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Fraudulent insurance claims: legal definition and judicial consequences

by

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ABSTRACT

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Johanna Carolina Catharina Hjalmarsson

While much of the narrative of this thesis chips away at imperceptible changes in case law, this is ultimately a text as much about legal policy as about law. The author will assert that it is time for a tectonic shift in the manner in which insurance is considered under the law of England and Wales, and sets out the basis for this view. Chapter 1 is a brief general introduction. Chapter 2 sets out the background of the reform project against which this work has been undertaken and its ongoing reform of insurance contract law, underlining how the research has been undertaken in a context of moving goalposts. It further provides some stipulative definitions and initial consideration of the concepts of good faith and moral hazard. Chapter 3 sets out the law on fraudulent claims – a fairly basic endeavour it might be thought, but as will be seen the law has been far from clear to the point of requiring clarification by the legislator. Chapter 4 explores how the burden and in particular the standard of proof operate in cases of insurance fraud, and explores how the courts address these, and how they ought to address them. Chapter 5 breaks new ground in exploring and setting out the strategies employed by insurers in achieving punitive results against insurance fraudsters, in the face of the difficult legal position created by the law as outlined in the previous chapters. A final chapter teases out the consequences of the preceding chapters and offers conclusions. It will be concluded that the law is in need of recalibration not just along contractual lines and with greater principle in mind, but also along procedural lines with close consideration of the remedies available to the parties.

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Academic Thesis: Declaration of Authorship

I, ……Johanna Hjalmarsson……

declare that this thesis and the work presented in it are my own and has been generated by me as the result of my own original research.

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I confirm that:

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Hjalmarsson, J *Fraudulent insurance claims* Shipping & Trade Law (2010) Vol 10(7) pp 3-5

Hjalmarsson, J, *The standard of proof in civil cases: the insurance fraud perspective* (2013) International Journal of Evidence and Proof, (2013)17, (1), 47-73

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Signed: ……

Date: ……20 June 2016……

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The thesis takes into account the law as it stood on 29 January 2016.

Fraudulent insurance claims: legal definition and judicial consequences

1 Introduction with methodology

Why does fraud matter? At its broadest, this is an actuarial question to which the answer rests on the immense combined value of insurance frauds committed in contracts subject to English law; the response to which involves unfathomable numbers and intensive social pressures in the form of e.g. witness corruption and criminality. As recently as in January 2016, the Insurance Fraud Task Force states in the Foreword to its Final Report:

> "Insurance fraud is a serious issue, which has been estimated to cost policyholders up to £50 each per year, and the country more than £3 billion. The costs of fraudulent insurance claims are passed on to customers, pushing up the prices of essential products, such as motor and home insurance, with consequences for everyone through an increased cost of living. Valuable public resources, such as those in our NHS and in the courts, are spent on dealing with fraudulent cases. It is also a source of funds for organised crime. Insurance fraud is socially corrosive, with opportunistic fraud often undertaken by otherwise honest individuals. Tackling insurance fraud helps society as a whole, which is why the Government established this Taskforce to investigate and make recommendations on how to reduce overall levels of insurance fraud." [1]

The statistics as well as the values discussed in this statement are applicable on a broad level to underpin the sort of society we should aim to build around us – with insurance as a valid risk management tool available to risk averse persons and businesses, large and small. Indeed, the very existence of the Insurance Fraud Task Force is noteworthy: a government task force set up to tackle a business problem that has become so widespread and entrenched that it is now a 'social evil'. From a technically legal perspective however, the questions to ask are how the law of insurance fraud operates and how it applies to insurance contracts; but also of enforcement of the values underpinning our society in this regard. Methodologically, the starting point is the insurance contract law of England and Wales as evidenced by legislation and case law, the reform process the law is currently undergoing and the reasons why it is under reform. Insurance contract law is burdened by a series of

[1] Introductory words from the Foreword of the Final Report of the Insurance Fraud Task Force, January 2016: The Report is available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/492980/PU1817_Insurance_Fraud_Taskforce.pdf (accessed 20 January 2016).

thorny problems created over sometimes several hundred years, recently the focus of review by the Law Commissions[2] who have endeavoured to find legislative solutions to problems with insurable interest, pre-contractual disclosure, the doctrine of post-contractual good faith, warranties, late payment of insurance claims and insurance intermediaries – recording some significant partial successes. Each of the areas of focus is characterised by the twin roots of fraud prevention and information asymmetry – that is, the law is designed to cater for a situation where the insurer is not provided with sufficient information and is at a disadvantage in obtaining that information. The law gives such an insurer the opportunity to impose heavy handed remedies on the contractual relationship; on the basis that an incentive for the insured to commit fraud against the insurer is inherent in the contractual relationship.

A key point to be considered is the obstacles of a systemic and procedural nature that insurers encounter in their efforts to avoid insurance fraud, namely the burden and especially the standard of proof. The more exacting the standard of proof that the insurer must meet, the more difficult it will be for the insurer to prove that the insured has committed, or is attempting through its claim to commit insurance fraud. The greater the difficulties become, the more inclined are the insurers to resort to alternative arguments, at the extreme entirely omitting the plea of fraud. Judges, who may agree that the insured is committing fraud, or sometimes cannot be certain that they are not, may be inclined to concentrate excessively on the remedies and may as a result even end up distorting the law with a hard case. Thus the native hue of the law is sicklied o'er by the pale cast of fraud.[3] These issues are considered on the basis of case law evidencing, it is argued, a shift in the consideration of such issues over the past century. While the original position was admittedly not favourable to insurers, there has been a tectonic shift not least in how the standard of proof is applied, now permitting insurers to plead or allege fraud without being procedurally penalised.

Finally, insurers have sought and found other means to enforce anti-fraud policy. The case law in this area has to this author's knowledge not been previously analysed and the analysis is therefore designed to determine the basic concepts derived from case law, with an eye on insurer strategy and judicial attitudes.

Methodologically, over the several years of work on this research, the focus has shifted remarkably compared to the original intent and purpose. It might be correct to say that the pendulum has swung, because as will be evident from this introductory chapter, the author has arguably returned to the

[2] The use of the plural is appropriate, given that it was a joint effort by the Law Commissions of Scotland and England and Wales. Where only England and Wales are at issue at any point in this work, the singular will be used, otherwise the plural. For a general introduction to the Law Commissions' project, see http://www.lawcom.gov.uk/project/insurance-contract-law/ (accessed 20 January 2016) – see also the complete list of relevant Reports in a footnote *infra*.

[3] After Shakespeare's *Hamlet*, Act 3, Scene 1, Hamlet's soliloquy: "And thus the native hue of resolution is sicklied o'er with the pale cast of thought".

starting point. While part of the thesis now before the reader is distinctly doctrinal in character, notably Chapter 5 and its discussion of the use of contempt of court, which employs little theory at all, much of the thesis is perhaps best characterised by a search for theory resulting in a finding of its absence.[4] This statement warrants further explanation.

The first proposal was to discuss law reform in light of fraudulent claims. The work on this thesis has coincided in time with that of the Law Commissions and the ongoing process of reform of English insurance contract law, and as a result has to some extent continuously been a work in progress. It was perceived by this author at the outset that the law on insurance fraud and the treatment by the courts thereof had been the primus motor behind many of the peculiar and excessive developments in the law which had come to necessitate reform. For instance, *Macaura v Northern Assurance Company Ltd*,[5] a case on insurable interest, is surrounded by a nebulous cloud suggesting that the insured had acted fraudulently in bringing about the claim. The suggestion of the presence of fraud was technically unfounded, given that the several charges of fraud made in arbitration had been decided in the insurance claimant's favour, but a cloud of fraud hanging over the proceedings would constitute no incentive for the House of Lords to be lenient in its interpretation of the requirement for an insurable interest, making the case an unfortunate apex precedent for modern law even on the assumption that the outcome was correct. An illustration of insurers' tenacity where fraud is suspected, even where it is disproved, may be seen in *James v CGU Insurance Plc*.[6] Insurers here pleaded fraud and non-disclosure, lost on fraud but succeeded on non-disclosure, having advanced no less than eight grounds of non-disclosure all unrelated to the loss. The suggestion is also present in the cases of *The Grecia Express*,[7] on non-disclosure; *The Kastor Too*[8] and *The Milasan* ,[9] a case on warranties. In the latter, a clause was interpreted by the book according to the harsh rule on warranties – this would not appear significant if it were not for the subsequent cases *The Newfoundland Explorer*[10] and *The Resolute*,[11] where an identical clause gave rise to completely different conclusions: in *The Newfoundland Explorer* the clause was said (*obiter*) to be not a warranty but a suspensory condition; in *The Resolute* the clause at issue ought to be interpreted *contra proferentem*

[4] The author finds inspiration on methodology particularly from the discussion of methodology of Brian R Cheffins, *Using Theory to Study Law: A Company Law Perspective*, 58 Cambridge LJ (1999).
[5] [1925] AC 619.
[6] [2002] Lloyd's Rep IR 206.
[7] *Strive Shipping Corp & Anor v Hellenic Mutual War Risks Association (The Grecia Express)* [2002] EWHC 203 (Comm), [2002] 2 Lloyd's Rep 88.
[8] *Kastor Navigation Co Ltd v AGF MAT* [2004] EWCA Civ 277, [2004] 2 Lloyd's Rep 119.
[9] *Brownsville Holdings Ltd. & Anor v Adamjee Insurance Co Ltd (The Milasan)* [2000] EWHC 223 (Comm), [2000] 2 Lloyd's Rep 458.
[10] *GE Frankona Reinsurance Ltd v CMM Trust No 1400 ('The Newfoundland Explorer')* [2006] EWHC 429 (Admlty), [2006] Lloyd's Rep IR 704.
[11] *Pratt v Aigaion Insurance Company SA* [2008] EWCA Civ 1314, [2008] 2 All ER (Comm) 574.

and with regard to the context. In these signal cases, more favourable interpretations were available in cases where the insured was manifestly not dishonest.

It is therefore evident that context matters – judges will interpret a clause in context and if there are circumstances where the insured merits the sympathy, or a punitive attitude, from the judge, this will be forthcoming. This attitude may not be stated in black and white in the judgment. It may be apparent between the lines or deduced from the factual circumstances, but judges will emphatically not say "this insured is akin to a consumer and therefore deserving of our sympathy" or "this insured is possibly dishonest and we will therefore apply the full force of the law". Such statements would indeed be inappropriate in a traditional insurance contract where the parties are taken to be contracting on an equal footing and from comparable bargaining positions.

At the outset of this research project, therefore, the curiosity of the author lay in discovering the impetus that insurance fraud has constituted in giving rise to the contortions of insurance law now necessitating reform. Such a reasoning inscribes itself neatly into a general paradigm of information asymmetry and moral hazard as developed by modern US theorists. Given that any impetus on the judge produced by fraud is *a priori* undiscoverable and as a result also immeasurable, there was never an ambition that this should go further than a state of curiosity – it was not the intention to quantify this impetus. The first objective was therefore to study the current state of the law on fraudulent claims and commit to the record a statement of the law as it currently stood. The evidence of this research is presented in chapter 3. In the course of this research, it became apparent that the rule of evidence of fraudulent claims has borne an impact on the inclination of insurers to bring proceedings on fraudulent claims, or to respond to a claim by an explicit allegation of fraud. Procedure is an integral part of the law and issues pertaining to that field may have a direct and crucial impact on the law in a precedent-based system. It therefore became essential to produce a study of procedural factors influencing when fraud is – or is not – pleaded. The findings of this study are presented in chapter 4.

In the course of this work, and while recognising that quantification of the influence of fraud on substantive insurance contract law could never be achieved, the author became curious about the capacity of the discipline of *Law and economics* and in particular its concepts of moral hazard and information asymmetry as a tool to provide a partially satisfactory analytical tool.[12] However, the author in the end found those theories inapt to correctly analyse a legal paradigm that ultimately depends on and harks back to a different conceptual reality. The author's study of the field quickly

[12] The author was at this stage influenced not least by George Akerlof. *The Market for Lemons: Quality Uncertainty and the Market Mechanism*, Quarterly Journal of Economics, 84 (3) pp 488–500 and retains information asymmetry as a valuable concept to refer to, if not fully analyse, the insurance relationship.

resulted in the discovery of Tom Baker's article *The Genealogy of Moral Hazard*, which[13] caused the author to conclude that neither the modern *Law and economics* concept of moral hazard, nor its original 19th century marine insurance practice denotation, regrettably present pertinent tools in attempting to understand or conceptualise the present state of the law. The author considers that better defined concepts of good faith and moral hazard, instead of their dissolution and dilution, would be a valuable tool in analysing insurance law, but that the present concepts available are not of such value. The author regrets this conclusion and presents it briefly in chapter 2, but it must be stated at the outset that a full discussion of this should probably be left for another thesis.

Having thus considered *Law and economics* methodology and found it wanting, the author found herself in the clutches of a historical approach – while also coming to the conclusion that the dearth of historical materials was not accidental. Attempts at a historical analysis of the subject of fraudulent claims, the author considers, returns the student to modern law-making as the entirely predominant source of law, and a mere doctrinal, litigation-strategy and opportunity mechanics of fraud and their influence on modern insurance law as the paramount subject for study. Based on that insight, the author then sought to understand the true nature of the law on fraudulent claims, the options for insurers to plead fraud before a court, penalising fraudulent behaviour, and the options available to insurers where contract law does not offer satisfactory solutions. While touches of sociology and psychology will be found in the observations, those are not systematic and should not be viewed as methodological in character. That is the analysis now before the reader.

[13] Tom Baker, On the Genealogy of Moral Hazard, *Texas Law Review* (1996) Vol 75 Number 2, 237-292.

2 Modern insurance law – under construction

The place to start is with the unsatisfactory state of the law as recently as in 2006, at the start of the successful reform process undertaken from 2006 and onwards. This starting point will not least serve to emphasise the modern character of the law now before us as a body of recent innovation, potentially conceptually detached from its legacy. There was at the time of the commencement of the reform process a clear and universally recognised need for reform.[14] Modern insurance law has undeniably undergone some exciting changes in the period of this research project, and it is impossible to do them full justice here, and probably also undesirable. The reforms are partially, but not entirely, reflected in the structure of what follows. This first chapter is dedicated to a review of the state of the law today and the successful reform process undertaken from 2006 and onwards. The use of the adjective 'successful' here is warranted by the fact that this process has resulted in two enacted items of legislation, one in force and the other most likely to be in force by the time this thesis is finalised. The reader is reminded that a broad review of the substance of the law reform process and its drivers is warranted by the author's assumption that the law on fraudulent claims has had an indirect impact on the general state of the law, its rules and remedies, as we found it still on 5 April 2013 before any reform proposal had entered into force. There follows a brief consideration of the use of some key concepts, including good faith and moral hazard. While this is not the place for a full review of their denotation and connotations, a brief overview with some basic assumptions is in place to underpin concluding thoughts at the end of the thesis. That part of this chapter is essentially aimed at demonstrating the dilution of these concepts over time and their reduced relevance to modern law.

