14, which relates to insurable interests, as a result of the repeal of sections 10, 11 and 12.

Item 12 repeals section 15, which relates to insurable interests, as a result of the repeal of sections 10, 11 and 12.

Item 13 repeals section 16, which relates to insurable interests, as a result of the repeal of sections 10, 11 and 12.

Item 14 repeals section 17, which relates to insurable interests, as a result of the repeal of sections 10, 11 and 12.

Item 15 repeals section 18, which relates to insurable interests, as a result of the repeal of sections 10, 11 and 12.

Item 16 repeals section 19, which relates to insurable interests, as a result of the repeal of sections 10, 11 and 12.

Item 17 repeals section 20, which relates to insurable interests, as a result of the repeal of sections 10, 11 and 12.

Item 18 repeals section 21, which relates to insurable interests, as a result of the repeal of sections 10, 11 and 12.

Item 19 repeals section 23, which provides that a contract of marine insurance is based upon the utmost good faith, and replaces it with a new section 23 based on

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<sup>1164</sup> If the Commission’s recommendation that the requirement for an insurable interest be abolished is not adopted, items 7 to 18 in Schedule 1 should be replaced by items amending MIA s 16 and inserting a new s 19A as recommended in alternative recommendations 30–31: see fn 1 and 2 in appendix B.

sections 13 and 14 of the ICA. The new section 23 provides that the duty of utmost good faith to be observed by both parties is an implied term of every contract of marine insurance. A party may not rely on a term of a contract of marine insurance if to do so would be not to observe the utmost good faith.

In addition, the new section 23 includes a novel provision that stipulates that the duties of utmost good faith persist throughout the duration of the relationship between the parties governed by the contract of marine insurance with one exception: where a claim or other aspect of the contract becomes the subject of litigation between the parties, the obligations of utmost good faith cease when that litigation is commenced but only in relation to the claim or other aspect that is being litigated.

Item 20 replaces the current obligation of pre-contractual disclosure by the assured in subsection 24(1) with a revised obligation that limits the circumstances that must be disclosed. Under the new subsection, the assured must disclose all circumstances that it knows to be material to the risk to be insured or that a reasonable person in the circumstances would know to be material. The test of what is material is found in subsection 24(2) and is unchanged. The new text is similar to that found in section 21 of the ICA.

The effect of the amendment to subsection 24(1) is that the assured does not have to disclose all circumstances that would influence the mind of a prudent insurer in fixing the premium or determining whether to take the risk, which involves a determination by the assured of what another person would find to be influential. Under the amended subsection, the assured only need disclose those circumstances that it knows to be material or that a reasonable person in its position would know to be material. The test is essentially objective although it remains partly subjective in that the assured must disclose all material circumstances that it actually knows to be material.

This amendment also removes the reference to the insurer's right to avoid the contract if there is a breach by the assured as the insurer's amended remedies are to be dealt with in a new section 26B: see item 24 below.

Item 21 replaces a reference in paragraph 24(3)(d) to warranties to a reference to terms of the contract. This is a consequential amendment that follows from the abolition of the concept of warranties.

Item 22 amends the insurance agent's obligation of disclosure in subsection 25(a) to match that of the assured itself. See item 20 above.

Item 23 removes the reference to the insurer's right to avoid the contract if the assured breaches the prohibition against misrepresentation found in section 26(1)

as the insurer's amended remedies are dealt with in a new section 26B: see item 24 below.

Item 24 inserts four new sections: 26A to 26D.

Section 26A provides that the assured's only duty of pre-contractual disclosure is that provided by section 24 of the MIA and that a contract of marine insurance may not impose any greater duty in this regard. Subsection 26A(2) permits a contract of marine insurance to include an express term providing for an assured's post-contractual duty of disclosure.

Section 26B sets out the structured remedies available to the insurer if the assured breaches its obligations relating to pre-contractual disclosure and representation.

- If the breach is fraudulent the insurer may avoid the contract from its outset and retain the premium (which is the present position).
  - If the breach is not fraudulent, the remedies depend on whether the insurer was induced to enter into the contract by the breach.
  - If the insurer proves that it would not have entered into the contract, it may avoid the policy from the outset but must return the premium. If the insurer proves that it would have entered into the contract but on different terms, the insurer is not entitled to avoid the contract. However, the insurer is not liable to indemnify the assured in relation to any loss that is proximately caused by the circumstance that was the subject of the non-disclosure or misrepresentation; it may reduce any liability it does have to the assured to reflect any additional premium, deductible or excess that would have been imposed; and it may avail itself of the new statutory right of cancellation. See item 49 below.
- (i) Section 26B states that the insurer bears the onus of proving that it was induced to enter into the contract by the assured's breach.
- (i) Section 26C prevents a contract of marine insurance from providing remedies for an assured's breach of its obligations relating to pre-contractual disclosure and representation that are more favourable to the insurer than those provided for by the Act.
- (j)
- (k) Section 26D clarifies the position concerning the inducement of following insurers. A following insurer enters into a contract of marine insurance solely because one or more other insurers (called "leading insurers") have already done so and does not make any independent assessment of the risk. It is the previous acceptance of the risk by the leading insurers that induces the

following insurer to accept part of the risk. There is some doubt as to whether a following insurer could ever be said to have been induced to enter into such a contract by a breach by the assured of its obligations relating to pre-contractual disclosure and representation. Section 26D provides that a following insurer is deemed to have been induced to enter into the contract by the assured's breach if all the leading insurers were so induced.

