Neutral Citation Number: [2008] EWCA Civ 1231

Case No: A3/2007/2741(B), A3/2007/2741(Z) & A3/2007/2741

IN THE SUPREME COURT OF JUDICATURE
COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM HIGH COURT OF JUSTICE
QUEEN'S BENCH DIVISION
COMMERCIAL COURT
JONATHAN HIRST QC (SITTING AS A DEPUTY HIGH COURT JUDGE)
2005FOLIO614

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 12th November 2008

Before :

THE RIGHT HONOURABLE LORD JUSTICE WARD
THE RIGHT HONOURABLE LORD JUSTICE LONGMORE
and
THE RIGHT HONOURABLE LORD JUSTICE JACKSON

- -

Between :

LIMIT NO. 2 LIMITED	**Appellant**
- and -	
AXA VERSICHERUNG AG.	**Respondent**

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Mr Gavin Kealey QC & Mr Peter MacDonald-Eggers (instructed by **Clyde & Co**) for the **Appellant**

Mr Nicholas Hamblen QC & Mr Charles Kimmins (instructed by **Kennedys**) for the **Respondent**

Hearing dates : 13th & 14th October 2008

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Judgment

Lord Justice Longmore:

Introduction

1. This is a salutary tale about two fac/oblig treaties of reinsurance, relating to construction and operating risks in connection with oil rigs. The first treaty was written for initially twelve months from 1st July 1996 and then extended (by an endorsement of 20th June 1997) for a further 7 months to 31st January 1998; the second treaty was written for twelve months thereafter up to 31st January 1999. The reassured were syndicates at Lloyd's, the reinsurers a German company, Albingia, now taken over by the Axa group. I shall refer to them as "the syndicates" and "reinsurers" respectively.

2. The deputy judge has held that reinsurers were entitled to avoid these treaties because the syndicates' brokers, Newman Martin and Buchan Ltd ("NMB") attached a front cover to the draft slip and information sheet provided by the syndicates for the purpose of placing the reinsurances. On 4th July 1996 NMB faxed a bundle of 43 pages (including that front cover) to reinsurers. On that front cover sheet NMB, referring to the syndicates, said:-

> "As a matter of principle they maintain high standards and would not normally write construction unless the original deductible were at least £500,000 and preferably £1,000,000."

3. The treaties turned out badly for reinsurers who in 2005 procured a Mr Jim Hunt to conduct an inspection of the relevant records of risks which were ceded to the treaties. He found that most of the relevant risks ceded by the syndicates had deductibles considerably lower than £500,000 (let alone £1,000,000). It is to be noted that the treaties themselves contained no clause requiring the ceded risks to have any particular deductible. Nevertheless reinsurers sought to avoid the treaties by asserting that the brokers' statement in the previous paragraph was a representation

   i) that the syndicates had, on 4th July 1996 (the date of NMB's fax) and earlier, a practice of writing risks with the stated deductibles; or

   ii) that the syndicates had, on 4th July 1996, the intention that they would, in the future, write risks with the stated deductibles; or

   iii) that this practice (or their intention) as at 1st July 1996 could be relied upon as an indication or guide to their future underwriting practice.

   (This is my attempt to paraphrase the allegations contained in para. 12 and 13 of the re-re-amended defence of reinsurers in the action). It was then said that one or more of these representations was false, was material to the risk, was intended to be acted upon, and induced reinsurers to write the treaties, with the result that the treaties could be avoided.

4. There are two reasons why these allegations of representation have been made in what may be thought to be a somewhat artificial way. The first is that for a representation to have legal effect, it must be a representation of existing fact not of future fact or opinion; see Chitty, Contracts 29th ed vol 1 para. 6-004 for the general law.

Reinsurers' own solicitors may not have completely understood this basic point since, in their letter of avoidance of 19th August 2005, they asserted that the syndicates had misrepresented that the risks "would have" substantial deductibles, on the face of it a representation that something would happen in the future. Secondly, it is axiomatic in the law of insurance that no representation as to expectation or belief is actionable if it is made in good faith. This common law rule has been codified for the purposes of contracts of marine insurance (which presumably these treaties are) by section 20(5) of the Marine Insurance Act 1906:-

> "A representation as to a matter of expectation and belief is true if it be made in good faith."