2.1 The Law Commissions' work

The work on this thesis has coincided in time with that of the Law Commissions and their ongoing process of reform of English insurance contract law.[15] The Law Commissions' work incepted in January 2006 with a so-called Scoping Paper,[16] which was followed by no less than ten Issues Papers,[17] an Introductory Paper,[18] summaries of responses,[19] a Policy Statement,[20] three Consultation Papers[21] and two Reports.[22]

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[14] See the Law Commissions' initial review *Insurance Contract Law: A Joint Scoping Paper*; available through http://www.lawcom.gov.uk/project/insurance-contract-law/ (accessed on 12 January 2016).
[15] The Law Commission reference page: http://lawcommission.justice.gov.uk/areas/insurance-contract-law.htm (accessed on 16 July 2014).
[16] *Supra*.
[17] Issues Paper 1: Misrepresentation and Non-Disclosure (September 2006) , Issues Paper 2: Warranties (November 2006) , Issues Paper 3: Intermediaries and Pre-Contract Information (March 2007) , Issues Paper 4: Insurable Interest (January 2008) , Issues Paper 5: Micro-businesses (April 2009) , Issues Paper 6: Damages for Late Payment and the Insurer's Duty of Good Faith (published March 2010) , Issues Paper 7: The Insured's Post-Contract Duty of Good Faith (July 2010) , Issues Paper 8: The Broker's Liability for Premiums - Should Section 53 be Reformed? (July 2010) and Issues Paper 9: The Requirement for a Formal Marine Policy: Should

The first tangible result was the Consumer Insurance (Disclosure and Representations) Act 2012, which entered into force on 6 April 2013 and notably amended the Marine Insurance Act 1906 for the first time in many decades by withdrawing consumer-owned vessels from its scope.[23] A further piece of legislation, the Insurance Act 2015, was enacted in February 2015 with entry into force on 12 August 2016, enabling also the Third Parties (Rights Against Insurers) Act 2010, which had been languishing on the shelves, to enter into force with a simple decision of the Secretary of State. It is not in doubt that further material contributions will be made to statutory insurance law in this jurisdiction, besides the significant contributions made to theory and analysis by way of the many discussion documents produced. This will include progress on insurable interest as well as provision in the Enterprise Act, already in progress, to address the issue of late payment of insurance claims which was unexpectedly excluded as controversial at late stages of consideration of the Insurance Act 2015. The Bill went through Parliament on the rapid procedure designed for uncontroversial Law Commission Bills.

Earlier attempts at reform by the Law Commissions resulted in reports published in 1957 and in 1980, but those attempts were of very specific and limited scope, encompassing only warranties and the pre-contractual duty of disclosure. However the sheer size of the reform venture this time is only one aspect – the real story is the success the process has enjoyed.

2.2 Drivers of insurance contract law reform

While this thesis does not aim to provide a historical account of the process of reform, and a short account is quite sufficient for the purposes set out in the introduction, it is nevertheless appropriate next to set out a wider background to the currently ongoing reform process. There are a number of drivers towards reform which as a matter of order should be fully noted, to give proper context to the law on insurance fraud.

Section 22 be Repealed? (October 2010) and Insurable Interest, 27 March 2015: Updated proposals for reform of the requirement for insurable interest.

[18] Introductory Paper: s 83 Fires Prevention (Metropolis) Act 1774 (March 2009).

[19] Responses to Consultation Paper (business insurance) (October 2008) , Responses to Consultation Paper (consumer insurance) (May 2008) , Responses to Issues Paper 5 (micro-business insurance) (November 2009) .

[20] Policy statement on intermediaries: for whom does an intermediary act in transmitting pre-contract information from consumer to insurer? (March 2009).

[21] First Consultation Paper: Insurance Contract Law: Misrepresentation, Non-Disclosure and Breach of Warranty by the Insured (CP182) (July 2007) . Second Consultation Paper: Insurance Contract Law: Post Contract Duties and other Issues (December 2011). Third Consultation Paper: Insurance Contract Law: The Business Insured's Duty of Disclosure and the Law of Warranties (June 2012).

[22] Consumer Insurance Law: Pre-contract Disclosure and Misrepresentation, December 2009 and Insurance Contract Law: Business Disclosure; Warranties; Insurers' Remedies for Fraudulent Claims; and Late Payment, July 2014.

[23] The Act was based on the *Consumer Insurance Law: Pre-Contract Disclosure and Misrepresentation: Report and Draft Bill*, published on 15 December 2009 along with the report Consumer Insurance Law: Pre-contract Disclosure and Misrepresentation (December 2009).

2.2.1 European insurance law harmonisation

An admittedly important factor behind the Law Commissions' reform project at its inception in 2006, which had not been present in earlier attempts at reform but was gathering powerful momentum at that time, was what might be referred to as the 'European dimension'. Going for a moment beyond the narrow legal discourse and observing insurance as a business, the nature of the insurance market and insurance as a business is that it fits into the European market integration project better than most.[24]

Unlike most other commodities or services, insurance business can without problems or obstacles be conducted from opposite ends of a continent, without any need for two people to meet and shake hands or for goods to be transmitted or traded or for the object on which the service is to be carried out to change hands. The product sold is basically a financial safety net to be activated upon the occurrence of certain defined circumstances, and therefore the main services to be performed under the contract are simply (on the part of the insured) the payment of the premium and (on the part of the insurer) the payment of any accruing indemnity. That said, it is clear that any insurance contract is highly dependent on applicable contract law and insurance law. For political reasons, consumer protection would be an essential feature of any European Insurance Contract Law regime, just as it is currently an essential feature of most national legislation in the EU. Harmonisation is therefore a difficult goal to achieve with current contract and consumer protection legislation in each Member State being subtly or even fundamentally different.

As a result of the potential of the market and of the deceptively simple and attractive goal of a single insurance market, the European Union was keen from the outset to work towards a pan-European insurance market. It is not surprising then that the European Union was the most significant driver of the development of a pan-European regulatory regime over several decades. This regulatory prong of the European project was the harmonisation of the insurance industry as such, and its corporate, authorisation and supervision aspects.[25] The project of the creation of a single market started as early

[24] The following was presented by this author in a talk to postgraduate research students in law at the University of Southampton in May 2008.

[25] The relevant EU measures in force before 1 January 2016, when much of existing law was superseded by Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance, also known as Solvency II, was the following catalogue. The First Council Directive of 24 July 1973 on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking-up and Pursuit of the Business of Direct Insurance other than Life Assurance (73/239/EEC) as amended; the Council Directive of 24 July 1973 Abolishing Restrictions on Freedom of Establishment in the Business of Direct Insurance other than Life Assurance (73/240/EEC); the Council Directive of 29 June 1976 Amending Directive 73/239/EEC on the Co-ordination of Laws, Regulations and Administrative Provisions Relating to the Taking Up and Pursuit of the Business of Direct Insurance other than Life Assurance (76/580/EEC); the Council Directive of 30 May 1978 on the Coordination of Laws, Regulations and Administrative Provisions Relating to Community Co-insurance (78/473/EEC); the Council Directive of 10 December 1984 amending, Particularly as regards Tourist Assistance, the First Directive (73/239/EEC) on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking-up and Pursuit of the Business of Direct Insurance other than Life Assurance (84/641/EEC); the Council Directive

as in the sixties and insurance contract law was then included in the group of measures being considered, although it was soon realised that for technical reasons, it was going to be the most difficult part. In spite of the ideal nature of insurance as a single European market commodity, the insurance industry was traditionally very insular and restricted in scope to each individual country. This is explained in part by the fact that some forms of insurance were provided by the State; there were frequently monopolies. Indeed in some extra-European countries, there is to this day still the requirement for a fronting arrangement in order to conclude insurance with a foreign insurer or reinsurer. Therefore the creation of a single market was always going to be a long-term project, with or without the contract law element. The focus of the early work towards a single market became the right of establishment and the freedom to provide services. In that connection, the main obstacle to overcome was that each State operated its own authorisation scheme with idiosyncratic requirements and regulations. As a result of harmonisation, the intra-European borders were opened by setting up passport arrangements so that authorisation in one State now allows the insurer to transfer to another state and also to provide services in another State.

The first Directives were issued in 1973 and the single market was finally achieved in 1994. An attempt at harmonisation of the contract law was initiated, but was deliberately and explicitly abandoned by the European Commission in 1993. The next step following the completion of the internal market was the project Solvency II, the entry into force of which was postponed repeatedly but finally achieved in January 2016.[26] This project too is entirely regulatory and addresses the solvency requirements of insurers and the level of reserves that they must keep to be deemed capable of meeting their liabilities. The nature of insurance business is to receive funds and keep them in reserve, because the premium is paid well before any claim is made and the potential temptation therefore arises to speculate with the funds held and to take greater risks than warranted. It is also expensive to maintain large funds to meet liabilities, and the natural incentive (not to say temptation)

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of 22 June 1987 on the Coordination of Laws, Regulations and Administrative Provisions relating to Legal Expenses Insurance (87/344/EEC); the Second Council Directive of 22 June 1988 on the Coordination of Laws, Regulations and Administrative Provisions Relating to Direct Insurance other than Life Assurance and Laying Down Provisions to Facilitate the Effective Exercise of Freedom to Provide Services and Amending Directive 73/239/EEC (88/357/EEC); the Third Council Directive of 18 June 1992 on the Coordination of Laws, Regulations and Administrative Provisions Relating to Direct Insurance other than Life Assurance and amending Directives 73/239/EEC and 88/357/EEC (Third Non-Life Insurance Directive) (92/49/EEC); the Directive 98/78/EC of the European Parliament and of the Council of 27 October 1998 on the Supplementary Supervision of Insurance and Reinsurance Undertakings in an Insurance or Reinsurance Group; the Directive 2001/17/EC of the European Parliament and of the Council of 19 March 2001 on the Reorganisation and Winding-up of Insurance Undertakings; the Directive 2002/13/EC of the European Parliament and of the Council of 5 March 2002 Amending Council Directive 73/239/EEC as Regards the Solvency Margin Requirements for Non-Life Insurance Undertakings and the Directive 2007/44/EE of the European Parliament and of the Council of 5 September 2007 Amending Council Directive 92/49/EEC and Directives 2002/83/EC, 2004/39/EC, 2005/68/EC and 2006/48/EC as Regards Procedural Rules and Evaluation Criteria for the Prudential Assessment of Acquisitions and Increase of Holdings in the Financial Sector.

[26] EIOPA web site: https://eiopa.europa.eu/regulation-supervision/insurance/solvency-ii (accessed on 12 January 2016).

for insurers and reinsurers is to seek to structure insurance arrangements such that the liabilities can be met as cheaply as possible, which also means reducing the amount of funds kept in reserve.[27] Solvency II, in simple terms, is designed to ensure on a European level that insurers must remain solvent.

2.2.2 Contract law

In the meantime, there was also a separate project with the aim of developing a European contract law (excluding insurance contract law). The impetus towards creating a European contract law came from the consumer field: it was discovered that various consumer protection measures used a variety of different contract law concepts; and soon enough the harmonisation ball was rolling.[28] With insurance contract law, the situation can be said to be analogous – a pan-European insurance business project with a single European insurance market, where contracts are entered into across borders will probably require some element of a pan-European insurance contract law.

Although the insurance contract law project of the European Union was abandoned in 1993, an alternative initiative by a group of academics, partly funded by the Commission, succeeded in developing principles of insurance contract law in the manner of the general contract law principles.[29] This initiative began in 1999, was conducted by a group of volunteer academics representing a wide range of European jurisdictions, including England and Wales, and was based in Innsbruck in Austria. The project was referred to simply as the "Restatement". The result was christened the Principles of European Insurance Contract Law (PEICL) and was submitted to the Commission at the end of December 2007. The text has subsequently been published in book form in several languages.[30] The Restatement group in its work subscribed to the terminology and conformed to the categories of the European contract law project, although the inception and context of the project were entirely different, arising out of the reform of the regulatory framework rather than out of the work on a harmonised European contract law.

The resulting PEICL are intended as an optional instrument which the parties to an insurance contract can incorporate in the policy as applicable law, in place of any national legal system. While there is currently no indication that the European Union might adopt this text as a single European insurance contract law enactment, this was undoubtedly the intention at the starting point. The law reform

[27] By way of example this incentive resulted in the policy that was the subject-matter of the *Feasey* litigation when Lloyd's of London had changed the rules defining long-tail insurance: *Feasey v Sun Life Assurance Company of Canada and another* [2003] EWCA Civ 885, [2003] Lloyd's Rep IR 637.
[28] Towards the Principles of European Contract Law, produced by the Commission on European Contract Law often referred to as the Lando Commission.
[29] Of the Lando Commission, supra.
[30] Jürgen Basedow. et al, *Principles of European Insurance Law (PEICL)* (Munich: Sellier European Law Publishers, 2009).

process that took place within the United Kingdom (*infra*) therefore originally took on additional urgency, due to the existence of the ongoing European initiative and the uncertain outcome of that venture. This factor is no longer a strong impetus due to the fact that the current plan is instead for the PEICL to be used as a supplementary or perhaps better expressed parallel legal system.[31]

2.2.3 Within the English horizon

Insurance contract law in most European countries is *sui generis* compared to other contract law, because its main feature is that of being protective of consumers. As outlined, this is part of the problem when trying to create a single European market: the various legal systems have produced vastly differing forms of consumer protection.

English insurance contract law on the other hand bears a heavy burden of tradition in this field, because the original forms of insurance came about as marine insurance and life insurance. There was also fire insurance, a mutual form of insurance particularly popular in densely populated cities. Marine and life insurance in particular were typically taken out by businessmen or by very rich people who could not be said to be contracting parties occupying a bargaining position significantly inferior to that of the insurers. Especially marine insurance was business insurance of a strictly commercial nature.[32] A distinctive feature was that the insured was assumed to possess significantly more information about the subject-matter insured and the perils to which it would be subjected, than the insurer could possibly hope to have.