Item 25 repeals the provision which renders inadmissible in court any contract in an action for recovery of a loss under the contract unless the policy has been issued. This was originally intended to protect stamp duty revenue. As no stamp duty is payable on any marine insurance policy in any state or territory, this provision is now outdated and unnecessarily restrictive. The amendment also restates the insurer's obligation to issue the policy although, under section 58, this does not have to be done until the premium has been paid or tendered.

Item 26 provides that a policy document that does not comply with all the formal requirements set out in subsection 29(1) is not invalid for that reason alone.

Item 27 repeals subsection 31(2), which prohibits time policies for periods over 12 months. This outdated provision was also originally intended to protect stamp duty revenue.

Item 28 amends subsection 35(1) and the heading to section 35 to ensure that open and annual cover are recognised as policies within the meaning of the Act to remove uncertainty about their status.

Item 29 expands subsection 35(1) to cover policies over insurable property as well as ships.

Item 30 amends subsection 35(3) to make it clear that the opening clause of that subsection also applies to the first clause in the second sentence. See also item 31 below.

Item 31 amends subsection 35(3) to make it clear that the opening clause of that subsection also applies to the first clause in the second sentence but not the second clause of that sentence. See also item 30 above.

Item 32 repeals section 36, which refers to the wording of the Lloyd's SG policy found in the Second Schedule to the Act. That Schedule is repealed by item 73 below although the Rules for Construction are re-enacted as section 3A by item 1 above.

Item 33 amends the heading to Division 7 of Part II of the MIA to reflect the abolition of the concept of warranties and their replacement by express terms of the contract.

Item 34 replaces section 39 and the definition of warranties with a new section 39. The new section provides that, subject to the Act itself, no term in a contract of marine insurance is a warranty or has the effect that an insurer is discharged from all liability under the contract if the assured breaches that term. However, an express term of the contract may state that the insurer is discharged from liability to indemnify the assured for any loss proximately caused by the assured's breach of an express term.

Subsection 39(3) specifies that the insurer bears the onus of proving that there was a breach of an express term and that the assured bears the onus of proving that any such breach did not proximately cause the loss for which it seeks indemnity under the policy. This is stated to be without prejudice to any other burden of proof provided for by statute or common law. For example, the insured bears the onus of showing that the loss for which it claims indemnity was caused by an insured peril, and the common law sets out the shifting onus of proof in cases where unseaworthiness is in issue.<sup>1165</sup> Subsection 39(3) as amended does not seek to disturb these principles.

Item 35 amends subsection 40(1) to remove all references to warranties and replace them with references to terms of the contract.

Item 36 repeals subsection 40(2), which prevents an assured from remedying a breach of warranty before loss.

Item 37 amends subsection 40(3) to replace a reference to a warranty to a reference to a term of the contract of marine insurance.

Item 38 repeals section 41, which deals with express warranties.

Item 39 repeals section 42, which deals with warranties of neutrality.

Item 40 repeals section 43, which deals with warranties of nationality.

Item 41 repeals section 44, which deals with warranties of good safety.

Item 42 replaces section 45(1) and in doing so removes the implied warranty of seaworthiness in voyage policies and states that there is no implied warranty of seaworthiness in any contract of marine insurance.

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<sup>1165</sup> See *Skandia Insurance Co Ltd v Skoljarev* (1979) 142 CLR 375.

Item 43 replaces subsection 45(2), which deals with an aspect of the implied warranty of seaworthiness, and replaces it with a provision that permits a contract of marine insurance to include an express term relating to the seaworthiness of a ship. Under this provision, an insurer may be discharged from liability to indemnify an assured for loss attributable to a breach of such a term if the assured knew or ought to have known of the facts that rendered the ship unseaworthy, that they rendered the ship unseaworthy, and if the assured failed to take any steps that were reasonably available to it to make the ship seaworthy.

Item 44 replaces subsection 45(3), which deals with an aspect of the implied warranty of seaworthiness, and replaces it with a provision that prevents a contract of marine insurance from containing a provision relating to the seaworthiness of ship that is more favourable to the insurer than provided for by section 45 as amended.

Item 45 repeals subsection 45(5), which provided for certain circumstances in which an insurer was not liable for any loss attributable to unseaworthiness under a time policy.

Item 46 amends subsection 46(1) to provide that there is no implied warranty in a contract of marine insurance that goods or other movables are seaworthy.

Item 47 repeals subsection 46(2), which provided for an implied warranty of seaworthiness of a ship in policies covering goods or other movables.

