

Assignment 1:
Marine Insurance

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Discussion of the CMI Guidelines for the
Formulation of Marine Insurance Law
Dealing with
Good Faith, Disclosure, Alteration of Risk and Essential Terms

<u>1. Introduction</u>	Pg.1
<u>2. 'Contracts of Good Faith'</u>	Pg. 2
<u>3. 'Each Party'</u>	Pg.3
<u>4. 'At All Times During the Contract'</u>	Pg.4
<u>5. Materiality</u>	Pg.6
5.1 'Objective Norms'	Pg.9
5.2 'Causative Link'	Pg.10
<u>6. Remedies</u>	Pg.11
6.1. 'Treat the Contract as at an End'	Pg.12
6.2. Damages	Pg.13
7. Conclusion	Pg.14

1. Introduction

The CMI guidelines which are discussed in this paper, deals mainly with the Doctrine of Good Faith in marine insurance contracts. This doctrine has in recent years been the subject of much controversy and is progressively causing more inequity amongst insurer and assured.¹ Due to its harsh effect in voiding the contract *ab initio*, it has even been described as a ‘draconian remedy’.² Furthermore the doctrine, which originated in Britain as the doctrine of *uberrimae fidei* or the duty of utmost good faith, is applied differently in maritime jurisdictions across the world.³

In drafting these guidelines the CMI is attempting to negate the negative effects of this doctrine, while fostering a more uniform approach to it. This paper seeks to analyse these guidelines in order to ascertain to what extent they differ from or conform to current law and how they might become applicable in the future. South African and English law on these matters will, specifically, be taken into account.

2. ‘Contracts of Good Faith’

Guideline 1 states that ‘Marine insurance contracts are contracts of good faith.’ The notion of good faith in marine insurance contracts was first established in English Law by the celebrated case of *Carter v Boehm*.⁴ By the time Sir MacKenzie Chalmers drafted the British Marine Insurance Act (MIA) in 1906, it was already accepted in English common law that the standard applicable to this notion was that of ‘Utmost Good Faith’. This principle found expression in ss17-20 of this act and specifically states that “A contract of marine insurance is a contract based on the utmost good faith...”⁵

Good faith has been recognised by many Anglo-American as well as civil law countries as a requirement for marine insurance contracts.⁶ Although the Anglo-American and English colonial

¹ Struckhoff, ‘*The Irony of Uberrimae Fidei: Bad Faith Practices in Marine Insurance*’, Summer 2005, 29 Tul. Mar. L.J. 287 at 295-296

² Hodges, ‘*Cases and Materials on Marine Insurance Law*’, 1st Ed. Cavendish Publishing 2003 at 214

³ Hare, ‘*Shipping Law and Admiralty Jurisdiction in South Africa*’, 1st Ed. Juta 1999 at 690

⁴ (1766) Burr 1905, 1 WBI 594

⁵ s 17 Marine Insurance Act, 1906 (6 Edw. 7.) Chapter 41

⁶ USA: *McLanahan v Universal Insurance Co.* 26 U.S. (1 Pet) 170, 1998 AMC 285 (1828); Australia: s 13 Insurance Contracts Act 1984, *Trans Pacific Insurance Co. (Aus) v Grand Union Insurance Co.* (1989) 18 NSWLR 675

systems accept the notion of ‘utmost’ good faith, there is little indication that it differs greatly from the good faith requirement in civil law countries.⁷

The breach of the duty of good faith is most commonly manifested as non-disclosure or misrepresentation, which are often confused with good faith as being one and the same thing.⁸ This would however be a mistake as the duty of good faith encompasses more than just disclosure and abstaining from misrepresentations.⁹ It is an extensive duty that is ‘moulded to the moment’¹⁰ and it is therefore a question of fact, in each case, whether it has been observed or not. What exactly good faith entails apart from non-disclosure or misrepresentation is not always clear, but it has been described (at least where the duty of ‘utmost’ good faith is concerned) as a positive duty that is ‘more than an absence of bad faith’.¹¹ This would clearly include fraud and in England even the innocent non-disclosure of a material circumstance would suffice to breach the duty of good faith.¹²