The Marine Insurance Act 1906 is a statement of common law insurance contract law at the turn of the century, developed in large part on the premises described. English insurance contract law and in particular the Marine Insurance Act are very different from other European insurance contract law not just in their feel and essence but also in that they have developed some peculiar concepts over the years. In particular, there is no heritage whatsoever of consumer insurance in English insurance contract law. Instead, the solutions to pervasive injustices were achieved through regulation, supervision and not least industry-wide undertakings by insurers – often referred to as self-regulation.

Towards the end of the twentieth century, an extra-legal framework developed in order to accommodate dissatisfied consumers who now have the right to bring their grievance before the Financial Ombudsman Service (FOS). FOS in its practice developed and applied a different set of

[31] However traces of this sentiment remain to be seen in literature: Aikens LJ in his article Richard Aikens, 'The post-contract duty of good faith in insurance contracts: is there a problem that needs a solution?', [2010] JBL 379-393, having analysed the state of the law and found it unsatisfactory, concluded by rejecting "reform for the sake of tidiness" and legislation generally – but accepting that the Law Commissions would be better placed to regulate the London market than Brussels.

[32] The author finds herself picturing the insured in the 18th and 19th century cases as a wily mariner on the model of James Onedin of 'Onedin Line' fame.

rules and principles, more favourable to the insured, than general insurance contract law.[33] The decisions of FOS are, by virtue of a voluntary agreement with the insurance industry, binding on insurers but consumers who are dissatisfied with the decision retain their right of action before the courts.[34] Although until the entry into force of the Consumer Insurance (Disclosure and Representations) Act 2012 in April 2013, if FOS did not side with the consumer, it was highly unlikely that a judge would do so, given that judges are bound by insurance contract law which until April 2013 was invariably stricter than the principles applied by FOS.

In terms of legislation, the Unfair Contract Terms Act 1977 excludes insurance contracts from its scope of application, and section 64(1) of the Consumer Rights Act 2015[35] holds that a 'transparent and prominent'[36] term will not be assessed as unfair (so long as it is in plain intelligible language) that relates to either the specification of the main subject matter of the contract, or to the appropriateness of the price payable.[37] The very essence of the insurance contract, namely the scope of the risk and the size of the premium, are therefore likely to continue to usually be excluded from the application of the Act, as was the case with the preceding Unfair Terms in Consumer Contracts Regulations 1999. The Act, like the Regulations, will apply to any other terms in the policy, but the central terms representing the essence of the insurance contract are excepted.

The English insurance market is leading, particularly in reinsurance but also in other forms of commercial insurance. The perception is that English law is predictable, yet flexible.[38] Consumer protection is satisfactorily addressed by other, extra-judicial means. Britain possesses no social interest in acquiring an alien consumer protection framework. It is therefore practically a foregone conclusion that any attempt at imposition of a European insurance contracts act will be ferociously resisted. Fortunately, there appears to be no such measure on the horizon.

2.2.4 Conclusion

It was against the background of this canvas that the Law Commissions' reform project began in 2006 and remains in motion, remaining projects being Enterprise Bill provisions addressing late payment of

[33] Explored in Judith Summer, *Insurance Law and the Financial Ombudsman Service* (London: Informa, 2010)
[34] The scheme bears a remarkable resemblance to the courts of equity that developed the principles of equity that were merged into mainstream law in the 1870s.
[35] The Consumer Rights Act 2015 revoked the Unfair Terms in Consumer Contract Regulations 1999 which implemented Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts. The regulations are revoked by Schedule 4 item 34 of the Consumer Rights Act 2015, section 64(1) in Part 2 of which is to the same effect as the previous Regulations.
[36] Section 64(2), Consumer Rights Act 2015.
[37] Section 64(1)(b), Consumer Rights Act 2015.
[38] When a judgment changes or does not follow the law, this is not regarded as unpredictability, it is considered an expression of the flexibility of the law and to be commended.

claims and the promise of action on insurable interest.[39] The approach of the Law Commissions was to identify and address the several issues referred to in the introduction above: insurable interest, pre-contractual disclosure, the doctrine of post-contractual good faith, warranties, late payment of insurance claims and insurance intermediaries. Review was slow and methodical, but legislation was enacted swiftly and in parts without sufficient reflection.[40]

Because English law is very different from that of other European countries, the potential harmonisation looming on the European horizon presented a serious challenge. Other European jurisdictions do have in common the feature that the law is essentially consumer protection oriented. However, even between civil jurisdictions there are difficulties because different protection mechanisms have been developed in different jurisdictions. Current thinking at the European level is that a European insurance contract law ought to be introduced as an optional regime that people could select at will, a "28th option". This option could be selected for instance when consumers buy electronic goods with insurance over the internet.[41] It might be observed that English insurers are likely to be happy to accept without major friction a voluntary regime available for use as an alternative. It is arguably a solution perfectly compatible with the *nous* of English law to be open to alternative solutions that the parties to the contract may at their discretion adopt as their preferred framework.

In the course of the Law Commissions' work, possibly related to the abandonment of a mandatory European insurance contract law, the Law Commissions also abandoned the idea of a comprehensive insurance contract code of the Australian type.[42] Consumer insurance was dealt with first, and then a more wide-ranging piece of legislation reframing the default position of the law received Royal Assent on 12 February 2015, to enter into force in August the following year. Further measures are expected as outlined above. In sum, there would be no Code.

2.3 Can modern law be conceptualised? Good faith, moral hazard

As foreshadowed in the introduction, this author considers that the philosophical conceptualisation that historically underpinned insurance law over time has become disjointed and ineffective as a framework in modern times, and that sometimes a conceptual coherence is assumed that is potentially

[39] The latest substantive development being Issues Paper 10: Insurable Interest: updated proposals, 27 March 2015, available from http://www.lawcom.gov.uk/project/insurance-contract-law (accessed on 20 January 2016). The Issues Paper was followed by a consultation. Further developments are expected in the immediate term.

[40] Perhaps a bold statement, argument for which will have to be saved for another context.

[41] As is the case for the planned European Sales Law which will apply to online sales if the parties choose it as the applicable law of the contract: http://www.europarl.europa.eu/news/en/news-room/content/20130916IPR20025/html/Common-European-Sales-Law-backed-by-legal-affairs-MEPs, accessed on 21 September 2013.

[42] Insurance Contracts Act 1984 (Cth).

absent and if existing arguably cannot provide the legacy framework we crave. What follows is mainly intended to justify the lack of use of some overarching concepts that the reader may rightfully expect to see employed in the discussion of the black letter of the law that follows in the subsequent three chapters.

2.3.1 Good faith and moral hazard

Setting out with the concept of good faith, *uberrima fides*, which amounted to a simple framework of mutual duties between the parties, developments in the law have meant that there is not much left of that original concept. There is unequivocal judicial authority that good faith does apply at the post-contractual stage, in the form of Lord Clyde's statement in *The Star Sea*:

> "The special provisions which immediately follow section 17 may embellish the general rule which applies at the period of formation, but not be exhaustive of it. But that solution now appears to be past praying for. In these circumstances the alternative remains available of adopting a flexible construction of the concept of utmost good faith."[43]

However, historical and subsequent case law as well as academic commentators have failed to supply any concrete content of this duty, and it may be said that it has been entirely dismantled by developments subsequent to *The Star Sea*. In no particular order, *Goshawk v Tyser*[44] crystallises the reduction of good faith on a level of principle to something definitely less than an actionable duty, as seen also in authored works;[45] the post-contractual aspects of contractual compliance have been divorced from that doctrine;[46] and the Insurance Act 2015 curtails the statutory embodiment of good faith into a provision without any function other than interpretation.[47] On this basis, the truncation of s 17 of the Marine Insurance Act 1906 is in line with modern perceptions of the concept of good faith – it is explicitly defined as an interpretive principle by the Insurance Act 2015.

In modern insurance legal literature, the insistence on a separate pre-contractual and post-contractual good faith is quite universal and it is almost impossible to find any article or text book that considers

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[43] *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] UKHL 1, [2001] 1 All ER (Comm) 193.

[44] "It is rather that the duty [of good faith] informs the content of the contractual obligation at the time of contract"; *Goshawk Dedicated Ltd (suing for and on behalf of all members of Lloyd's Syndicate 102 & 2021 for the 1999 year of account) and others v Tyser & Co. Limited and another* [2006] EWCA Civ 54, [2007] Lloyd's Rep IR 224, per Rix LJ at [53].

[45] Philip Rawlings and John Lowry, 'Insurance fraud: the "convoluted and confused" state of the law', LQR 2016, 132, 96-119; Christopher Butcher, 'Good faith in insurance law: a redundant concept?' JBL 2008, 5, 375-384; Francis D. Rose, 'Informational asymmetry and the myth of good faith: back to basis' [2007] LMCLQ 181.

[46] See further Chapter 3.

[47] The new wording of the Marine Insurance Act 1906 is: "A contract of marine insurance is a contract based upon the utmost good faith." The author thanks Professor Rob Merkin QC for sight of forthcoming updates to Robert Merkin, *Colinvaux's Law of Insurance*, 10th ed (in press) where it is argued that section 17 has the potential to be very powerful as an interpretative principle, now that the remedy of avoidance has gone.

them together, under a single unifying principle – while nevertheless (if only for editorial purposes) grouping them under the single heading of good faith. The potential references are far too numerous to quote or footnote here, but it may perhaps usefully be illustrated. Thus the insistence with which the framework has been separated into a pre-contractual and a post-contractual element is well illustrated by one author who opined that it is

> "not surprising if the law imposed a duty not to present a fraudulent claim within the principles of good faith. The pre-contractual duties and the post-contractual duty applicable to claims would have the same goal, the prevention of fraud."[48]

The author of this quote[49] implicitly recognises the moral hazard component of good faith and asserts that the prevention of fraud meets with the same or at least similar obstacles at the "pre-contractual" and "post-contractual" stages, but does not refer the two aspects of the "duty of good faith" back to its origin in the concept of moral hazard.[50] He also considers a failure to apply the remedy of avoidance at the post-contractual stage a failure of policy rather than a failure of logic and principle.[51]

The concept of moral hazard, in turn, has undergone similar developments of inflation and explosion. It appears to have begun its life as one aspect of non-disclosure, complemented by the physical hazard.[52] Accordingly, there was a species of non-disclosure referring to the physical hazard, namely non-disclosures of matters referring to the risk itself, the real measure of risk that the ship succumbs to perils of the seas or that her equipment and procedures are not adequate for the insured adventure. The other species of non-disclosure referred to the insured's own moral standards and the risk that insurers be exposed to a conspiracy to submit a false claim. This was the position, and remains the analysis in modern times in English law,[53] under traditional rules and examples of required disclosure in historical cases. However in the course of the 20th century its perception changed fundamentally, it having been adopted by authors on law and economics and given a subtly different meaning to that of its origins.[54] This development means that moral hazard is now an ambiguous concept that requires stipulative definition before it can be legitimately used in an academic context.

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[48] Peter MacDonald-Eggers, 'Remedies for the failure to observe the utmost good faith' [2003] LMCLQ 249 at p 254.

[49] Discussing *Manifest Shipping Co. Ltd v Uni-Polaris Shipping Co. Ltd (The Star Sea)* [2001] UKHL 1, [2001] 1 All ER (Comm) 193; *The Mercandian Continent* [2001] EWCA Civ 1275, [2001] Lloyd's Rep IR 802; and *Agapitos v. Agnew (The Aegeon)* [2002] EWCA Civ 247; [2002] 2 Lloyd's Rep. 42.

[50] The author nevertheless goes on to argue that avoidance ought to be the appropriate remedy for the submission of a fraudulent claim.

[51] Peter MacDonald-Eggers, 'Remedies for the failure to observe the utmost good faith' [2003] LMCLQ 249 at 262.

[52] If one wanted to compile a complete catalogue of errors, one could probably add further categories such as the insured's (or more correctly the proposer's) credit rating and perhaps others.

[53] See prominently Robert Merkin et al, *Marine Insurance Legislation*, 5th ed (Abingdon: Informa 2014).

[54] Tom Baker, 'On the Genealogy of Moral Hazard', *Texas Law Review* (1996) Vol 75 Number 2, 237-292.

The original, historic concept of a separate moral and a physical hazard are not beyond reproach from a systematic and analytical point of view. While grouping types of risk is a non-analytical venture that must be considered free of reproach, deeper systemic analysis necessitates consideration of whether a particular failure to disclose is necessarily best analysed as related to moral hazard. Can the physical hazard really be said to constitute a completely separate concept, if the supervening act of failure to disclose in itself is always separately a moral hazard? Yes, but only in respect of innocent non-disclosure.[55] In such cases, there may be cases of failure to disclose a fact pertaining to the physical hazard which would not fall under the description of moral hazard. However, as soon as there is a non-innocent state of mind, any case can be analysed as one of moral or physical hazard. As an analytical tool, "the moral hazard" therefore has its limitations.

2.3.2 The existence of a post-contractual duty of good faith

The above has crystallised in recent years into a questioning of the very existence of a post-contractual duty of good faith by several commentators.[56] In the context of the law reform process, the Law Commissions in Issues Paper 7[57] closed on a general discussion of the existence and role of the post-contractual duty of good faith. In this connection it asked the following questions. Should clauses requiring the insured to notify the insurer about any increases in the risk be interpreted restrictively? Should the duty of good faith have no particular application to such clauses? Are there any advantages in legislating for such clauses along the lines set out in the Principles of European Insurance Contract Law? Should an insured's duty of good faith be confined to the duty not to make a fraudulent claim, or should it continue to have some general but unspecified effect?[58]

The outcome of the Law Commissions' deliberations on this matter was the reduction of the Marine Insurance Act 1906 by exclusion of the remedy, limiting the provision to a statement that an insurance contract is one of good faith. In addition, section 14(1) of the Insurance Act 2015 abolishes "[a]ny rule of law permitting a party to a contract of insurance to avoid the contract on the ground that the utmost good faith has not been observed by the other party". While the absence of a remedy means that post-contractual good faith arguably no longer has a life on its own, closure of the grand debate that followed *Black King Shipping Corp v Massie (The Litsion Pride)*[59] would probably, given the perceived risk of further judicial creativity, entail throwing out the concept of good faith originally

[55] Which at the pre-contractual stage attracts the same remedy as other forms of non-disclosure.
[56] Howard N. Bennett, *Mapping the doctrine of utmost good faith in insurance contract law* [1999] LMCLQ pp 165-222, Butcher, Christopher, *Good faith in insurance law: a redundant concept?* [2008] JBL 2008 375-384, Francis D. Rose, Informational asymmetry and the myth of good faith: back to basis [2007] LMCLQ 181.
[57] Issues Paper 7: The Insured's Post-Contract Duty of Good Faith (July 2010) ,
[58] List of consultation questions, page 78 of the Issues Paper.
[59] [1985] 1 Lloyd's Rep 437.

introduced by Lord Mansfield in its entirety. While there has been both judicial ambivalence[60] and academic reservations,[61] it is doubted whether this would be a constructive step: good faith regarded as a quality of the insurance policy and taking different guises as required by the context seems to this author to be a perfectly viable way forward.