Item 48 replaces the implied warranty of legality in section 47 with new provisions. These new provisions:

- remove the concept of a warranty of legality;
- permit a contract of marine insurance to include an express term that, to the extent that the assured can control the matter, the insured voyage will have a lawful purpose, in breach of which the insurer is discharged from all liability under the contract and may retain the premium;
- permit a contract of marine insurance to include an express term that, to the extent that the assured can control the matter, the insured voyage will be carried out in a lawful manner, in breach of which the insurer is discharged from all liability to indemnify the assured for any loss attributable to the breach;
- prevent a contract of marine insurance from containing a term relating to the lawful purpose and manner of the insured adventure that is more favourable to the insurer than those set out in section 47 as amended.

Item 49 inserts a new section 47A that sets out the insurer's statutory rights of cancellation in the event of breach of the contract or a fraudulent claim by the assured. Section 47A is modelled on sections 59 and 60 of the ICA. The right to cancel under section 47A is also expressly granted by section 26B (see item 24 above).

Item 50 repeals section 48, which provides for an implied condition about the commencement of the risk. The matters covered by section 48 and 51–55 (which are repealed by items 51–55 below) can be dealt with by express terms of the contract.

Item 51 repeals section 51, which relates to the insurer's remedies if there is a change of voyage.

Item 52 repeals section 52, which relates to the insurer's remedies for deviation.

Item 53 repeals section 53, which also relates to deviation.

Item 54 repeals section 54, which relates to delay.

Item 55 repeals section 55, which sets out seven excuses for deviation and delay.

Item 56 amends the heading to Part III of the MIA, which relates to the assignment of the policy or contract.

Item 57 expands subsection 56(1) to cover the assignment of contracts as well as policies of marine insurance.

Item 58 expands subsection 56(2) to cover the assignment of contracts as well as policies of marine insurance.

Item 59 expands subsection 56(3) to cover the assignment of contracts as well as policies of marine insurance.

Item 60 repeals section 57 as a consequence of the repeal of the requirement for an insurable interest in items 8 and 9 above.

Item 61 repeals section 59. This repeal takes effect when the changes to the *Insurance (Agents and Brokers) Act 1984* (Cth) or the Financial Services Reform Bill 2000 recommended by the Commission take effect.<sup>1166</sup>

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<sup>1166</sup> The wording of this item will depend on how and when the *Insurance (Agents and Brokers) Act 1984* or the Financial Services Reform Bill 2000 is amended.



Item 62 repeals section 60. This repeal takes effect when the changes to the *Insurance (Agents and Brokers) Act 1984* (Cth) or the Financial Services Reform Bill 2000 recommended by the Commission take effect.<sup>1167</sup>

Item 63 amends subsection 82(1) and the heading section 82 to changes all references to warranties to references to express terms of the contract.

Item 64 amends subsection 82(2) to changes all references to warranties to references to express terms of the contract.

Item 65 amends subsection 82(3) to changes all references to warranties to references to express terms of the contract.

Item 66 amends subsection 82(4) to changes all references to warranties to references to express terms of the contract.

Item 67 inserts a new section 85A modelled on section 68 of the ICA. This section prevents an insurer relying on term of a contract of marine insurance which limits its liability to indemnify the assured on the basis that an agreement between the assured and a third party limits the insurer's rights of subrogation unless that assured was clearly informed in writing of that term before the contract of marine insurance was concluded.

Subsection 85A(2) provides that the assured does not have to disclose the existence of any such agreement with a third party before the contract of marine insurance is concluded.

Item 68 inserts a new section 87A that sets out a comprehensive regime specifying how money recovered from a third party is to be distributed between insurer and assured.

Item 69 repeals paragraph 90(3)(c) as a consequence of the repeal of the requirement for an insurable interest by items 8 and 9 above.

Item 70 repeals paragraph 90(3)(d) as a consequence of the repeal of the requirement for an insurable interest by items 8 and 9 above.

Item 71 amends the definition of mutual insurance in subsection 91(1) to insert a reference to an association formed by two or more persons to provide mutual insurance.

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<sup>1167</sup> The wording of this item will depend on how and when the *Insurance (Agents and Brokers) Act 1984* or the Financial Services Reform Bill 2000 is amended.

Item 72 inserts a new section 96 to give the Federal Court of Australia jurisdiction over all matters arising under or relating to any contract of marine insurance to be exercised concurrently with the courts of the states and territories.

Item 73 repeals Schedule 2 of the MIA, which contains the wording of the Lloyd's SG policy. The 17 Rules for Construction found at the end of the Schedule have been re-enacted in the body of the MIA in a new section 3A by item I of Schedule 1 of this Bill. See also item 32.

#### **SCHEDULE 2 – AMENDMENT OF THE *INSURANCE CONTRACTS ACT 1984***

Item 1 inserts a new section 9B into the *Insurance Contracts Act 1984* which provides that contracts for the transportation of goods other than goods being transported for the purposes of a business, trade, profession or occupation carried on or engaged in by the assured (that is, non-commercial goods) are not covered by the *Marine Insurance Act 1909* but, as a result, by the *Insurance Contracts Act* itself.

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