No suggestion of bad faith has been made in this case.

5. The deputy judge found (para. 46) that the single sentence relied on as a representation

> "was a statement of the syndicates' current policy as regards deductibles."

By current policy I understand him to mean the syndicates' policy as at 4th July 1996. He held, secondly (para. 48):-

> "In July 1996, it was not the syndicates' policy normally to write construction risks unless the deductible was at least £500,000 and preferably at least £1,000,000."

There was accordingly a misrepresentation. He held thirdly that the syndicates had acted in good faith throughout since their underwriter, Mr O'Farrell, had not seen the brokers' fax cover sheet with its reference to deductibles. He held next (para. 53) that the misrepresentation was material. He then held (para. 61) that it had induced the 1996 Treaty which could accordingly be avoided (para. 62). The endorsement extending the treaty could likewise be avoided either because it was a mere extension (or amendment) to the treaty or because the representation continued to be effective as at July 1997. The representation continued also to be effective as at 1st February 1998 and the second treaty could, therefore, also be avoided. The syndicates now appeal.

6. There are 4 surviving grounds of appeal put forward by Mr Gavin Kealey QC (who did not appear before the deputy judge) for reinsurers:-

i) That, although the reinsurers' pleaded defence asserted a representation of both the syndicates' "current practice" and their "intention", the trial had focused, correctly, on their intention. The deputy judge's decision that NMB's fax was a statement of the syndicates' "current policy" reverted back to the allegation of "current practice", which had never been investigated at the trial since no disclosure of the syndicates' underwriting before 4th July 1996 had been requested. Had it ever been requested, it would have emerged that the practice of the syndicates as at 4th July 1996 was indeed to write business with the stated deductibles. The judge's second conclusion that it was not the syndicates' "policy" in July 1996 to write with the stated deductibles had therefore been reached on an unfair basis and was in fact wrong. Judgment in

favour of reinsurers could not stand and should be entered for the syndicates; alternatively the case should be remitted to the judge for him to determine what the syndicates' policy was in July 1996 after proper discovery and evidence. I shall call this "the unfairness ground";

ii) That, even if NMB's fax did constitute a statement of the syndicates' intention in July 1996 to write business with the stated deductibles, it was no more than a statement of expectation or belief; moreover it was a statement of expectation or belief made by NMB as brokers, not even a statement by the syndicates themselves;

iii) That the judge was wrong to hold that the 1997 endorsement only amended or extended the 1996 contract for seven months; it was a separate contract; and the same arguments applied to it as to the 1998 treaty;

iv) That the judge was wrong to hold that (both in June 1997 and in January 1998) the representations as to the syndicates' "current policy" in July 1996 were continuing representations or that there was any obligation on the syndicates to disclose that their "policy" had changed.

The Unfairness Ground

7. In the light of the way that the syndicates' argument has been developed in their grounds of appeal and in this court, it is perhaps a little unfortunate that the deputy judge used the phrase "current policy" in para. 46 of his judgment, rather than the words "practice" or "intention" as used in the pleading. The words "practice" and "intention" are precise words, the first relating to what was actually happening in relation to the writing of risks in July 1996 and perhaps earlier and the second relating to what the syndicates intended to do in the future. The word "policy" can in general import elements of both the present and the future and thus carries with it an element of ambiguity. The phrase "current policy" could be said not merely to emphasize that ambiguity but even to put greater stress on the present rather than the future.

8. The judge cannot, however, be blamed for this because it was Mr Hamblen QC, who was then (as now) appearing for the syndicates, who introduced the word "policy" into the legal arena when he was making submissions after the conclusion of the evidence. He was making a submission (Day 6, pages 76-7) as to how the reinsurers' underwriter, Mr Holzapfel, understood the representation:-

> "as being a statement of the underwriter's policy, philosophy if you like, of underwriting as part of their [maintaining high] standards ….

JUDGE Is there any difference between policy and intention. I don't think there is there?

MR HAMBLEN Not really my Lord, it's just a way of labelling it really but I suppose it does carry with it implications of being on-going."