The notion that s 17 of the Marine Insurance Act 1906 must necessarily apply to all instances of duties of good faith is soon to be a historical notion, but even in its lifetime was prominently put in question.[62] There indeed appears to be no reason, other than the lack of a mention of any other remedy in s 17, why the remedy ought to have been avoidance, and the mere suggestion perhaps demonstrated how far insurance law had come down an unprincipled and statute-focused route. In reality, there never appeared to be any compelling reason to interpret section 17 as applying comprehensively to post-contractual disclosure, and to say that its remedy is exclusive. Indeed, there appears to be no case law pre-dating the Marine Insurance Act from which one would draw the conclusion that a post-contractual lack of disclosure must always attract the same remedy as a pre-contractual one. The very cogent argument of Aikens LJ seeks to commandeer other remedies, resulting in a proposal that damages be again considered for employment as a remedy for post-contractual breaches of duty of good faith.[63] However, that remedy was rejected by the House of Lords in *Banque Keyser Ullman v Westgate*.[64] The amendments of the Insurance Act 2015 open new doors in this regard: avoidance is deliberately removed as a remedy both under s 17 of the Marine Insurance Act and for other forms of insurance, by s 14(1). The latter provision explicitly removes any existing remedy of pre—or post-contractual avoidance. Accordingly, the consideration of what remedy applies to post contractual duties is opened to renewed scrutiny with the development of a coherent set of remedies. Speculation on such developments is out of place here. However it is worth mentioning that future precedents on fraudulent claims may well consider that the rule and its new statutory remedy, to be discussed in the following chapter, fit into the redefined good faith concept.

2.3.3 Modern insurance law: the view from the moral hazard perspective

What is moral hazard? There are a number of definitions by authors in modern insurance law. Some are shorthand, some are tentative, some are stipulative – not all definitions cover the full meaning of the concept, and most fall short of encompassing the full and appropriate width of the concept.

[60] Eg in *The Star Sea* [2001] UKHL 1, [2001] 1 Lloyd's Rep 389, where Lord Clyde memorably said that the existence of the duty was "past praying for".

[61] See especially Francis D. Rose, 'Informational asymmetry and the myth of good faith: back to basis' [2007] LMCLQ 181.

[62] Notably by Aikens LJ in a lecture given to the British Insurance Law Association, published at Richard Aikens, 'The post-contract duty of good faith in insurance contracts: is there a problem that needs a solution?', [2010] JBL 379-393 .

[63] See also Peter MacDonald-Eggers, P., 'Remedies for the failure to observe the utmost good faith' [2003] LMCLQ 249-278.

[64] [1985] 2 Lloyd's Rep 1.

Without attempting a definition or settling on a narrow meaning of the concept, it will be appropriate first to review the various meanings of the concept in use in modern insurance literature. It will be seen that there is no single accepted definition of the concept in modern English insurance literature. This lack of coherency in relation to the concept of moral hazard is in turn arguably a contributing cause of a lack of deliberation on the grand construction and concepts of insurance law.

One author limits the scope of the concept to previous criminal convictions – in fairness without attempting a definition.[65] Another does provide a short and elegant definition: "an aspect of general human behavioural weakness, the risk of which the insurer is unable or unwilling to assume."[66] On the contrary, in *The Grecia Express*,[67] Colman J approved the underwriter's argument saying that "[the moral hazard] has nothing directly to do with the prospective incidence of an insured peril. Instead, it is relevant only to whether the proposer for cover will be an honest assured."[68] This definition falls short of assigning temporal or ethical aspersions to the concept, which as demonstrated by another author is intrinsic to the historical origins of the concept of moral hazard.[69] According to that author, the English historical insurance market embraced the concept of moral hazard as a means to distinguish insureds who presented an enhanced risk due to the identity of the insured.

A very pragmatic definition, focusing entirely on the actual usage of the term, is this:

> "Moral hazard is the phrase by which the insurance industry refers to material facts relating to the question of the moral integrity of the proposer rather than material facts about the subject-matter of the insurance. The greater the degree of control which the prospective insured has over the incidence of the risk prospectively to be insured against, the more concerned an underwriter will be about the moral integrity of his prospective insured."[70]

Although the first part of this definition is purely descriptive of the type of cases in which the concept moral hazard is used, elements of the economic effect of moral hazard are brought into the scope of the concept in the second half of the quoted text.

The next quote does in fact contain an attempt at a definition:

> "[I]t refers to the prospect of the assured himself acting in a way which would add to the risk to be insured in that a loss may be sustained through the fraudulent design of the assured,

[65] Francis D. Rose, *Marine Insurance: Law and Practice,* 2nd ed (London: Informa, 2012), para 5.50.
[66] Malcolm A. Clarke, *The Law of Liability Insurance* (London: Informa, 2013), para 10.2.
[67] *Strive Shipping Corp v Hellenic Mutual War Risks Association (Bermuda) Ltd (The Grecia Express)* [2002] EWHC 203 (Comm), [2002] 2 All ER (Comm) 213.
[68] At pp 460-461.
[69] Tom Baker, 'On the Genealogy of Moral Hazard', *Texas Law Review* (1996) Vol 75 Number 2, 237-292.
[70] Nicholas Ridley, Insurance against pecuniary loss, in Jonathan Mance, Robert Merkin and Ian Goldrein (eds), *Insurance disputes*, 3rd ed, (London: Informa, 2011.

> whether in the procurement of the loss or the fabrication or exaggeration of a claim; indeed, it might also refer, in the broad sense, to the unacceptability of contracting with dishonest assureds. The term may also refer to the prospect of fraud by another person which may cause loss to the assured; usually, such a person is intimately associated with the interest insured, such as the alter ego or a director of the assured, servants or agents of the assured (including an insurance broker), the master or manager of a ship, the manager of a business or a warehouseman."[71]

This definition focuses entirely on fraud by various persons including the insured and omits the aspect of increased carelessness by the insured. It also commingles what others have separated into the moral hazard pertaining to the insured and the physical hazard in relating to the subject-matter insured.

The same author identifies *Trading Company L & J Hoff* v *Union Insurance Society of Canton Ltd*, a case from 1929 as the earliest example of the use of the term and indeed this author has not found any earlier reference.[72] The case concerned insurance of bearer railway shares in transit. The shares never arrived in London. The plaintiffs' argument was that insurers must pay and be subrogated to salvage rights. It is a case of sue and labour in the context of the Russian Revolution. Lord Justice Scrutton referred to the plaintiff's statement:

> "the first reason, which he calls the moral hazard, which is this, which I am afraid is inherent in human nature, that there is a tendency if you are insured to a very high value not to be diligent in trying to get the thing back because you do so well out of losing the thing that it is rather a disappointment if you do not lose it; and the underwriter is entitled in the view of underwriters, and as I understand the law, to judge for himself whether he will take the risk of insuring a thing at a value so much higher than the present value of the thing insured that it will be a considerable gain to the assured if he does lose the thing. Now, that as I understand is the law."[73]

The conclusion here was that the value of the subject-matter insured ought to be disclosed as it was a factor in assessing the moral hazard. Scrutton LJ mentions the concept in citing counsel, but does not use it as conceptual guidance. The plaintiff's case is dismissed on the basis of failure to disclose the correct valuation of the shares. The issue of overvaluation in itself has been addressed in more recent case law.

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[71] Peter MacDonald Eggers, *Good Faith and Insurance Contracts* (3rd ed), (London: Informa, 2010), at para 15.25.

[72] At para 15.20 – the case identified is *Trading Company L & J Hoff* v *Union Insurance Society of Canton Ltd* (1929) 34 Ll L Rep 81.

[73] At page 89.

It is fair to note here that any definition drawn from case law is likely to quite legitimately be inaccurate or at least unrepresentative, given that the moral hazard is not a prescriptive but a descriptive concept and that therefore the concept advanced by an individual judge in a specific case is likely to be designed for the circumstances of the case. Greater demands may be made upon academic authors to attempt more widely comprehensive or at the very least useful definitions.

Some instances of use of the expression moral hazard manifestly do not constitute an attempt at defining the concept or are merely working definitions or descriptions of one aspect of the concept. What is manifest is that different users have a different understanding of the meaning of moral hazard. Some authors use the concept to refer to fraud only. In some instances it refers to a category of material facts, namely that relating to the insured as opposed to the subject-matter insured. Others again use a wider, economic definition of the concept, encompassing also the mechanics and impetus that the very existence of insurance has on the mind and actions of the insured, whether intentional or merely negligent.

Thus, the definition to note is entirely anodyne and void of attribution of negative moral qualities onto the insured. It refers uniquely to the mathematics of the insurance risks covered: "what is the nature of the incentive provided to the insured through the existence or provision of insurance?"[74] This definition stems from modern US economics and emphasises the insurer-side economics of the transaction, with a view to the large numbers and in a way perhaps more usually associated with reinsurance rather than with direct insurance where the actual risk itself is under scrutiny in the underwriting process. Being economic rather than legal in character, this definition does not explicitly note the tools and measures available to the insurer to correct an economic imbalance, but the inference is that on the subjective level, a perceived imbalance should lead the individual insurer to amend the contract terms or the premium required to accept the risk offered.

The review of the concept of moral hazard that this author finds most appealing is that of Baker.[75] It clarifies that while the concept of moral hazard has its origins in Victorian social values and the view that gambling is an intrinsic evil, it has in modern times come to be an anodyne concept of no real use except to carry the implication that the insurer may wish to perform some form of selection or vetting of its insureds. It may even be used to state that the (or an) insured is likely to commit fraud, without actually using the morally tainted word fraud.

However, a principled definition of moral hazard would arguably be at odds with usage: referring again to the 19th century usage described by Baker, English court cases appear to use moral hazard not

[74] Tom Baker, 'On the Genealogy of Moral Hazard', *Texas Law Review* (1996) Vol 75 Number 2, 237-292.
[75] Tom Baker, 'On the Genealogy of Moral Hazard', *Texas Law Review* (1996) Vol 75 Number 2, 237-292.

primarily as a concept needing definition or capable of influencing thought processes, but as a convenient header.[76]

It must be concluded that modern available definitions of the concepts of good faith and moral hazard, and their usage in modern English insurance literature are not consistent or indeed terribly useful analytical tools. While it would most likely be possible to establish clear, single concepts, that is not the direction in which modern law is pointing. The modern law of insurance does not seek clarity derived from an underlying principled framework. Instead, certainty is expected to arrive from legislation and the regulatory framework. There is increasing denunciation or disregard for overriding concepts in the form of greater principle. This is by no means surprising in an era of large-scale grass roots participation in the global society – for better and for worse – as well as the capacity and propensity for detailed regulation deriving from EU as well as domestically.

2.4 Conclusion with perceptions

The current situation as well as the future of English and Welsh insurance contract law is the result of a multitude of historical and political influences. This Chapter has attempted to set out, by way of introduction, a 360 degree view of the policy ambient of the law and some current influences, and to assess the current position of recent reforms. It has been an assumption of the author that the law has contained uncertainties and injustices. Indeed, the initial impetus of the research project was a curiosity about the extent to which these injustices could be traced to the law on fraudulent claims and its wider good faith context, and to establish the causal relationships at work. While this was not seriously pursued as a line of inquiry, on the basis that the relationship, while present, was unverifiable and unquantifiable in real terms, the concepts of moral hazard and information asymmetry appeared to retain some usefulness – however the author did not find morally satisfaction that the existing conceptual framework of good faith and moral hazard formed a solid foundation from which to extrapolate a coherent and clear system of current law. The understanding of the concepts among commentators is too variable and the historical framework - in this author's understanding - lacks the teeth or reach to become a valuable source of interpretation of modern legislation and other modern rules. This author is not convinced that historical sources and framework are there to begin with. It is not overstating the matter to say that older treatises on insurance law do not seem to take much interest in cross-cutting principles – much like the case law of the time, they focus on precedent and on the wording of the contracts themselves. Marshall[77] in his chapter on illegality does not refer to non-insurance case law or principles. His chapter on fraudulent claims is largely directed to

[76] A prominent example occurring in Robert Merkin et al, *Marine Insurance Legislation*, 5th ed (Abingdon: Informa 2014).
[77] Samuel Marshall, *Treatise on the law of insurance*, 2nd ed (London: Butterworth, 1808) at 645 onwards.

criminal statute. Perhaps a lack of principle in modern law is owed to a lack of early principle and alignment with general contract law and general principles of fraud?

The project from this point on must therefore be to discover the content of the law without reference to concepts such as moral hazard or good faith, on the understanding that they are insufficiently precise to contribute to the understanding of the law as outlined.[78] The aim has instead become to establish a bare-bones understanding of the law on fraud, its deficiencies and insufficiencies, and what alternative measures insurers take where the obvious route of pleading fraud in the civil litigation is unavailable. To begin to discover the law in this regard, the first issue to consider must be the substantive, factual and basic law on fraudulent claims. As will be set out in the following, that law itself has developed and crystallised surprisingly recently, the previous uncertainty causing effects that will be discussed in the subsequent two chapters.

[78] By way of aside, another point where insurance law has developed in parallel to other fields of law is tort law, where *Leyland Shipping* is lacking the influence it might have on tort law. This is not the place for analysis of that point.

3 The law on fraudulent claims

Having set out several aspects of the background and policy relevant to insurance contract law as it stands today, including perceived deficiencies and needs for reform, it is appropriate next to give an overview of the law on fraudulent claims as it currently stands.[79] As noted above, the author's view is that the law on this point has had a profound impact on the current state of insurance contract law generally, and that many of the perceived deficiencies and the ensuing need for reform have their root in this sole aspect of the law. However this chapter can hopefully demonstrate that the substantive law on fraudulent claims is now as clear as one could ever hope for it to be, so that it should not continue to contribute to a skewing of other concepts of law. This chapter will attempt to set out in full the law on insurance fraud at its present stage of development. It is at first glance certainly surprising that the law on fraudulent claims has crystallised as comparatively recently as it has.