In South Africa, general contract law accepts that contracts are acts that involve good faith.¹³ Previously the Roman-Dutch remedy of *exceptio doli generalis* allowed a party to a contract, averring the existence of *dolus*, to present facts not allowed under the strict *ius civile*.¹⁴ Although this remedy was done away with in the case of *Bank of Lisbon & South Africa Ltd v De Ornelas*¹⁵ it did not negate the underlying requirement of good faith in contract law.¹⁶ The notion of ‘utmost good faith’ was however abandoned (at least in non-marine insurance) in *Mutual & Federal Ins. Co. v Outdshoorn Municipality*.¹⁷ Joubert JA found that South African law should rely upon Roman-Dutch principles of good faith and that the English notion of *uberrimae fidae*s cannot be used in our law.¹⁸ Hare, however argues that due to the coming in effect of the Admiralty

⁷ Hare, ‘*Shipping Law and Admiralty Jurisdiction in South Africa*’, 1st Ed. Juta 1999 at 693

⁸ *Ibid.*

⁹ Hodges, ‘*Cases and Materials on Marine Insurance Law*’, 1st Ed. Cavendish Publishing 2003 at 216: “The duty of good faith is an independent and overriding duty, with the ensuing sections on disclosure and representation providing mere illustrations of that duty.”

¹⁰ *Manifest Shipping Co. Ltd. v. Uni-Polaris Shipping Co. Ltd & Ors* (‘*The Star Sea*’) 1995, 1 Lloyd’s Rep 659 at 667

¹¹ *Container Transport Int. & Reliance Group v Oceanus Mutual Underwriting Ass. (Bermuda)* 1984, 1 Lloyd’s Rep 476 CA at 525

¹² Hodges *supra* at 237 and 247

¹³ Van der Merwe *et al.*, ‘*Kontraktereg; Algemene Beginsels*’, 1st Ed. Juta 1996 at 235; *Mutual & Federal Ins. Co. v Outdshoorn Municipality* 1985 1 SA 419 (SCA) at 431 as per Joubert JA

¹⁴ *Ibid.* at 234

¹⁵ 1988 3 SA 580 (A)

¹⁶ Hare, ‘*Shipping Law and Admiralty Jurisdiction in South Africa*’, 1st Ed. Juta 1999 at 689

¹⁷ 1985 1 SA 419 (SCA)

¹⁸ *Ibid.* at 433 E-F

Jurisdiction Regulation Act (ARJA) of 1983, that a South African court deciding the same matter in a marine insurance claim, might be able to distinguish it from *Outdshoorn Municipality* and find that ‘utmost good faith’ became a part of our law in relation to the duty to disclose and misrepresentation in marine insurance.¹⁹

It is thus clear that there should be little difficulty in applying the duty of good faith to marine insurance contracts both locally and abroad. What is included under the definition of this duty is however less clear. At the very least it should include the duty to abstain from misrepresentation and to disclose material information as mentioned in guideline 2. Most jurisdictions are reluctant to treat the duty of good faith as an independent prerequisite to marine insurance contracts and the CMI guidelines could benefit from providing a clearer view of what constitutes a breach of this duty apart from non-disclosure and misrepresentation.²⁰

3. ‘Each Party’

The guidelines make it clear that good faith is a reciprocal duty which is owed by each of the parties to the insurance contract.²¹ Lord Mansfield in *Carter v Boehm* made it clear that the duty of utmost good faith is owed by both the assured towards the insurer and vice-versa. American law similarly accepts the mutuality of this duty.²²

The English MIA also confirms this mutuality in s17 by the use of the word ‘either’. However in ss18 and 20, dealing with disclosure and misrepresentation, the act only mentions that these duties are owed by the assured to the insurer and not also the other way around. Various cases have however established that the duty to disclose is reciprocal, due to the overriding effect of s17. Thus in *Banque Keyser Ullman v Skandia* Lord Justice Slade remarked that ‘...*the obligation to disclose material facts is a mutual one imposing reciprocal duties on insurer and insured.*’²³ South African contract law accepts the equality and mutuality of parties in contracting, and should thus also accept that the duty of good faith should be reciprocal.