To be fair to Mr Hamblen, the word "philosophy" may not have sprung unprompted into his mind. That word had already been used by the reinsurers' expert, Mr

Compton-Rickett in para. 12 of his report, in which he described the statement about the syndicates' deductibles as their "philosophy". But the actual word "policy" does appear to have originated with Mr Hamblen, although then espoused by the deputy judge.

9. My own view is that "intention" is at least an important element of the concept of "policy". It does seem to be correct, as the syndicates submit, that the pleaded concept of their "practice" as to deductibles played little (if any) part in the trial. Certainly no relevant disclosure was requested or given. In those circumstances, there could have been no doubt in the minds of those participating in the trial that the word "policy", if not actually synonymous with "intention", at least included intention as a major element. This is confirmed by the deputy judge's description of Mr Hamblen's first argument about the representation relied on by reinsurers:-

> "Mr Nicholas Hamblen QC submitted on behalf of Albingia that, by their fax cover sheet dated 4th July 1996, NMB represented on behalf of the syndicates that the syndicates intended to stick to their stated principle of maintaining high standards and writing construction risks of which the great majority would have deductibles of at least £500,000. These words were "designed to encourage the recipient to participate in the reinsurance" (cf. Saville LJ in Hill v Citadel Insurance Co Ltd (CA) [1997] Lloyds Rep. IR 167,170 col.2) and, whilst they must be read in the context of the other placing information, there was nothing to qualify what was said in the fax. On the contrary, the statement about deductibles appeared on the front page of the presentation. The words spoke for themselves, and the phrase looked to the future, as well as the present and the past. A statement of current intention or policy was a statement of fact, and is not one of expectation or belief."

The last sentence, in particular, shows that "intention" and "policy" are for the judge synonymous concepts. The concept of the syndicates' "practice" only surfaces in the deputy judge's description of Mr Hamblen's second argument, now the subject of a respondent's notice.

10. It is true that when the deputy judge comes to the point of decision he cites the statement of Moore-Bick J, as he then was, in Kingscroft v Nissan [1999] Lloyds Rep. IRLR 603, 627, that a statement of present intention amounts to a statement of fact and adds

> "I think that is even more so as regards a statement of policy."

As a dictum that is not altogether easy to follow since any given statement either is (or contains) a statement of fact or it does not. A statement of policy is not, to my mind, more obviously factual than a statement of intention. But, in the light of the earlier paragraph, I do not believe the deputy judge had changed the meaning he was attributing to the word "policy" now to mean the word "practice".

11. When the deputy judge came to consider falsity he said this:-

> "In July 1996, it was not the syndicates' policy normally to write construction risks unless the original deductible was at least £500,000 … In the past, the syndicates had managed to maintain the policy, but by July 1996, the prevailing market conditions were such that these deductibles could not be achieved. This is borne out by the syndicates' actual underwriting of construction risks."

Here the judge is expressly drawing a distinction between the past and the future in assessing the policy (and thus the intention) of the syndicates in July 1996. There was a practice in the past whereby the policy had been maintained up to July 1996 but "by that date" the stated deductibles "could not be achieved" (as shown by the risks actually written and ceded to the treaties). So the syndicates' erstwhile policy not only could not be achieved but no longer existed at the time when the treaties were written. On a fair construction of his judgment, the judge was not saying (inappropriately) that there was a representation as to the syndicates' practice relating to deductibles which was a misrepresentation because no such practice existed. Rather, he was saying (appropriately) that the policy (or intention) to write with the stated deductibles had been maintained before July 1996 but by July 1996 had evaporated.

12. In these circumstances, the unfairness for which syndicates contend, does not arise. The judge made no incorrect findings about the syndicates' pre-July 1996 practice; indeed he said, correctly as it turns out, that the policy and, therefore, the practice was maintained. What did not exist was the intention to continue that practice.

13. Mr Kealey then submitted that was an unfair conclusion in the light of the actual evidence given by the syndicates' underwriter Mr O'Farrell. What the evidence showed, said Mr Kealey, was that Mr O'Farrell did intend to write business with the stated deductibles, if he could, although he recognised that in the prevailing market conditions he was unlikely to achieve it. If this is the right interpretation of Mr O'Farrell's evidence, he would win a high price in any competition for the display of casuistry. The judge, however, described his evidence as "frank" and I agree.