The law underwent partial reform in February 2015 when the Insurance Act 2015 was enacted. The entry into force date is 12 August 2016. While the Act reforms the law on pre-contractual disclosure in the round, the part of the Act pertaining to fraudulent claims is mostly designed to codify the law in place at the time of enactment. The Act appears to do little more than codify current case law, such as it is.[80] Much of the following discussion will therefore centre on the law in place up until 12 August 2016; simply because it will continue to be in force afterwards.

3.1 Summary introduction with typology

It would be convenient to start with a definition of fraudulent claims, accompanied by breakdown of the various types of fraudulent claim. However it is a striking feature of the law on this point that there is no generally valid legal definition of a 'fraudulent claim' – case law has failed to provide and the Insurance Act 2015 equally falls short of supplying a definition: the definition of fraudulent claims was not addressed at all, quite possibly because of the pending appeal in *Versloot*. However there is a generally accepted typology of insurance fraud, set out by Mance LJ as recently as in *Agapitos v Agnew*.[81] A typology is in some ways more helpful than a definition – in the context of alternative remedies, it will sometimes be pertinent to note what type of insurance fraud was at issue in the primary claim.

In particular the fate of the rule on fraudulent means and devices[82] was left entirely unaddressed by section 12 of the Insurance Act 2015. The explanation for this omission is that at the time of the

[79] An earlier version of much of this chapter was published at Johanna Hjalmarsson, 'The law on fraudulent insurance claims' (2013) JBL 1, 103-117.
[80] These views were first expressed along similar lines by the author in Hjalmarsson, 'Insurance Act 2015 – a new beginning or business as usual?', Shipping & Trade Law (2015) STL 15(2) p 4.
[81] [2002] EWCA Civ 247, [2002] 2 Lloyd's Rep 42.
[82] *Infra*.

hearings of the Special Committee hearings in December 2014, where the Act was finalised, the Court of Appeal's judgment in *Versloot Dredging BV v HDI-Gerling Industrie Versicherung AG (The DC Merwestone)*[83] was the subject of an application for leave to appeal. While the Act therefore embodies a radically new approach to disclosure and contract terms, in this part the Act represents succinct clarity but perhaps not an unambiguously successful reform.

There had been comprehensive consideration of the law before the statute was finalised. It is therefore appropriate briefly to consider the Law Commissions' Issues Paper 7.[84] The paper was issued in July 2010 and comments were invited by 11 October 2010.[85] It provided an overview of the existing state of the law and went on to cover the definition of fraud; the appropriate remedy for fraud; the law applicable to co-insureds and group insurance; and closed with a general overview of the post-contractual duty of good faith. The Paper went on to set out the early thinking of the Law Commissions on proposals for reform, closing with a list of further questions to which responses were invited. Foreshadowing the subsequent outcome embodied in the Insurance Act 2015, the Law Commissions posited with regard to the definition of fraud that the law would be best left to the courts to develop, and that it did not require statutory reform. Accordingly, the Insurance Act 2015 sets out the remedies for fraudulent claims in terms of the effect on the claim and the contract, in individual insurance and group insurance, but does not go much further.[86] This author has argued against the need for legislation and accordingly generally approves of the minimalist approach so adopted.[87]

3.1.1 What is a fraudulent claim?

Legacy provides no assistance on the definition of a fraudulent claim. As noted above, early text books do not consider fraudulent claims a valid category but refer merely to wilful misconduct as a cause to reject the claim. While the modern approach is to rely on cross-cutting principles and maxims, or to borrow from other parts of the law on obligations, it appears likely that an honest project of historical attribution to theory underpinning the law of post-contractual fraud is doomed to fail. The approach in this chapter will therefore be to describe the law from the bottom up, as it were, starting with an attempt at setting out (in the absence of a persuasive accepted definition) the categories of loss that may fall under the heading of fraudulent claim in terms of a typology rather than defined sub-categories. The law unquestioningly recognises a few different kinds of insurance

[83] [2014] EWCA Civ 1349, [2015] 1 Lloyd's Rep 32.
[84] What follows is in part based on Johanna Hjalmarsson 'Fraudulent insurance claims', Shipping & Trade Law (2010) Vol 10(7) pp 3-5. The article was cited by the Law Commissions in the report Insurance Contract Law: Summary of Responses to Issues Paper 7: The Insured's Post-Contractual Duty of Good Faith, December 2010 at pages 1 and 4.
[85] Issues Paper 7 is available to download from the Law Commissions' web site www.lawcom.gov.uk (accessed 8 September 2010).
[86] Insurance Act 2015 sections 12 and 13.
[87] Johanna Hjalmarsson, 'Fraudulent insurance claims' Shipping & Trade Law (2010) Vol 10(7) pp 3-5.

claims: an entirely fraudulent claim; a genuine claim fraudulently exaggerated; or the insured may have subsequently discovered that there was in fact no loss or that the loss was smaller than originally thought; or the loss may be brought based on false information.[88] These may manifest themselves in a number of different ways.

The first and most obvious is that the insured presents a claim where there has in fact been no loss at all. Such a claim is false from beginning to end: the ship is safe, the cargo has been recovered, or there never was any loss event at all – but the insured decides in any case to claim.[89]The complete absence of any loss has scarcely presented any legal or definitional intricacies – it will be a matter of evidence how the case is resolved.

The second type is that the insured has suffered a small loss, but decides to exaggerate the loss and claim for a larger amount; *Galloway v Guardian Royal Exchange*.[90] Some exaggeration is permissible and indeed expected by way of negotiation, but the line was drawn in in *Galloway v Guardian Royal Exchange*.[91] A burglary had resulted in the theft of a number of household items to the value of about GBP 16,000 – the genuine loss. Mr Galloway claimed for that loss and falsely added GBP 2,000 said to be in respect of a stolen computer. The question was if the insurer could decline to pay and if so what amount. If the common law rule on fraudulent claims applied, it was clear that the insured could not recover; however there was no such provision in the policy. The Court of Appeal surmised that even in the absence of an express provision in the policy, there was a common law rule on fraudulent claims which required the insured to claim in good faith. As for what part of the claim could be rejected, the Court of Appeal rejected a mathematical approach based on the size of the false claim compared to that of the true claim, because adopting that approach would result in the absurd rule that a larger genuine claim would also allow for a larger fraudulent claim. The Court also politely disagreed with the apportionment approach in *Orakpo v Barclays Insurance Services*,[92] wherein it had been held that there must be fraud to a "substantial extent". According to the court in *Galloway*, we must "*consider the fraudulent claim as if it were the only claim and then to consider whether, taken in isolation, the making of that claim by the insured is sufficiently serious to justify stigmatising it as fraud*."[93] In other words, we must look not at the size of the fraud but at the blameworthiness of the conduct of the insured. There are nevertheless also decisions emphasising the proportion of the total claim, and it has never been judicially doubted that the *de minimis* rule applies; although actual support for this hypothesis is weak.

[88] Philip Rawlings & John Lowry, supra fn 45 note two categories – at page 96. The number of categories is open to each author's definition as the position is necessarily descriptive.
[89] The design of the forfeiture rule, *infra*, means that it has almost no impact in such a case.
[90] [1997] Lloyd's Rep IR 209.
[91] [1997] Lloyd's Rep IR 209.
[92] [1995] LRLR 443.
[93] *Galloway v Guardian*, per Millett LJ, page 214 col 2.

However, in practice the position in respect of exaggerated claims is not so straightforward. It has been said[94] that where the insured makes an inflated claim not with the intention to deceive the insurer, but with the intention of setting up a good initial negotiating position for himself, in the anticipation that insurers will object to parts of the claim and the valuation of the loss. Clearly it will be very difficult in practice to distinguish between a fraudulently exaggerated claim, and a claim inflated with the intention to later negotiate the value of the claim. Nevertheless, this only applies to the figures of the claim – an invented portion of a claim is always fraudulent.

Thirdly, the insured may have submitted information that has subsequently become incorrect, for instance because part of the subject-matter insured has been recovered, or circumstances have otherwise changed; *Piermay Shipping Co SA v Chester (The Michael)*.[95]

Fourth, the insured may be aware of some defence that the insurers could use, if they were aware of it, but elect not to inform insurers about it. The deliberate suppression of a defence is considered by some a type of fraudulent claim, although this has not been tried in court. Some authors consider that in the absence of deliberate suppression amounting to misrepresentation, there is no fraudulent claim.[96] Others prefer to include this as a separate category of fraudulent claim, so that if the insured suppresses some defence on which the insurers would be entitled to rely, the insurer has the choice of whether to invoke the fraudulent claims rule or the remedy applicable to the suppressed defence.[97] This category of fraudulent claim may well be technically redundant. The issue of its existence need not be resolved here.

Fifth, the loss or damage may have been self-inflicted. While in such a case a loss has actually happened, this is not a true recoverable loss due to the fact that a self-inflicted loss is not a fortuitous event and the insurer is not liable under the policy; and furthermore the insured can justifiably be accused in such a situation of wilful misconduct. This type of claim may appear akin to the first category, non-existent loss, but is perhaps more similar to the category of suppression of defence.

Finally, the most recently emerging category of fraudulent claim is an entirely genuine claim, supported by 'fraudulent means and devices'. This category merits its own header and will be dealt with in the following.[98]

For each of these types of fraudulent claim, the rule has emerged that the whole claim is forfeit. This rule is not considered new, yet it may be said that it was only finally confirmed in *Agapitos v Agnew*[99]

[94] In *Orakpo v Barclays Insurance Services* [1995] LRLR 443.
[95] [1979] 2 Lloyd's Rep 1.
[96] Howard N. Bennett, *The Law of Marine Insurance*, 2nd ed (Oxford: OUP, 2006), at paragraph 22-83.
[97] Robert Merkin, *Colinvaux' Law of Insurance,* 9th ed (London: Thomson Reuters (Legal) Ltd, 2010) at para 9-028.
[98] See under 3.1.2

and that before that case, there was doubt as to whether section 17 of the Marine Insurance Act 1906 and a duty of good faith somehow influenced the outcome. Be that as it may, the common law rule on fraudulent claims now applies to the effect that the invented or fraudulently exaggerated claim is forfeit. The same applies to claims supported by fraudulent means and devices – although genuine, they are defeated in their entirety.[100]

3.1.2 Fraudulent devices

The category of claims supported by fraudulent means and devices as a defined phenomenon, if not the practice,[101] originated with the judgment of the Court of Appeal *Agapitos v Agnew* [102] and remains hotly contested.[103] Bringing a genuine claim in reliance on false evidence became known as the use of 'fraudulent means and devices' and was, following this case, equally subject to the rule on fraudulent claims. The inclusion of fraudulent means and devices into the fraudulent claims rule was heavily circumscribed:

> "the courts should only apply the fraudulent claim rule to the use of fraudulent devices or means which would, if believed, have tended, objectively but prior to any final determination at trial of the parties' rights, to yield a not insignificant improvement in the insured's prospects"[104]

This nevertheless constituted a victory for insurers, albeit not a terribly useful one in a context where a plea of fraud was not a straightforward matter.[105] The promotion of a claim by 'fraudulent means and devices' is thus now regarded as a fully-fledged fraudulent claim. What is meant here is the promotion by fraudulent means, such as the submission of forged evidence, of an *originally genuine* claim. In *Agapitos v Agnew (The Aegeon)*,[106] Mance LJ set out the parameters for a claim promoted by fraudulent means and devices to be considered fraudulent. The case concerned marine insurance for a passenger ferry laid up for maintenance. It was warranted that the ship would not undergo any

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[99] [2002] EWCA Civ 247, [2002] 2 Lloyd's Rep 242.

[100] What is not clear is if the development of this rule was influenced by forfeiture in the common law more generally, as also illustrated by the rule, well-known from murder mystery puzzles, that a person responsible for the death of another cannot inherit their property. Both appear to have developed as modern day descendants of the *ex turpi causa non oritur actio* maxim; perhaps a suitable topic for another thesis. For general treatment, see Peter MacDonald-Eggers QC, *Deceit: The Lie of the Law* (London: Informa Law, 2009).

[101] In evidence in many prior cases not least the early case *Lek* v *Mathews* (1927) 29 Ll L Rep 141.

[102] [2002] EWCA Civ 247, [2002] 2 Lloyd's Rep 42.

[103] The author is at a disadvantage in not having seen the final word of the Supreme Court in *Versloot Dredging BV v HDI-Gerling Industrie Versicherung AG (The DC Merwestone)* [2015] 1 Lloyd's Rep 32 , to be heard in March 2016.

[104] *Agapitos v Agnew* [2002] EWCA Civ 247, [2002] 2 Lloyd's Rep 42, at [38], per Mance LJ.

[105] *Infra*.

[106] [2002] EWCA Civ 247, [2002] 2 Lloyd's Rep 42.

'hot works'[107] until a Salvage Association certificate had been obtained. The owner proceeded with the hot works and the ship caught fire. The insured sought to conceal the breach of warranty by submitting a forged affidavit to the effect that no hot works had been undertaken. The claim was thus genuine, but the insured had sought to sustain it by this forged piece of evidence. Mance LJ defined fraudulent devices as follows.

> "A fraudulent device is used if the insured believes he has suffered the loss claimed, but seeks to improve or embellish the facts surrounding the claim by some lie."[108]

He stipulated that (i) the false statement must be directly related to the claim; (ii) it must be intended to improve the assured's position; and (iii) it must, if believed, be capable of improving the assured's position; see *Agapitos v Agnew*.

There is a clear logic behind bringing claims promoted by fraudulent means and devices in under the fraudulent claims rule, because sometimes it is not clear on the evidence precisely what elements of the claim are genuine, and whether the fraud was contemporaneous or subsequent. However the rule is open to criticism on the basis that the outcome for an honest insured is quite disproportionate.