¹⁹ Hare, ‘*Shipping Law and Admiralty Jurisdiction in South Africa*’, 1st Ed. Juta 1999 at 692; especially with regard to the operation of s 6 of the act [marine insurance claims are maritime claims under s 1(u)]

²⁰ *Ibid.* at 688

²¹ See specifically guidelines 1,2 and 6

²² Shoenbaum, ‘The Duty of Utmost Good Faith in Marine Insurance Law: A Comparative Analysis of American and English Law’, January 1998, J. Mar. L. & Com. 1 at 16

²³ 1988 2 Lloyd’s Rep 513 CA at 544

The duty of good faith, however, operates mostly against the assured and its application against insurers is rare.²⁴ Even though the duty is a mutual one its effect certainly does not foster equality between the parties. The usual consequence of a breach of this duty is rescission of the contract.²⁵ This affords the insurer the very effective remedy of avoidance of the duty to pay the loss, while it affords the assured the scant comfort of having his premiums paid back to him.²⁶ In order to make the duty of good faith truly reciprocal, attention should not only be paid to its mutual operation but also its effect.²⁷ Thus awarding damages to an assured where the insurer breached the duty of good faith might allow 'each party' to benefit equally from the duty.²⁸

3. 'At all times during the contract'

The duration of the duty to observe good faith has caused much confusion in marine insurance legal circles.²⁹ It is clear that the duty to observe good faith persists at least until the conclusion of the contract.³⁰ Both ss18 and 20 state that the duties to abstain from misrepresentation and disclosure only apply to the period 'before the contract is concluded'. Section 17 however contains no such limiting language.

Guideline 2 suggests that the duty to act in good faith should operate not just before the contract but also 'at all times during the contract and in the submission of claims.' In the American federal system certain circuits have held that there exists a duty to disclose material information after the formation of the contract, while other circuits found that such a duty only exists in the pre-contractual stage.³¹ However, recent English cases conclude that the duties continue, albeit in a modified form, throughout the contractual relationship.³²

²⁴ Staring & Waddell, 'Admiralty Law Institute Symposium: Admiralty Law at the Millennium', June 1999 Tul. L. Rev. 1619 at 1659

²⁵ Shoenbaum, *supra* at 16

²⁶ Lee Kiat Seng, 'Ubi Ius Ubi Remedium? The Insurer's Duty to Disclose – Time for Another Look?', July 1997, Sing. J. Legal Stud. 185 at 199

²⁷ *Ibid* at 227

²⁸ For a further discussion on these issues see §.6.2 'Damages' below

²⁹ Pring, 'The Continuing Duty of Utmost Good Faith: Clear (legal) Water at Last?' 1 March 2001 at www.dentonwildesapte.com

³⁰ Hare, *supra* at 699

³¹ Struckhoff, 'The Irony of Uberrimae Fidei: Bad Faith Practices in Marine Insurance', Summer 2005, 29 Tul. Mar. L.J. 287 at 298

³² Shoenbaum, *supra* at 32

The possibility of a continuing duty of good faith was first considered in *The Litsion Pride*³³ where Hirst J. said: “*It must be right, I think... to hold that the duty in claims sphere extends to culpable misrepresentation.*” Similarly the ruling in *The Star Sea*³⁴ made it clear that a continuing duty of utmost good faith does exist albeit a qualified one. Lord Hobhouse found that there is a clear distinction to be made between the pre-contract duty of disclosure and any duty of disclosure which may exist after the contract has been made.³⁵ He then determined that only a post-contractual breach of the duty that involves fraud would allow the aggrieved party to rescind the contract at this point in their relationship.³⁶

Longmore J in *The Mercandian Continent*³⁷ stated that when discussing a post-contractual duty of good faith that the contract itself should be the correct starting point. Applying the traditionally pre-contractual principles of good faith to a contract that has already been made, would be perverse as it would enable the insurer to by-pass the rights and duties imposed on the parties by the contract by using the disproportionate remedy of avoidance.³⁸ Longmore J. suggested that the remedy of avoidance would only be appropriate in the post-contractual context where a) the fraud was material in the sense that it would affect the underwriters’ ultimate liability and b) that the gravity of the breach was such that it would enable the underwriters to terminate the contract.³⁹

From these cases it is clear that, while there is a positive obligation, at the pre-contractual stage, on the parties to act in good faith, this duty does not continue in an unmodified form after the contract it concluded. There is, however, a continuing duty on the parties not to be materially fraudulent in relation to the performance of the contract.⁴⁰