14. It is true that when, at a comparatively early stage Mr Hamblen put to Mr O'Farrell that he was not intending to insist on the stated deductibles which he had had in the past, he did say it was not fair to say he did not intend to insist on them and he added

> "It would always be the idea to get as high deductibles as possible but recognising fully at any moment in time what the market place is doing." Day 1, pages 75-76

He recognised, however, that the market would get more and more difficult so when it was put to him that he could not have a plan to insist on substantial deductibles he said that that was a reasonable assumption to make. There was then this question and answer.

> "Q … It wasn't your plan or intention to insist on substantial original deductibles going forwards, was it, in July 1996?

A … I think that's a fair observation but I was trying to underwrite in the market." (Page 77)

15. That might have sufficed for Mr Hamblen's purposes but be persisted as follows (at page 79):-

"MR HAMBLEN: So that had been – in the past you'd managed to command deductibles at those levels, correct?

A. Correct.

Q. But in the prevailing market conditions in July 1996, you appreciated that you couldn't expect to command those deductibles going forwards?

A. Correct.

Q. And your opinion at the time was one that could not be maintained in the prevailing market conditions?

A. Correct.

Q. So you didn't expect that practice to be maintained going forwards?

A. Correct.

Q. And as far as you saw it, in the light of the market conditions, there was going to be no point in sticking to your previous practice of insisting on significant deductibles; correct?

A. As I say, the marketplace was changing and I operate in the marketplace and I need to work within the confines of the market.

Q. And since, as you saw it, there would be no point in sticking to that practice, it wasn't your intention to do so?

A. Correct."

16. A fair reading of this evidence as a whole leads to the inexorable conclusion that Mr O'Farrell did not intend in July 1996 that his future writing would be on terms that there would be deductibles of at least £500,000. He was, moreover, at pains to say that he had never said that was his intention – it was only the brokers who had said that. But on the inevitable basis that any representation made by the brokers is made on their client's behalf, the syndicates cannot disavow it and the judge was, in my view, entitled to come to the conclusion that the syndicates had no policy (or intention) normally to write construction risks with the stated deductible. There being no appeal in relation to materiality or inducement that has to be the end of the matter in relation to the 1996 treaty, subject to the second ground of appeal.

Statement of opinion or expectation?

17. Once it has been decided that the fax cover sheet did contain a representation that the syndicates intended to write construction business with the stated deductibles, this ground is not seriously arguable. It is not a statement of opinion or belief; nor is it framed as a statement of expectation. The words "would not normally write construction unless …." mean that the syndicates will normally write (namely intend normally to write) with the stated deductibles. That statement of intention is a representation of existing fact. The judge cited Moore-Bick J in Kingscroft as well as the old case of Traill v Baning. One might add the famous dictum of Bowen LJ in Edgington v Fitzmaurice (1885) 29 Ch. D. 459, 483:-

> "The state of a man's mind is as much a fact as the state of his digestion."

18. The fact that the statement was made by the brokers who might be said not to have personal knowledge of Mr O'Farrell's intent and could, therefore, have no more than an expectation of what Mr O'Farrell would do in the future is nothing to the point. The brokers were the agents of the syndicates to present the risk; it is unfortunate that Mr O'Farrell had no idea that the brokers had added a fax cover sheet to his own summary of relevant information and would, according to the judge, have corrected it if he had known about it. But it is a statement that has, in law, to be attributed to the syndicates and, so attributed, it amounts to a statement by the syndicates of their intention, not merely a brokers' statement of what the syndicates might be expected to do in the future.