There is ultimately a difference between fraudulent claims and claims supported by fraudulent means and devices in that the latter place the insurer in a radically different position. In order to prove fraud, the insurer may find itself obtaining and presenting proof on such elusive matters as the financial situation of the assured, previous losses of a suspicious nature and whether financial incentives ought to lead the judge to consider that a fraud was likely. In relation to fraudulent means and devices, the situation is quite different. Whether or not the underlying claim is genuine, the burden of proof may well be fulfilled *a priori* by just comparing a submitted forged document with a ledger or other written evidence. It has even been said that cases of fraudulent means and devices are suitable candidates for summary judgment.[109] It is therefore reasonable to suggest that this element of the doctrine on fraudulent claims is motivated at least in part by a need to make the law on fraudulent claims more readily accessible to insurers in spite of the difficulties with the standard of proof to be described in the following.[110]

3.2 The 'common law rule' on fraudulent claims

While the duty of disclosure and the duty not to misrepresent facts to the other party at the time of making the insurance contract are expressions of the doctrine of good faith as it applies to insurance

[107] Welding.
[108] At [30].
[109] *Interpart Comerciao e Gestao SA v Lexington Insurance Co* [2004] Lloyd's Rep IR 690; wherein nevertheless summary judgment was refused because the law on fraudulent claims was under development.
[110] Chapter 4, especially 4.3.

contracts, the duty not to misrepresent at a later stage, after the contract has been concluded and in the making of a claim, cannot as obviously be described as an expression of that same doctrine.[111] It should be mentioned here for completeness' sake that there is a further issue for analysis namely whether the rule on fraudulent claims falls under the duty of utmost good faith.[112] That debate appears to have achieved a resolution to the effect that good faith does not affect the content of the fraudulent claims rule or its operation. While there was for some time a perception that there was a contractual duty of care under the banner of good faith not to make a fraudulent claim, that is not the favoured statement of the law at present. Therefore, while the question is interesting, it – perhaps surprisingly – has no real bearing on the content or operation of the rule on fraudulent claims in modern law and will therefore not be discussed further in this chapter; although it returns below in the specific context of the burden of proof.[113]

Not to overstate the doctrinal basis of the common law rule of fraudulent claims, the rule may at a minimum be said to arise out of a duty at common law not to make fraudulent claims, which found expression historically in a clause in the policy stating the consequences of making a fraudulent claim.[114] If a claim is submitted fraudulently, the whole claim, including any genuine part, is forfeited. The reason is as stated by Lord Hobhouse in *The Star Sea*:[115]

> "The fraudulent insured must not be allowed to think: if the fraud is successful, then I will gain; if it is unsuccessful, I will lose nothing."[116]

The modern rule is loosely related to the common law principle that no man may profit from his own wrong – *ex turpi causa non oritur actio*; but the genealogy is far from clear – modern authors do not generally refer to or rely on the maxim. Historical sources consider fraudulent claims only in the context of criminal law, appearing to consider rejection of the claim based on wilful misconduct the only available paradigm for fraudulent insurance claims, with pre-contractual fraud being the only species of fraud that leads to avoidance.[117] Instead of the *ex turpi causa* maxim, modern discourse has focused instead on the analysis necessary to detach fraudulent claims from the avoidance rule in

[111] What follows is based on the author's synopsis of her presentation at the 37th Maritime Law Short Course on 7 September 2010 in Southampton. The synopsis was distributed to course delegates and is archived in the Philippa Kaye Library of the Institute of Maritime Law.
[112] See pro *Shah v Ul-Haq* [2009] EWCA Civ 542, [2010] 1 All ER 73 and contra *Agapitos v Agnew* (CA) [2002] EWCA Civ 247, [2002] 2 Lloyd's Rep 42 and *Axa v Gottlieb* [2005] EWCA Civ 112. There is more detailed discussion of these cases above at pages 46 to 49.On fraudulent claims and good faith, see Malcolm Clarke, *Lies, Damned Lies and Insurance Claims*, 2000 NZLRev 233-261.
[113] Chapter 4, especially 4.2.
[114] On the common law rule of fraudulent claims, and foreshadowing much of what has since been decided, see Clarke (2000).
[115] [2001] UKHL 1, [2001] 1 All ER (Comm) 193.
[116] *Per* Lord Hobhouse at [62].
[117] Marshall, Samuel, Treatise on the law of insurance, 2nd ed (London: Butterworth, 1808), pages 556- 558.

section 17 of the Marine Insurance Act 1906 and its unfitting remedy of avoidance. An early statement of the rule in this guise and its policy background is found in *Britton v Royal Insurance Co*:[118]

> "It would be most dangerous to permit parties to practise such frauds, and then, notwithstanding their falsehood and fraud in the claim, to recover the real value of the goods consumed. And if there is wilful falsehood and fraud in the claim, the insured forfeits all claim upon the policy."[119]

Accordingly, modern law recognising a common law rule (of uncertain theoretical origin) relies on arguably anecdotal historical case law to underpin a common law rule and the hypothesis that a punitive element finds its place in the law on fraudulent claims.[120] These are well founded in a modern systematic and legislative context, but the author retains a doubt as to whether the legacy foundation can genuinely underpin such considerations. Fortunately the Insurance Act 2015 removes the relevance of such doubts by creating the punitive element and creating a context in which a punitive rule can legitimately operate.[121]

3.2.1 Source of the rule: contract clauses

The common law rule on fraudulent claims cannot be found in the Marine Insurance Act. It is unknown why it was not included, although it was well established by the nineteenth century. It is possible that it was not included because it is not a rule applying specifically to *marine* insurance; or alternatively because the fate of fraudulent claims is usually settled by contract clauses. The first sources or perhaps expressions of the common law rule were in fact clauses contained in insurance contracts. Virtually every policy contains these, so that historically there was no particular need for case law to elaborate on the rule of law. As a result of this usage, the rule has developed slowly over the years. Reference may again be made to the early source of *Britton v Royal Insurance Co*,[122] where Willes J said the following.

> "It is the common practice to insert in fire-policies conditions such that they shall be void in the event of a fraudulent claim; and there was such a condition in the present case. Such a condition is only in accordance with legal principle and sound policy."[123]

[118] (1866) 4 F&F 905.
[119] At page 909.
[120] The validity of the approach has been recognised in the context of procedure by Adrian Zuckerman, 'Must a fraudulent litigant be allowed to think: if the fraud is successful, I will gain much; if it is not, I will still recover my legitimate claim?', C.J.Q. 2011, 30(1), 1-14 .
[121] See further on the remedy under 3.4 below.
[122] (1866) 4 F&F 905.
[123] At page 909.

Clauses may variously provide for forfeiture of the fraudulent claim, forfeiture of the benefit of the policy from the date of the fraud, forfeiture of the benefit of the policy from the date of the claim and forfeiture in respect of the benefit *ab initio*. In the case *Michael Phillips Architects Ltd v Riklin,*[124] the clause was very simple:

> ***Clause 8 Fraudulent Claims***
>
> If you make any claim which is fraudulent or false, the policy shall become void and all benefit under it will be forfeited.
>
> ***Clause 9 Cancellation***
>
> "(c) The insurer may cancel the policy immediately…and reclaim any payments made under the policy, if
>
> …
>
> (iv) you make any claim which is fraudulent or false

Clauses are not always precisely drafted. In this example, it may be noted that the first provision states that the policy shall become void – this looks like an automatically ensuring consequence of the fraud; but the policy then appears to contradict itself in that according to clause 9, the insurer is apparently also entitled to cancel, which would not be necessary if the policy were really void.

Marine insurance contracts, including liability insurance contracts, do not tend to include any such clause. However it is worth noting clause 45 of the International Hull Clauses 2003 (IHC 2003):

> 45.1 The Assured shall, upon request and at their own expense provide the Leading Underwriter(s) with all relevant documents and information that they might reasonably require to consider any claim.
>
> 45.2 Upon reasonable request, the Assured shall also assist the Leading Underwriter(s) or their authorised agents in the investigation of any claim, including but not limited to
>
> 45.2.1 interview(s) of any employee, ex-employee or agent of the Assured
>
> 45.2.2 interview(s) of any third party whom the Leading Underwriter(s) consider may have knowledge of matters relevant to the claim
>
> 45.2.3 survey(s) of the subject matter insured
>
> 45.2.4 inspection(s) of the classification records of the vessel.

[124] [2010] EWHC 834 (TCC), [2010] Lloyd's Rep IR 479.

Clauses 45.1 and 45.2 are wide-ranging and have justifiably been seen as attempting to impose a general duty of disclosure upon the insured, so that not just an attempt at fraud, but also a lack of disclosure would entitle insurers to a remedy. This is what applies in the pre-contract context but it is generally considered that different concerns apply in the post-contract context.

As for the remedy, clause 45.3 provides:

> 45.3 It shall be a condition precedent to the liability of the underwriters that the Assured shall not at any stage prior to the commencement of legal proceedings knowingly or recklessly
>
> 45.3.1 mislead or attempt to mislead the Underwriters in the proper consideration of a claim or the settlement thereof by relying on any evidence which is false
>
> 45.3.2 conceal any circumstance or matter from the underwriters material to the proper consideration of a claim or a defence to such a claim.

The reference to the commencement of litigation is recognition of the validity of the conclusion in *The Star Sea*.[125] The clause curiously does not stipulate what is to happen to the contract itself, that is whether it is to be terminated or not. One possible interpretation is that the policy is to remain in force so that there is no question as to the insurer's entitlement to the premium, but that the insurer is not to incur any further liability thereunder. The IHC 2003 have not been widely adopted, possibly because of cll 45.1 and 45.2 above, so judicial clarification may not be forthcoming on this point.

3.2.2 Limits of the rule

The rule on fraudulent claims is not applied to attempts at fraud that are committed once litigation has been commenced. The rule in this regard is the same as that for post-contractual good faith generally; see *The Star Sea* wherein it was decided that upon commencement of litigation, procedural rules on disclosure and on perjury replaced any good-faith obligations the parties might have under the insurance policy. We will return to this rule in a later chapter when considering alternative proceedings.[126]

It has also been decided that a settlement agreement has the same effect as the commencement of litigation; *Direct Line Insurance Plc v Fox*.[127] A man had achieved a settlement with his insurer according to which he was to be paid a sum of money following a fire in his kitchen. According to the settlement agreement, Mr Fox had to substantiate part of the sum in question by submitting an invoice

[125] [2001] UKHL 1, [2001] 1 All ER (Comm) 193; see immediately below.
[126] See chapter 5.
[127] [2009] EWHC 386 (QB), [2009] 1 All ER (Comm) 1017.

from builders. The invoice was provided but was discovered to be fraudulent, and the insurer asserted that it was entitled to decline to pay the whole settlement according to the common law rule on fraudulent claims. The Judge however held that the claim could only be partially avoided, because the fraud had taken place after the claim had been compromised by settlement and the rule no longer applied. The principled basis for the outcome was that a settlement agreement is not subject to any duty of good faith.[128] It would seem that insurers should be advised not to finalise their settlement until all the documentation has been presented.

Finally, as to the limits of application of the rule on fraudulent claims, it has been suggested that a retraction of a fraudulent claim by the insured ought to result in mitigation of the rule, on the basis that this would encourage honesty,[129] but this has been judicially rejected in *Direct Line Insurance Plc v Fox*.[130]

3.2.3 Nature of the rule

The origin and nature of the common law rule on fraudulent claims has not to date been satisfactorily analysed – perhaps as a result of collective relief when the *Litsion Pride* conundrum was finally given a workable resolution. The obvious assumption is that the rule has something to do with the good faith nature of the insurance contract, however this is far from obvious. As noted above, a candidate providing arguably a more principled foundation, but which must probably be confined to history, is the *ex turpi causa* maxim.

The Court of Appeal in *Shah v Ul-Haq*[131] declined to apply the same rule to a partially fraudulent claim in tort, made against a negligent driver by a person posing as a victim of a car crash. The rule was said to apply to insurance contract claims only, and to exist for the specific reason that insurance contracts were contracts of good faith. Against that, there are also several cases where fraudulent claims have been said not to fall under the "duty of good faith", namely *The Star Sea*,[132] *Agapitos v Agnew*[133] and *Axa v Gottlieb*;[134] however, there is also clear support for the view that the rule on fraudulent claims is somehow related to the character of the insurance contract as one of good faith in an early case, namely *Britton v Royal Insurance Co*,[135] wherein Willes J said notably that

[128] Demonstrating the ambivalence in the approach of the judiciary to the concept of good faith.
[129] See D. Rhidian Thomas, 'Fraudulent insurance claims: definition, consequences and limitations' [2006] LMCLQ 485.
[130] [2009] EWHC 386 (QB), [2009] 1 All ER (Comm) 1017.
[131] [2009] EWCA Civ 542, [2010] 1 All ER 73.
[132] [2001] UKHL 1, [2001] 1 Lloyd's Rep 389.
[133] [2002] EWCA Civ 247, [2002] 2 Lloyd's Rep 42.
[134] [2005] EWCA Civ 112, [2005] Lloyd's Rep IR 369.
[135] (1866) 4 F&F 905.

> "The law upon such a case is in accordance with justice, and also with sound policy. The law is, that a person who has made such a fraudulent claim could not be permitted to recover at all. The contract of insurance is one of perfect good faith on both sides, and it is most important that such good faith should be maintained."[136]

It is not yet obvious how these judicial statements may be reconciled.[137] The reasoning goes as follows. The insurance claim is a contractual claim, whether it is made by the insured itself or by a third party, based on the liability in tort incurred by the first party. The liability claim is a claim based on a contract or tort that is by definition separate to the insurance contract. The former involves considerations, or so we are informed by the law, of good faith given that an insurance contract is a contract *uberrimae fidei*. However, insurance claims cannot be entirely independent of the underlying tort – there ought to be some sort of inter-relationship between the tort committed and the insurer's liability under the policy. Therefore, where there is a *bona fide* claim in tort which nevertheless involves a breach of good faith duties, should that affect the rights of the insurer under the insurance policy, or should the two be seen as entirely separate? The issue has been broached a few times[138] but never satisfactorily resolved.

If the fraudulent claims rule is a common law rule stemming ultimately from the *ex turpi causa non oritur actio* rule, the resolution to this conundrum is simple – whoever has sullied their hands will be unable to recover in tort or in contract. However that does not appear to be the resolution favoured by Smith LJ in *Shah v Ul-Haq*, where she specifically made the point that insurance claims are subject to good faith duties and must be distinguished from tortious duties. The hypothesis of striking out a claim in tort was tested in *Shah v Ul-Haq & Ors*[139] but rejected. The main issue was whether a claim could be struck out for dishonesty under the procedural rule CPR 3.4(2). As it happened, it could not, but Lady Justice Smith, giving the leading speech, also considered whether it could be done as a matter of substantive law. She said as follows.

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[136] At page 909.

[137] While the substantive law of tortious claims and insurance claims appears to diverge, a similar effect was achieved by procedural means in *Fairclough Homes Ltd v Summers* [2012] UKSC 26, [2013] Lloyd's Rep IR 159; although the rule stipulated is perhaps a little more on the restrictive side than that applied in insurance contract law. The Supreme Court decided that the court has power under the CPR and under its inherent jurisdiction to strike out a statement of case at any stage of the proceedings, even when it has already been determined that the claimant is in principle entitled to damages in an ascertained sum; setting the scene for the striking out of claims in tort. However, the Supreme Court also concluded that the power to strike out under CPR 3.4(2) should only be exercised where it is just and proportionate to do so, and therefore only in very exceptional circumstances not including the case before the Supreme Court on that day (*Fairclough v Summers* at [65]).