The CMI guidelines make no mention of this differing approach to the duty of good faith in the pre- and post-contractual stages. Applying an unaltered duty of good faith throughout the contract might be severely unjust if the only remedy available for a breach of that duty is the avoidance. Thus although there seems to be support for a continuing duty of good faith as set out in the

³³ *Black King Shipping Corp. v Massie* 1985 1 Lloyd’s Rep 437 especially at 512-513

³⁴ *Manifest Shipping & Co. v. Uni-Polaris Ins. Co.* 1997 1 Lloyd’s Rep. 360 (C.A.).

³⁵ Woloniecki, ‘*The Duty of Utmost Good Faith in Insurance Law: Where is it in the 21st Century?*’; Def. Couns. J., January 2002 at 66

³⁶ Shoenbaum, *supra* at 33

³⁷ *K/S Merc-Scandia XXXXII v Lloyd’s Underwriters* 2001 EWCA CIV 1275 CA

³⁸ Woloniecki, *supra* at 68-69

³⁹ 2001 EWCA CIV 1275 CA at 18 (para. 35)

⁴⁰ Woloniecki, *supra* at 17

guidelines, it might have to be tempered by either allowing for damages instead of the traditional remedy of avoidance, or in differentiating between the duty of good faith applied to the pre-contractual and the post-contractual stage.

4. Materiality

The CMI guidelines state that the acts of good faith required by the parties are only in relation to material facts, matters and alterations.⁴¹ It has always been a crucial qualification to the right to avoid a contract of marine insurance that the breach of the duty of good faith was ‘material to the risk’.⁴² Both American and British law, require that the fact, not being disclosed or misrepresented, be material before the duty of good faith is breached.⁴³

In Britain this is a requirement set forth in both statute and case law. Although s 17 is silent on the matter of materiality, the sections dealing with disclosure and misrepresentation both qualify the breach of the respective duties with the requirement of materiality. Both these sections also give similar definitions of material facts: ‘Every circumstance/representation is *material* which would *influence* the judgment of a *prudent insurer* in fixing the premium, or determining *whether* he will take the risk.’⁴⁴

According to the MIA and case law in both America and Britain it seems clear that materiality is judged by the response of the hypothetical prudent insurer.⁴⁵ There has never been any dispute as to the use of the hypothetical prudent insurer in the test for materiality.⁴⁶ There are however uncertainties about how the breach should ‘*influence*’ the mind of the prudent insurer: Must it be shown that the insurer would have come to a different decision in rating or accepting the risk or does ‘influence’ only require a lesser impact on the mind of the prudent insurer?⁴⁷

⁴¹ CMI guideline 2

⁴² *Container Transport Int. & Reliance Group v Oceanus Mutual Underwriting Ass. (Bermuda)* 1984, 1 Lloyd’s Rep 476 CA at 507

⁴³ Shoenbaum, *supra* at 17

⁴⁴ ss 18(2) and 20 (2) [emphasis added]

⁴⁵ Hodges, ‘*Law of Marine Insurance*’, 2nd Ed. Cavendish Publishing 2001 at 90; for American cases on this matter see *Kilpatrick Marine Piling v. Fireman’s Fund Ins. Co.*, 795 F.2d 940, 942-43 (11th Cir. 1986) and *All Underwriters at Lloyds (London) Subscribing to Policy No. 200-451-7275 v. Kenney*, 986 F. Supp. 1384, 1997 AMC 2373 (S.D. Fla. 1997)

⁴⁶ Hodges, ‘*Cases and Materials on Marine Insurance Law*’, 1st Ed. Cavendish Publishing 2003 at 256

⁴⁷ *Pan Atlantic Insurance v Pine Top Insurance* 1994, 3 All E.R. 581 HL at 592

This question was considered in *C.T.I v Oceanus*⁴⁸ where Lloyd J. held that a circumstance was only material if it would influence the insurer to decline the risk altogether or charge a higher premium. This is known as the ‘decisive influence’ test as the circumstance must then have exerted a ‘decisive influence’ or have induced a ‘different decision’ on the mind of the prudent insurer.⁴⁹

This case, however, was appealed and this time the court rejected the stiff test for materiality espoused at first instance.⁵⁰ The court seemed to have opted for proof merely that a prudent underwriter would want to have known about the circumstance and not that the breach of good faith would have led to a different decision or have had a decisive influence on the prudent insurer.⁵¹ This decision was much criticized as being too favourable to insurers.