The Respondent's Notice

19. Reinsurers argued that, if the judge had decided that the representation related to the syndicates' existing practice in July 1996 rather than their intention, he should have found further that the fax did state their intention. Alternatively the judge should have accepted reinsurers' second argument (recorded in para. 30 of the judgment) that the syndicates' previous or current practice of writing risks with the stated deductibles could be relied upon as an indication of their future practice. (It is here that the concept of previous or current "practice" becomes important). In the light of my conclusions so far it is unnecessary to consider these arguments; it may be, as Mr Kealey submitted, that the alternative suggested representation would be a statement of expectation or belief. The judge did not accept this second argument because it was, he said, an over-elaborate reading of what was said in the fax cover sheet. If it were important, I would agree with the deputy judge in relation to this second argument. But none of these matters needs to be decided and I refrain from saying anything more.

The 1997 Endorsement – amendment or new contract?

20. This again is a short point. The endorsement records the agreement between the parties that the period clause is "amended" to read as follows:-

> "PERIOD: Losses occurring on risks attaching during the period nineteen months effective 1st July 1996 or as original …."

This is the language of amendment by the substitution of the word "nineteen" for the word "twelve". It would be artificial to regard it as a new contract. No doubt, as Mr Kealey submitted, a fresh duty of good faith arose in June 1997 prior to the agreement for an extension to 19 months in relation to any matter relevant to the extension and, if there was a breach of the good faith obligation in relation to the amendment, the amendment would be avoidable without the whole contract being avoided. But it does not at all follow that the extension is a new contract rather than an amendment or variation of the existing contract. That question can only be answered by construing the endorsement and, in my judgment, it operates as an amendment to an existing contract not a new contract. It must follow that the next question is whether the contract as amended is voidable for misrepresentation and, on my conclusions so far, it is.

The 1998 renewal

21. On any view this was a new contract. There were new obligations of good faith and the question does therefore arise whether the representation made by the brokers in July 1996 continued to be effective in 1998. There is also the question whether there was any obligation on the syndicates to disclose that their policy (or intention) as to deductibles had changed.

Continuing representation?

22. The deputy judge relying on the fact that, before the 1998 renewal was written, NMB explained the failure of the 1996 treaty to achieve its estimated premium income by reference to the syndicates' refusal to write other then quality business and relying also on Traill v Baring (1864) 4 De G J & S 318, The Moonacre [1992] 2 Lloyd's Rep 501 and Hill v Citadel [1997] Lloyd's Rep IR 167, decided that reinsurers were entitled to assume that the syndicates' "policy" (para. 81) or "practice" (para. 84) as to deductibles was being maintained. The assimilation of "policy" and "practice" in these paragraphs is, I think, unfortunate. It was the "policy" (in the sense of "intention") that the deputy judge had held to be the critical part of the representation which he found (and I would uphold). The question is therefore whether the syndicates' representation of their intention was a continuing one.

23. I have already said that a representation of intention may be thought to be a somewhat artificial concept at the best of times. It is also a somewhat elusive one because a person's intentions are always subject to change. In Traill v Baring the reinsured said he intended to retain one-third of the risk but changed his mind before the risk incepted. Any statement of intention would, of course, be intended to be operative when the risk began and would continue up to that time. It does not follow it would be operative on renewal. The Moonacre was not a representation of intention at all but a case of non-disclosure of the fact that a proposer's signature on the proposal form was forged. Not surprisingly the failure to disclose the forgery was held to be as operative on renewal as on the original insurance. But the dishonest fact of forgery is very different from an honest but wrong statement of intention made 19 months before renewal takes place.

24. The relevant representation in Hill v Citadel related to the costs of excess loss protection which was said to have amounted in recent years to about 20% of premium income. It was then said that that past practice was represented as being an accurate

guide to future practice. There was then further placing information on renewal which then stated that excess loss protection had been placed at a very reasonable cost ratio. This was a virtual repetition on renewal of the information given before inception. The deputy judge thought that that was very similar to the present case.

25. I cannot agree. The explanation of the low premium income on the 1996 treaty, as being referable to the syndicates' underwriter, Mr Copping, only writing quality business, is not a repetition of policy about deductibles; the question must remain whether the representation of intention made in July 1996 continued to be operative nineteen months later in February 1998. To my mind it puts altogether too much weight on a representation of intention relating to deductibles to say that it must be taken to be still operative after a lapse of 19 months. The fact that the deputy judge had chosen to call the syndicates' intention a "policy" does not make any difference to this conclusion.