[138] *Shah v Ul-Haq* [2009] EWCA Civ 542, [2010] Lloyd's Rep 84, *Fairclough Homes Ltd v Summers* [2012] UKSC 26, [2013] Lloyd's Rep IR 159.

[139] [2009] EWCA Civ 542, [2010] Lloyd's Rep 84.

> "I had thought that the only circumstances in which a genuine claim would be dismissed on account of dishonest exaggeration were where the claim was based on an insurance contract: see *Axa General Insurance Ltd v [Gottlieb]* [2005] EWCA Civ 112, in particular Mance LJ's discussion of authority at paragraphs 17 et seq. There is a well established common law rule that if a genuine claim made under an insurance contract is dishonestly exaggerated, the whole claim will be dismissed; further, if money has already been paid pursuant to a claim under such a contract before the fraud is discovered, all the sums paid under that claim will be recoverable by the insurer, including any sum referable to the genuine part of the claim. However, this rule is limited to claims brought under insurance contracts, which are, of course, contracts of good faith. If there were a general rule of law, whether in contract or tort, that the dishonest exaggeration of a genuine claim would result in the dismissal of the whole claim, there would be no need for a special rule applying to contracts of insurance."[140]

Lady Justice Smith and her peers in the Court of Appeal thus characterised the forfeiture rule as an emanation of the special quality of insurance contracts as being contracts of good faith.

It being an emanation of the good faith rule is arguably what justifies the result in *Galloway*,[141] where the court held that a small exaggeration was sufficient to trigger the forfeiture rule. Only good faith could prompt a court to look at the blameworthiness of the conduct rather than the proportion of the exaggeration as compared to the genuine part of the claim. Comparing the exaggeration to the genuine amount would be a business-like and measured way of viewing the issue in search of a fair and equitable solution. It would be appropriate if no punitive effect were desirable and the main aim in solving the dispute were a correct, clear-headed interpretation of the contract or a solution capable of creating some description of equilibrium between the parties. A punitive remedy by its very nature presumes an underlying "duty" of good faith and a "breach" of that duty.[142] A contract of good faith would be capable of producing such "duties" and they could in turn attract a punitive remedy in support of that good-faith duty.

A claim in tort tainted by fraud or by fraudulent means and devices may be struck out, as decided by the Supreme Court in *Summers v Fairclough*, but not because of any relation to good faith. The law at present operates one rule for fraudulent insurance claims, and another for fraudulent claims in tort. Pragmatic attempts at assimilation include *Summers v Fairclough*[143] wherein the Supreme Court

[140] At [16].
[141] *Supra*.
[142] Not a real duty in the contractual or tortious sense.
[143] *Summers v Fairclough Homes Ltd* [2012] UKSC 26. There can be no improvement upon Lord Clarke's summary of the facts and judgments in Clarke, Anthony, *What shall we do about fraudulent claims?* The William Miller Commercial Law Annual Lecture, Edinburgh Law School, 20 November 2015, transcript available at https://www.supremecourt.uk/docs/speech-151120b.pdf, accessed on 4 January 2016. The speech will be referred to in the following as 'Clarke (2015)'

agreed in principle that fraud in a claim in tort can be a cause for the claim to be struck out, approving earlier case law to that effect in *Zahoor v Masood* [144] and *Arrow Nominees Inc v Blackledge*.[145] However the Supreme Court in its judgment decided not to strike out the claim in that case and subsequent case law to date similarly demonstrates distinct reluctance on the part of courts to strike out a claim simply on the basis of exaggeration or other 'minor' fraud,[146] including claims pursued by fraudulent means which in insurance law would be considered fraudulent.[147]

Clarke, commenting extra-judicially, put it thus:

> "We tried quite hard to think of circumstances in which it would be proportionate to strike a claim out after a trial on liability and quantum. The only possibility that occurred to us was one where there had been a massive attempt to deceive the court but the measure of damages would be very small."[148]

It appears therefore that in the context of a claim in tort, the fraud in question must be of a rather serious kind for striking out to be appropriate. It must in fact amount to an abuse of process. In the presence of such abuse, the appropriate course of action for the judge is to dismiss the claim at the end of the trial. Failing the presence of abuse of process, the claim will be permitted to be litigated in full. The claim is of course likely to fail not least for the reason that the judge will be unlikely to believe any other evidence offered by the fraudulent claimant in support of the claim.[149] These cases are superseded in practice for the purpose of personal injury claims only, by the newly enacted section 57 of the Criminal Justice and Courts Act 2015, entitled 'Personal injury claims: fundamental dishonesty'. Without going into excessive detail, it is noted that the provision replicates the insurance position in forfeiting the entire claim where the claimant has been dishonest.[150]

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[144] [2009] EWCA Civ 650, [2010] 1 All ER 888.
[145] [2000] EWCA Civ 200, [2000] 2 BCLC 167.
[146] "We have reached the conclusion that, notwithstanding the decision and clear reasoning of the Court of Appeal in *Ul-Haq*, the court does have jurisdiction to strike out a statement of case under CPR 3.4(2) for abuse of process even after the trial of an action in circumstances where the court has been able to make a proper assessment of both liability and quantum. However, we further conclude, for many of the reasons given by the Court of Appeal, that, as a matter of principle, it should only do so in very exceptional circumstances." *Fairclough Homes Ltd v Summers* [2012] UKSC 26, [2013] Lloyd's Rep IR 159, at [33].
[147] *Summers v Fairclough*, *Shah v Ul-Haq*, and most recently *Alpha Rocks Solicitors v Alade* [2015] EWCA Civ 685, [2015] 1 WLR 4534. See on this point Clarke (2015), esp para 41 onwards.
[148] Clarke (2015) at [26].
[149] Clarke (2015) at [27] notes three ways by which deterrence can be achieved short of striking out the claim: the judge will be reluctant to believe other evidence from the fraudulent claimant; the claimant can be ordered to pay the costs of any part of the trial caused by its fraud; and the defendant may protect its position by means of a *Calderbank* offer. It is submitted that each of these is arguably just as applicable in the context of an insurance claim.
[150] Criminal Justice and Courts Act 2015, s 57. The Act has apparently already been put to good use: http://www.lawgazette.co.uk/law/insurer-invokes-fundamental-dishonesty-to-see-off-claims/5050820.fullarticle (accessed on 26 January 2016).

If claims in tort that would be considered fraudulent where made under an insurance policy are not struck out, it is interesting to consider what will be the consequences if there are insurers on both sides of the litigation.

If the claim is litigated, and the (fraudulent) claimant does not succeed, the loss lies where it falls. The claimant may wish to claim against its own insurers, if it has any and is still within time. There does not appear to be any case deciding whether prior litigation on the exact point of the insurance claim containing some kind of fraud will defeat the insurance claim, but especially given the outcome in *Sharon's Bakery (Europe) Ltd v Axa Insurance UK Plc and another*[151] it may be thought that fraud will defeat that claim.

If the claim in tort is permitted to be litigated and is successful, in spite of the fraudulent attempt, which it may well be if other convincing evidence is presented and accepted by the judge, the insurers on the (honest) defendant's side may be entitled under the policy to reject the claim, because of the fraud committed in making it. However if the defendant (who is the insurance claimant) has been honest, they are not in a position to reject the claim. Should they be permitted to reject the claim, the innocent defendant will be in the position of covering the claim itself. That does not seem to be a desirable outcome. The defendant is the innocent party in the context and has taken the prudent measure, or complied with the mandatory rule, and obtained insurance, and for present purposes it is assumed that the insurance claimant has been honest at every stage.

The judicial system abhors circuity. It is entirely unlikely that the insurers of the innocent defendant, having paid the third party claim of its innocent insured, would be given a remedy even if technically subrogated to the claim against the third party. The point does not appear to have been tried.[152]

The author takes the view that having separate or different fraudulent claims rules for insurance and other fields of law is not an unworkable nor undesirable state of affairs.[153] An important factor is the difficulty in discovering the fraud. Insurers are at arm's length even after the conclusion of the contract, with the insured under no obligation for instance to disclose business secrets or report regularly on any state of affairs. This is entirely different from, by way of example, the typical employment contract which presumes continued collaboration and contact and therefore also plentiful opportunity to detect fraud.

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[151] [2011] EWHC 210 (Comm), [2012] Lloyd's Rep. IR 164.

[152] Given the already advertised interest in these issues demonstrated by Clarke extra-judicially, a member of the panel in the Supreme Court's forthcoming hearing in *Versloot*, it appears highly likely that these issues will be addressed *obiter* in that case; Clarke (2015); fn 143 above..

[153] A reference to the works of James Davey & Katie Richards, 'Deterrence, human rights and illegality: the forfeiture rule in insurance contract law' [2015] LMCLQ 314 as well as Peter MacDonald-Eggers, 'Remedies for the failure to observe the utmost good faith' [2003] LMCLQ 249-278 is appropriate here, although the author – with great respect – disagrees.

3.3 The subjective element

The subjective element of insurance fraud is a topic that has developed significantly in the course of the work on this thesis. It is probably fair to say that when work started in April 2007, the idea of a subjective element was far from anyone's mind. The closest to a subjective element was the feature outlined above[154] whereby a genuine but exaggerated claim would not be considered fraudulent, if the intention behind the negotiation was not to defraud but to give the claimant a good starting point for negotiations. The idea of how to assess a strategy of fraud was arguably not otherwise present in the insurance claims context.

The idea first arose in the judgment of Mr Justice Eder in the consumer insurance case *Aviva Insurance Ltd v Brown*, [155] which will be discussed in depth in the following. Two years later, the marine insurance case *Versloot Dredging BV & Ors v HDI Gerling Industrie Versicherung AG (The DC Merwestone)*[156] provided an opportunity for Mr Justice Popplewell to express his dissent with the test employed in *Aviva v Brown* and to pave the way for future consideration of the matter by a higher instance. This chapter will endeavour to demonstrate why such consideration is desirable or even essential to the re-development of insurance law.

3.3.1 The historical position and the theoretical starting point

The words "historical position" in this context carry the perhaps unusual meaning of "before 2011". Until the judgment of Mr Justice Eder in *Aviva v Brown*,[157] the subjective element of insurance fraud had been limited to an (also relatively recently established) exculpatory element in cases where an enhanced claim was not subject to censure where it was put forward by way of negotiation.[158] In addition, claims for barratry under maritime policies were subject to a discussion of intent whereby it was decided only in the 1980s that the Rule of Construction on Barratry[159] did not mean that it was the insured's duty to prove its lack of involvement in the scuttling of a vessel.[160] Besides those sporadic examples, there was no discussion of intent, or the test applicable to such intent, inside insurance law. There was perhaps a silent assumption that the test in *Derry v Peek* applied, but that assumption had not been spelled out or indeed tested judicially.

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[154] At 2.2.3.
[155] [2011] EWHC 362 (QB), [2012] Lloyd's Rep. IR 211.
[156] [2013] EWHC 1666 (Comm), [2013] 2 Lloyd's Rep 131.
[157] *Supra*.
[158] In *Orakpo v Barclays Insurance Services* [1995] LRLR 443.
[159] Marine Insurance Act 1906, Schedule 1, Rule 11 reading: 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.
[160] See *The Elias Issaias* (1923) 15 Ll L Rep 186 and *Piermay Shipping Co. SA v Chester (The Michael)* [1979] 2 Lloyd's Rep 1, *The Zinovia* [1984] 2 Lloyd's Rep 264, *Continental Illinois National Bank and Trust Company of Chicago (The Captain Panagos DP)* [1985] 1 Lloyd's Rep 625.

The fact that the purpose and essence of the fraudulent claims rule was to introduce a punitive element into the law meant that it was only logical to expect the insured to be particularly careful in the making of a claim and that a draconian remedy for even minor infractions was not inappropriate. The gradual extension of the concept of fraud, and in particular the inclusion of fraudulent means and devices into its scope, conspired to shift the equilibrium to the advantage of the insurer. Somewhere along the trajectory of that process, there must exist a hypothetical point when the scope of the fraudulent claims rule has been enlarged past the point of equilibrium, so that a simple draconian rule is no longer appropriate for all cases of fraudulent claims. A reformer may then propose a reversal of development of the law; or if reversal is not desirable, the concept of moral hazard suggests a range of solutions that may be used to mould a rule that has thus become inappropriate back into a workable and fair rule. One of the solutions available is to look at the actual blameworthiness of the conduct in question.

Post-contractual good faith is not centred on contract-making and the fairness of the bargain,[161] it is concerned with the truthfulness of the claim itself and the correctness of it being indemnified under the policy. It is therefore a situation marked by the moral hazard to an even greater extent than the pre-contractual disclosure context. In the pre-contractual context, the insurer has a range of methods at its disposal to address any concerns related to moral hazard – the terms of the contract or the premium may be adapted, or the risk may be declined. In the post-contractual situation, the instruments available to the insurer are by necessity more blunt – not only as a result of the concrete manifestation of the fraudulent claims remedy. On a theoretical level, only a narrow range of options is available to the insurer: declining the claim; terminating the policy; and damages for the costs incurred in investigating the claim. Of these, declining to pay the claim has become the most important option under English law with termination of the policy being important in practice, although the support from the law is not emphatic and termination will be on the terms of the policy itself and not generally as a result of the operation of a rule of law. Damages has to date not played a significant role,[162] although at least one author has argued against the use of the remedy of forfeiture but in favour of the use of the remedy of damages.[163]

Because in the post-contractual context, there is a much smaller range of options available to the insurer, the insurer will be deeply concerned with awareness of what was at the root of the claim and

[161] *The Star Sea* [2001] UKHL 1, [2001] 1 Lloyd's Rep 389, *Agapitos v Agnew* [2002] EWCA Civ 247, [2002] 2 Lloyd's Rep 42.

[162] See also the Law Commissions' discussion of damages as a remedy for fraudulent claims; Law Commission Consultation Paper No 201 and The Scottish Law Commission Discussion Paper No 152 Insurance contract law: post contract duties and other issues - A Joint Consultation Paper at para 1.21.