The question was posed again in the *Pine Top* case⁵² where it was found that although the appeal court in the *C.T.I.* case rejected the ‘decisive influence’ test it left open the question of what an appropriate test would be. In considering what such a test might be the court opted for a more stringent test for materiality which asks whether the prudent insurer would view the risk as increased or different to what was contemplated for the insurance, a test remarkably similar to the decisive influence test.⁵³

This case was appealed to the House of Lords⁵⁴ which roundly rejected the ‘decisive influence’ test and upheld the appeal court test for materiality in *C.T.I.* However, the court added an additional obstacle for the party seeking to avoid the contract: He now not only has to show that the breach was material, but also that he was in fact induced to enter into the contract on the relevant terms.⁵⁵ Thus if the breach of the duty of utmost good faith, whether it be non-disclosure or misrepresentation, did not actually induce the making of the insurance contract, the insurer/assured will not be able to rely on it as a ground for avoiding the contract.

⁴⁸ 1982, 2 Lloyd’s Rep 178

⁴⁹ Bennet, ‘*The Law of Marine Insurance*’ 1st Ed. Oxford 1996 at 49

⁵⁰ See note 39

⁵¹ Bennet, *supra* at 50

⁵² *Pan Atlantic Insurance v Pine Top Insurance* 1993, 1 Lloyd’s Rep 469 (CA)

⁵³ *Ibid* at 505; Shoenbaum *supra* at 21; Bennet *supra* at 52

⁵⁴ 1994, 2 Lloyd’s Rep 427 HL

⁵⁵ Hodges, ‘*Law of Marine Insurance*’, 2nd Ed. Cavendish Publishing 2001 at 91

In the American system the test for materiality has been much less controversial. The United States' courts apply an objective test for materiality which is much the same as the 'decisive influence' test.⁵⁶

In South Africa the prudent underwriter test, favoured in English law prior to the *Pine Top* case, was generally accepted as the test for materiality.⁵⁷ This test was, however, rejected in the non-marine insurance case of *Oudtshoorn Municipality*.⁵⁸ Joubert JA considered himself released from English Law and he accordingly applied the generalised Roman-Dutch standard of the *diligens paterfamilias* or reasonable man. It has been argued that this test might be inequitable in the context of marine insurance as the reasonable man could not be expected to appreciate and understand the specialist and technical knowledge required in the industry.⁵⁹ South African courts might still be able to distinguish the *Oudtshoorn Municipality* decision by applying the English law prior to the 1906 MIA to a similar case dealing with marine insurance. In such an event the standard would be that of the hypothetical prudent underwriter and not that of the reasonable person.⁶⁰ Furthermore the test of materiality applied in England, before the 1906 MIA, which was similar to the 'decisive influence test', would thus also be applicable in South African law.⁶¹

The CMI guidelines propose a two-tier test also involving the standard of the reasonable insurer/assured.⁶² This in itself should provide no problems for general application as this is already the standard in both Britain and America and, as has been shown above, could also be the standard in South Africa. The second tier to this test requires that the reasonable insurer/assured consider the acceptance of the risk/cover, the assessment of the premium and the evaluation of the claims to be affected. This is remarkably similar to the 'decisive influence' test which requires that the prudent underwriter would have either rejected the risk or would have accepted it but on more onerous terms, for the breach of good faith to be material.⁶³ This test should thus be acceptable in both America and South Africa. In England the 'decisive influence' test was rejected following the *Pine Top* decision which upheld the lower threshold for materiality

⁵⁶ Shoenbaum, *supra* at 25

⁵⁷ Hare, 'Good Faith, Disclosure, Misrepresentation and the Omnipotent Warranty: A South African Perspective', Paper presented at the BMLA/Tulane Conference, London, May 2000

⁵⁸ See note 16

⁵⁹ Hare, *supra* at 697

⁶⁰ *Ibid* at 696

⁶¹ Shoenbaum, *supra* at 26

⁶² CMI Guideline 4

⁶³ Hodges, 'Law of Marine Insurance', 2nd Ed. Cavendish Publishing 2001 at 90

espoused in the appeal court decision in *C.T.I.* The test mentioned in the guidelines would thus be incompatible with English law.