26. Mr Kealey relied on a dictum of Sir Nicholas Browne-Wilkinson V-C in Tudor Grange Holdings v Citibank [1992] Ch. 53, 67 in relation to an alleged representation of intention on the part of Citibank:-

> "The representation is that Citibank would provide long term finance for all the products in the Tudor Grange Group business plan. That is either a representation as to future conduct or a representation as to the then intention of Citibank. A representation as to future conduct has no effect unless it constitutes a contract. Therefore the only legally effective representation is a representation of existing fact, namely that at the date of the representation it was the intention of Citibank to provide the finance. In those circumstances I find it difficult to see how allegation of a continuing representation to that effect is of any avail. The continuing representation would be that it was Citibank's intention back in 1988, a matter of irrelevance in 1989."

It is true that the Vice-Chancellor proceeded to strike the claim out on the facts of the case on the basis that he would assume in favour of the claimants that the representation did, in fact, continue in 1989 but it is clear that he had great difficulty in relation to the continuity of the representation. A representation of intention cannot last for ever; it only relates to the time when it is made; there must come a time when it is spent and, to my mind, that is well before the passage of 19 months. It may be said that a statement of intention to provide finance is less long-lasting than a statement of "intention" to write business with a stated deductible, but to distinguish Tudor Grange in that way would be to give the statement of intention in the present case an element of firmness and futurity it could never have been meant to have, given the fact that market conditions changed and anyway cannot be expected to be stable over a long period. As the Vice-Chancellor said a statement of intention made in 1988 is irrelevant in 1989; whatever the syndicates' intention as to deductibles was in July 1996 had become irrelevant by February 1998 and no statement as the syndicates' 1998 intention was ever made.

27. It must also be remembered how powerful the remedy of avoidance is in the hands of an insurer or reinsurer. The entirety of a contract can be avoided for a wholly

innocent misrepresentation provided it is material to the risk in the eyes of a prudent underwriter. If the contract is for 12 months (or, as here, 19 months) that is a very stark remedy. I do not, for my part, consider that a court should struggle to hold that everything said at inception is to be impliedly repeated on renewal. In this context the following dictum of Ferris J in WPP Group Plc v Reichmann, 23rd August 2000 is apposite:-

> "The representation which is to be implied from the statement that "I will let you know if anyone else is interested" is, in my judgment, of an entirely different nature [from a representation that a business has been honestly conducted]. Granted that, as I accept, it implies that "There is at this moment no one else interested" it is essentially a statement of the position which exists at the time the statement is made. It may not have been true in the past and it imports no warranty (other than in the form of an unenforceable non-contractual promise) that it will remain so in the future. There is, in my judgment, a complete artificiality about an argument which starts with a statement which appears to amount to a promise, accepts that such promise has no contractual effect, proceeds to extract an implied statement of fact out of the promise, treats that as a statement that, unless corrected, the fact continues to exist, and concludes by stating that the legal effect is substantially the same as if the promise had been enforceable in the first place."

28. Then it is said that the syndicates should have disclosed that their intention had changed but this is just to repeat the same argument in a different form. If, as Lord Lloyd said in Pan Atlantic v Pine Top [1995] 1 AC 501, 554-5 (a passage recited by the deputy judge) misrepresentation was there the converse of non-disclosure, so here the suggested non-disclosure is but the converse of the suggested misrepresentation. It might be different if it were suggested that it was generally material to disclose the level of deductibles intended to be written but that has never been suggested. The case has always been put on the basis of a misrepresentation of intention or non-disclosure of a change of intention, not on the basis of any "general duty to disclose" the level of deductibles, see para. 86 of the deputy judge's judgment.

Conclusion

29. I would therefore uphold the deputy judge's judgment in relation to the 1996 year and the 1997 endorsement but set his order aside so far as the 1998 year is concerned. Since the deputy judge was unable to reach a final conclusion in relation to the 1998 year if he was wrong on the points he decided, this litigation may not yet be finished. But I trust that counsel will be able to draw up the appropriate order, if Ward LJ and Jackson LJ agree with this judgment.

Lord Justice Jackson:

30. I agree.

Lord Justice Ward:

31. I also agree.