5.1 'Objective Norms'

Guideline 1 states that the duty of good faith requires each party to a marine insurance contract to conduct itself 'according to objective norms recognized by the society in which they are being judged.' This requirement surely relates to the two-tier test involving the reasonable insurer mentioned in guideline 4. The standard of the reasonable insurer, and thus also the test of materiality, is inherently objective.

Prior to *CTI*, Kerr J. in *Berger & Light Diffusers Ltd v Pollock*⁶⁴ held that in order to render a marine insurance contract voidable, the breach of good faith (in this case non-disclosure) should not only be objectively, but also subjectively material. A breach was subjectively material if it induced the underwriter to conclude the contract on the terms agreed.⁶⁵ This decision was overruled in the Court of Appeal on the ground that the wording of the MIA did not accommodate any subjective requirement.⁶⁶ The court held that the view of the particular insurer as to materiality was irrelevant.⁶⁷ Some courts in America also stress that the standard applicable is an objective one.⁶⁸

However, both the American and English decisions have allowed a subjective element to creep into their concept of good faith. Both countries' courts require that in order for a party to be allowed the remedy of avoidance due to the breach of the duty of good faith, that such a breach (at least in terms of non-disclosure and misrepresentation) should not only be objectively material, but also that the party concerned should have been subjectively induced into the contract.⁶⁹ This actual inducement test concerns the actual underwriter rather than the hypothetical prudent or reasonable underwriter. Although this additional test was omitted from the MIA it is said to be 'an implied qualification of the right to avoid the contract under the act.'⁷⁰

⁶⁴ 1973 2 Lloyd's Rep. 422

⁶⁵ Bennet, *The Law of Marine Insurance* 1st Ed. Oxford 1996 at 48

⁶⁶ *Ibid* at 49

⁶⁷ Lee Kiat Seng, 'Ubi Ius Ubi Remedium? The Insurer's Duty to Disclose – Time for Another Look?', July 1997, Sing. J. Legal Stud. 185 at 196

⁶⁸ Shoenbaum, *supra* at 25

⁶⁹ *Pan Atlantic Insurance v Pine Top Insurance* 1994, 2 Lloyd's Rep 427 HL at 430; Shoenbaum, *supra* at 27

⁷⁰ *St. Paul Fire and Marine v McConnel* 1995, 2 Lloyd's Rep 116 CA at 124

It is clear that this additional subjective test does not conform to the 'objective norms' set out in the guidelines. The 'actual inducement' test was introduced due to the need for a causal connection between the breach and the making of the contract of insurance.⁷¹ Due to the lower threshold required for the test of materiality and the lack of any duty on the alleging party to prove a causal connection between the breach and the loss, it was felt that an additional requirement was necessary in order to avoid the contract of insurance.

Apart from the fact that this test does not comply with the requirement of objectivity espoused in the guidelines, it is also clear that it would be an inappropriate prerequisite for a breach of the duty to observe good faith in the post-contractual period. The continuing duty of good faith proposed by the guidelines is thus also completely incompatible with the notion inducement. For the guidelines to take effect, serious thought should be paid to the operation of an inducement requirement. Setting a higher test for good faith, such as the 'decisive influence' test, and doing away with the inducement requirement altogether or only applying the inducement test in the pre-contractual period, might be possible solutions.

In South Africa the *Oudsthoorn*⁷² case confirmed that non-disclosure should be assessed according to an objective prudent insurer test. The wording of s 53 of the Short Term Insurance Act⁷³ however allowed for a quite different test of materiality when considering misrepresentation: that of the actual insurer.⁷⁴ This test was considered in the case of *Qilingele v SA Mutual Life Assurance Society*⁷⁵ where the Supreme Court of Appeal held that the clear wording of the act imputed a test of subjectivity. S 53 was however amended in 2002 and it incorporated a specifically objective test for the materiality of both misrepresentation and non-disclosure.⁷⁶ South African law would thus very comfortably conform with the objectivity requirement set out in the CMI guidelines.

5.2 'A Causative Link'

Another solution to the problem posed by inducement for the guidelines would be to require that a causal connection be established, not between the breach of the duty to observe good faith and

⁷¹ *Pan Atlantic Insurance v Pine Top Insurance* 1994, 2 Lloyd's Rep 427 HL at 440 as per Lord Mustill

⁷² See footnote 16

⁷³ previously s 63(3) of the Insurance Act

⁷⁴ Hare, *supra* at 701

⁷⁵ 1993 (1) SA 69 (SCA)

⁷⁶ s 53 (2)(b) states that '*The representation or non-disclosure shall be regarded as material if a reasonable prudent person would consider that the particular information... should have been correctly disclosed...*'

the formation of the contract, but between the breach and the actual loss suffered. This is exactly what guideline 5 attempts. This provision requires an added step in proving the materiality of a breach, namely proof of ‘a causative link between the breach and the loss or the claim.’

It has been established early in English case law that there is no requirement to establish a causal relationship between the breach of the duty and the loss.⁷⁷ All that is required to avoid the contract is for the breach to be material.

The causal link proposal is certainly novel, but it would fit well in the framework the guidelines propose. The initial reason for the imposition of the duty to act in good faith was to create an equal footing between the parties to a contract of marine insurance. Lord Mansfield in *Carter v Boehm* argued that the ‘special facts upon which the contingent chance is computed lie most commonly in the knowledge of the assured only.’⁷⁸ It was thus required from a proposer to volunteer all information material to the assessment of the risk. The question of what information might be material, is often difficult to ascertain, especially for an assured entering into his first contract of insurance. The situation has changed much from the days of Lord Mansfield. The balance of information must certainly now be in favour of the multi-billion dollar insurance industry and the insurers who have honed the art of estimating risks to an exact science.⁷⁹ The requirement of causality would be commensurate with the practical realities of our modern era and would again level the playing field between assured and insurer, especially if the only remedy available is that of rescission.

6. Remedies

Presently rescission is the only remedy available for the breach of the duty of good faith in both Britain and the United States.⁸⁰ Breach of the duty of good faith renders the contract voidable and liable to be avoided *ab initio* at the insurer’s option.⁸¹ Section 17 states that in the event of the duty of good faith not being observed by one party, ‘the contract may be avoided by the other party.’ No other remedy is mentioned and both ss18 and 20 reiterate this remedy. From the point

⁷⁷ Struckhoff, ‘*The Irony of Uberrimae Fidei: Bad Faith Practices in Marine Insurance*’, Summer 2005, 29 Tul. Mar. L.J. 287 at 291; *Joel v Law Union and Crown Insurance Company* 1908, 2 KB 863, CA; Shoenbaum, *supra* at 27

⁷⁸ (1766) Burr 1905, 1 WBI 593 at 593-594

⁷⁹ Lee Kiat Seng, *supra* at 189

⁸⁰ Shoenbaum, *supra* at 35

⁸¹ Bennet *supra* at 67

of view of the assured this remedy is draconian as he is deprived from all cover whether he made an innocent mistake or a calculated concealment. Recent litigation in the English courts has however considered the availability of damages.⁸²

6.1 'Treat the contract as at an end'

Much has been said about the inequality created between the insurer and assured by the 'all or nothing' remedy of rescission.⁸³ The CMI guidelines, however, seeks to do away with this remedy altogether.⁸⁴ Instead of avoiding the contract *ab initio* the guidelines gives the aggrieved party 'the right to treat the contract as at an end, effective from the date of the breach.' Added to this remedy is the right to claim damages.

It is an open question as to whether this remedy will operate with equal effect on both the insurer and the assured. Where the duty of good faith was breached by the insurer this remedy will probably be much preferred to that of avoidance. Under this remedy the assured might not receive back all the premiums paid to the insurer from the start of the contract (although he should be able to claim back the premiums paid after the breach), but the additional option of claiming damages should provide him with an effective remedy to cover his losses. These losses could also include the cover promised in the insurance contract which would not be recoverable through the remedy of avoidance. For the insurer it would similarly be an effective remedy: if the breach was in the pre-contractual stage it would operate the same as avoidance.

The remedy proposed by the CMI guidelines is a flexible remedy that should be able to create substantive equality in the operation of the duty of good faith. Schoenbaum gives three arguments against the remedy of avoidance: 1) It is often disproportionate with the breach, 2) there does not need to be a causal relationship between the violation of the duty of good faith and the loss, and 3) it fails to distinguish between degrees of fault.⁸⁵ All these arguments can be answered by the good faith regime proposed by the guidelines. By including the option to claim damages and by requiring a causal link between the breach and the loss for the purposes of materiality, the guidelines ensure that this remedy will be proportionate, flexible and will promote equality between the parties.

⁸² *Ibid*; *Banque Keyser v Skandia* 1987, 1 Lloyd's Rep 69; *Bank of Nova Scotia v Hellenic Mutual War Risks Association (Bermuda)* ("The Good Luck") 1989, 2 Lloyd's Rep 238

⁸³ Lee Kiat Seng, *supra* at 227

⁸⁴ See Guideline 6

⁸⁵ Schoenbaum, *supra* at 35

6.2 Damages

In the Court of Appeal in the *Pine Top* case Nichols V.C. said in relation to rescission: ‘The remedy is all or nothing... when what is needed is a more sophisticated remedy more appropriate, and in that sense more proportionate, to the wrong suffered.’⁸⁶ Awarding damages would certainly provide a more proportionate and appropriate remedy, especially in cases where the breach would merely have caused an increase in the premiums. Thus in French Law the insurer has the option of demanding an increase in the premium if the loss is discovered before the loss. If discovered after the loss the indemnity payable is reduced proportionately with the increased premium and the premium already paid.⁸⁷ In English Law a similar financial adjustment through an award in damages may be made through a mechanism in s2(2) of the Misrepresentation Act 1967, although it will only cover a breach of the duty of good faith made by misrepresentation.⁸⁸

Steyn J. proposed that damages be awarded to an assured for a breach of the duty of good faith by the insurer in *Banque Keyser v Skandia*.⁸⁹ He argued that for the principle of utmost good faith to impose meaningful reciprocal duties on both parties to the contract, it would be inappropriate to refuse a claim for damages to an assured, if it were the only effective remedy.⁹⁰ However both the Court of Appeal and the House of Lords reversed this decision and held that rescission is the only remedy available for a breach of the duty of good faith.⁹¹

The question about damages was again raised case concerning *The Good Luck*.⁹² The Court of Appeal again reiterated that a breach of the duty of utmost good faith by an insurer did not give rise to an action for damages. Thus even though there has been some argument for the application of damages as a remedy for the breach of the duty of good faith, rescission is still the only remedy available in England. There are also no reported marine insurance cases giving damages for breach of the duty of good faith in United States.⁹³

⁸⁶ 1993 1 Lloyd’s Rep 496 at 506

⁸⁷ Bennet, *supra* at 68

⁸⁸ *Ibid* at 68-69

⁸⁹ 1987, 1 Lloyd’s Rep 69

⁹⁰ *Ibid* at 96

⁹¹ 1988 2 Lloyd’s Rep 523; 1990 2 Lloyd’s Rep 377

⁹² *Bank of Nova Scotia v Hellenic Mutual War Risks Association (Bermuda)* (“The Good Luck”) 1989, 2 Lloyd’s Rep 238

⁹³ Shoenbaum, *supra* at 38

Even though there seems to be little support for it, the regime proposed by the CMI guidelines would certainly negate many of the arguments raised against rescission as the only remedy for a breach of the duty to observe good faith. The prerequisite of a causal link between the breach and the loss for the requirement of materiality is complemented by guideline 7 which states that a non-material absence of good faith may still give rise to a claim for damages. The framework seems to provide equitable and proportionate remedies to both parties whether the breach occurred before or after the conclusion of the contract.

7. Conclusion

The guidelines proposed by the CMI address many of the problems faced by the doctrine of good faith. Unfortunately there seems to be little support for most of these provisions in many jurisdictions. To my mind, the proposed framework must be implemented as a whole for it to have full effect. This would require a comprehensive overhaul of any legal system which wishes to apply it. As this seems to be a very unlikely prospect, it is only to be hoped that it will influence future decisions in this area of law in a constructive way.