[163] Peter MacDonald-Eggers, 'Remedies for the failure to observe the utmost good faith' [2003] LMCLQ 249-278; see esp pp 273-277. See also *Parker v National Farmers Union Mutual Insurance Society Ltd* [2012] EWHC 2156 (Comm) where the right to damages was asserted by the insurer, not contradicted by the defendant, and accepted without discussion by the judge.

any tendency towards carelessness or indeed fraud in the insured. It is therefore unsurprising that a pre-occupation with the remedy for fraudulent claims has followed the crystallisation of the remedy in the case law from the turn of the century.[164]

That said, any presence of an element of moral hazard at the post-contractual stage is arguably partly the insurer's fault. The influence of the post-contractual scenario on the pre-contractual scenario is immense. The insurer had the opportunity at the pre-contractual stage of weeding out any undesirable insureds and to introduce contract terms and set premium levels at a satisfactory level. If there is no excess or deductible in the policy, and no promissory warranty covering the concern of the insurer, and if the insured possesses no insurable interest enabling the principle of indemnity to operate, the insurer can only blame itself for not insisting upon such features when it had the opportunity.[165] Once the bargain has been struck, the insurer should arguably live with the mistakes it has made. This is the technical rationale for the presence of a draconian, unforgiving rule at the claims stage: if the honest insured under a considered and well-tailored policy still commits insurance fraud, the insurer to some extent has itself to blame for insufficient contemplation of the moral hazard and insufficient compensation for any dangers detected, or within its constructive knowledge.

The only circumstances where the insurer needs not blame itself at all would be circumstances where the proposer has purposely concealed its intentions to later commit fraud, or where the intention to commit fraud entirely post-dates the policy.[166] That being the case, even the remedy of avoidance for post-contractual breaches of good faith duties, as mooted in *The Litsion Pride*[167] but now dismissed in English law can be defended on the basis that the post-contractual moral hazard is objectively the same as the pre-contractual moral hazard.

There is therefore a logic and purpose to the historic structure of the law, and it is based on an overall equilibrium in relation to the insured's moral hazard. But once one element of that logic and structure is tampered with, other elements begin to synergise into a lop-sided system that is difficult to recalibrate. In the case of insurance law, the introduction of an element of intent is only one such supervening element. It is a trite observation that the law is based on the historic information asymmetry situation where the insured has entirely the upper hand, and thus the full advantage of any

[164] *The Star Sea* [2001] UKHL 1, [2001] 1 Lloyd's Rep 389, *Agapitos v Agnew* [2002] EWCA Civ 247, [2002] 2 Lloyd's Rep 42.

[165] *Per* Brett MR in *Stock v Inglis* (1884) 12 QBD 564 at p 571 : "In my opinion it is the duty of a Court always to lean in favour of an insurable interest, if possible, for it seems to me that after underwriters have received the premium, the objection that there was no insurable interest is often, as nearly as possible, a technical objection, and one which has no real merit, certainly not as between the assured and the insurer."

[166] As appears to have been the case in *Lek v Mathews* (1927) 29 Ll L Rep 141 where it appears from the account of the facts that the insurance claimant appeared to have begun fictionalising the claim only after he realised that unless it exceeded a certain sum, there would be no compensation at all. Viscount Sumner commented at page 165 that "*Nemo repente fuit turpissimus"* – no one ever became thoroughly bad in one step (a quote from Juvenal).

[167] *Black King Shipping Corp v Massie (The Litsion Pride)* [1985] 1 Lloyd's Rep 437.

moral hazard too. In comparison, the present situation is that the insurer is incomparably better informed than any insured, with such tools as extensive databases on crime and health statistics, GPS tracking devices to monitor driving habits and even some information exchange among insurers permissible under European Union competition rules.[168]

With these considerations in mind, it is appropriate next to review the recent case law on the subjective element of fraudulent claims in order to appreciate the impact on the overall equilibrium.

3.3.2 The law on fraudulent claims – the subjective element

Aviva Insurance Ltd v Brown[169] was the first case to directly discuss the subjective element in relation to a fraudulent insurance claim. Mr Brown's house had become uninhabitable due to subsidence (an insured loss under his home policy) and he made claims for repairs and for renting alternative accommodation. He first made a claim in 1989 and insurers only admitted the claim and made payment in 2008 in respect of repairs and alternative accommodation. One of the reasons why it took so long to make payment was that the insurer imposed a limit[170] on the cost of accommodation, whereas Mr Brown considered that he was entitled to "equivalent" accommodation costing more than that limit. As part of the long intervening process, Mr Brown had at one stage proposed renting a property owned by himself as alternative accommodation, without disclosing that he was the owner. He had in the end rented another house in the same street which was owned by a company in which he had a controlling stake. Upon discovering these matters, Aviva sought to recover the payments made, alleging that Mr Brown had presented a fraudulent claim or otherwise used fraudulent means or devices in order to persuade Aviva that there was a genuine arm's length transaction in respect of the alternative accommodation; that Aviva was entitled to repudiate the claim in its entirety and to terminate the contract from the date of the claim; and that Aviva was entitled to decline to pay the balance of the claim and to recover payments made. The judge agreed that it had been fraudulent to present a property owned by Mr Brown himself as a property available for rent; but not that it had been fraudulent to rent a house from a company that he himself owned.

The judge agreed that there was a subjective element to fraud and – in the absence of arguments on the point from the parties – applied the test of subjective intent from *Twinsectra Ltd v Yardley*,[171] wherein the House of Lords held that a test with two limbs was to be applied to fraud, namely that a finding of dishonesty required that the conduct in question was dishonest (1) by the ordinary standards

[168] See generally Andrea Lista, *EU Competition Law and the Financial Services Sector* (London: Informa, 2013), Chapter 5.
[169] [2011] EWHC 362 (QB).
[170] Purporting to have support in the policy for such a limit, although by the time of the trial it was accepted that the limit had been imposed and was maintained in defiance of a FOS decision in favour of Mr Brown.
[171] [2002] UKHL 12, [2002] 2 AC 164.

of reasonable and honest people and that (2) he himself realised that by those standards his conduct was dishonest.[172]

Accordingly, if insurers were to prove the alleged failure to disclose that Mr Brown was the majority shareholder in the company owning the property such conduct would be dishonest by the ordinary standards of reasonable and honest people. However, the judge said,[173] that Aviva must also show that Mr Brown realised himself that by these standards his conduct was dishonest, and Mr Brown had in cross-examination been genuinely indignant that insurers claimed that they did not know, given that he had not at any time sought to cover up this fact and that it was manifestly recorded in insurers' own documentation.

The reason why the subjective element arises for consideration is that many claimants may feel quite justified in thinking that they are entitled to recover for the very loss for which they claim, even if it is not strictly speaking the insured loss; or they may feel that the made-up loss is for all intents and purposes equivalent to the one they have in fact suffered, so that it will not really matter to a distant, corporate insurer which of the two is the subject of the claim.[174] However, although this appears to be the first application of the objective and subjective test from *Twinsectra v Yardley* in an insurance context, it cannot be said to 'open the floodgates' – Mr Brown was excused from insurance fraud because the law in relation to the ownership of the property was on his side, it being owned by someone other than himself, and because the correct information had indeed been available to insurers at all material times. There is thus only limited scope for application of a subjective test to escape the consequences of a fraudulent claim.[175]

The judge's conclusions were subjected to criticism in *Versloot Dredging BV v HDI-Gerling Industrie Versicherung AG (The DC Merwestone)*,[176] a marine insurance case. The judge held that where the fraudulent device consisted of a representation, the test in *Aviva v Brown* would give the same result as the definition of fraud in *Derry v Peek*,[177] which was a case about the tort of deceit rather than insurance:

[172] *Twinsectra v Yardley* at [12].
[173] At [101].
[174] Quite separately from the fraud issue, the case makes a mockery of the Financial Ombudsman Service. FOS had upon a complaint by Mr Brown ordered that Aviva should pay for the expenses Mr Brown sought, and Aviva had then agreed to do so. The judge's decision that Aviva may rescind from that agreement renders FOS decisions, which in principle are binding on insurers, completely toothless.
[175] A helpful discussion of subsequent limitations to the test in *Twinsectra v Yardley* can be found at page 139 of Claire Blanchard, 'The fraudulent claims principle: the mental element', Chapter 6 in D. Rhidian Thomas, ed, *The Modern Law of Marine Insurance* Vol 4 (London: Informa Law from Routledge, 2016).
[176] [2013] EWHC 1666 (Comm), [2013] 2 Lloyd's Rep. 131.
[177] *Derry v Peek* (1889) 14 AC 337.

> "I think the authorities establish the following propositions: First, in order to sustain an action of deceit, there must be proof of fraud, and nothing short of that will suffice. Secondly, fraud is proved when it is shewn that a false representation has been made (1) knowingly, or (2) without belief in its truth, or (3) recklessly, careless whether it be true or false. Although I have treated the second and third as distinct cases, I think the third is but an instance of the second, for one who makes a statement under such circumstances can have no real belief in the truth of what he states. To prevent a false statement being fraudulent, there must, I think, always be an honest belief in its truth. And this probably covers the whole ground, for one who knowingly alleges that which is false, has obviously no such honest belief. Thirdly, if fraud be proved, the motive of the person guilty of it is immaterial. It matters not that there was no intention to cheat or injure the person to whom the statement was made."[178]

Without directly doubting the application of the test from *Twinsectra v Yardley* in *Aviva v Brown*, the judge in *Versloot* applied the test from *Derry v Peek* instead. Although the judge in *Versloot* only said that the two tests would give the same result, the case paves the way for appeal to a higher court in a case where there is doubt as to the subjective element of the fraud. There is likely to be room for further development through case law on this point because the implication is that the judge did not approve of the test used in *Aviva*. However, it might be said that *Twinsectra* is a case on constructive trusts and the application of the more generally stated test from *Derry v Peek* in *Versloot* arguably has more systemic appeal.[179]

3.3.3 The effect of introduction of a subjective element and the choice of test

Mr Justice Popplewell criticised Mr Justice Eder's use[180] of the *Twinsectra* test and said that the test from *Derry v Peek* ought to be preferred as the test used for the subjective element of the fraudulent claim. This is not the place to enter into that debate, however interesting. What is of interest is the assumptions involved and the implications of a decision to use a test of one description or another. Is there a need in the first place for a subjective element, and by extension also for a test of that element? Given that there are at least two potential tests available in English law to adopt, and that additional

[178] (1889) 14 AC 337 at 374.

[179] The Court of Appeal in its decision, [2014] EWCA Civ 1349, [2015] Lloyd's Rep IR 115, steered clear of the point and the Insurance Act 2015 does not address it. The appeal of the Court of Appeal's decision is pending before the Supreme Court at the time of writing with scheduled hearing dates on 16 and 17 March 2016. The right timing for pursuing this issue in depth is perhaps after the judgment of the Supreme Court, expected in the first half of 2016.

[180] In fairness to Eder J the application of the *Twinsectra* test appears to have been agreed between the parties who perhaps had bigger fish to fry.

permutations are probably available further afield or susceptible to invention, what are the implications of adopting a test generous to the insurer or a test generous to the insured, respectively?

It has already been demonstrated that the subjective test is a recent invention and in particular what the reasons were for inventing that test. The subjective element may appear an obvious and necessary element of the law of insurance fraud, indeed it is present in other sectors of the law including criminal law and the law of obligations. The lack of intent to commit an act is usually exculpatory with the effect that the action is treated as innocent or negligent and therefore valid. In spite of this basic and seemingly obvious reflection, intent has never heretofore been a factor to be considered in insurance fraud. This could simply be an indirect function of there being a very low number of cases, which may simply mean that the issue has never yet arisen in a meaningful or pivotal manner, as insurers prefer to make their case on other bases. It could alternatively (or cumulatively) be a more direct, technical result of the difficulties of proof. The insurer must prove fraud on the part of the insured before the burden shifts to the insured to prove its innocence (or other lack of intent). If the first hurdle is too high a threshold in most cases, the second issue will never arise.

Thirdly, it could also be the result of intent not having until now been an element of insurance fraud, so that these cases (*Aviva v Brown* and *Versloot*), are introducing a new element to the law of insurance whether the judges are consciously aware of doing so or not. While the cases do not acknowledge this to be the case, but seek only to find the correct test of intent, the description of historic law above under certainly underpins this at first glance implausible theory.[181] It was outlined above[182] how information asymmetry was entirely in favour of the proposer so that the insurer was at its mercy. Extrapolating from this starting point, the reality of underwriting was that moral hazard had to be addressed once and for all at the underwriting stage. Good faith was a matter for the pre-contractual situation, and the insurer's contribution was not to raise spurious objections to paying. Once the bargain had been struck, the insurer must live with it and not use the technicalities of the contract or the law against the insured – the author refers again to the strikingly useful quote of Brett MR in *Stock v Inglis*.[183] This was said in relation to insurable interest, which is a different weapon in the insurer's arsenal to counter the moral hazard, but is equally in place in the present argument. The notion that once the bargain has been struck, the insurer has preferred to take the risk, opting out of the safe options of "no deal" or of modifying the bargain with appropriate safeguards for the sake of

[181] Marshall does not consider intent; indeed only wilful misconduct is available as a basis for rejecting claims based on fraudulent losses' at page 558.
[182] Under 2.3.
[183] (1884) 12 QBD 564.

receiving the full premium. The following reflection by Lord Justice Waller in *The North Star* conveys the same idea:

> "The underwriter may prefer to take the extra premium rather than investigate whether the good management reasons establish US$4 million as opposed to some lesser figure."[184]

Accordingly the historical position is arguably based on the Roman law maxim *pacta sunt servanda* – once there is a bargain, the law will uphold it and the insurer must suffer the consequences of doing business with a fraudster, or at least person of doubtful moral hazard status. What are the implications of this for the modern cases *Aviva v Brown* and *Versloot*? *Aviva* is a peculiar case and it is not surprising on the facts that the judge felt compelled to look at Mr Brown's intent. For much of the time in litigation, it was in fact the insurer who was not abiding by its contractual undertakings. It failed generally for over twenty years to supply the service which it had contractually undertaken to provide to Mr Brown, ie the insurance policy was from the outset of no value to him, and more specifically it declined to provide replacement accommodation to which Mr Brown would have been entitled, even after having been corrected by the Financial Ombudsman Service (whose rulings are binding on insurers – a double failure to abide by agreed stipulations).

But is looking at the intent of the insured the logical action in such a case? If what was at issue was implicitly (although not on the pleadings) a failing in the duty of good faith of the insurers, is the intent of the insured in its actions the correct counterweight to which to attend? It is arguably a *non sequitur* on a theoretical level.

Finally, on the choice of test, the two cases apply different subjective tests. The judge in *Versloot* was diffident in criticising the choice of test in *Aviva v Brown*, pronouncing only words to the general effect that the two tests would produce the same conclusion and achieve the same result. It should also be noted that in applying the *Twinsectra* test in *Aviva v Brown*, Mr Justice Eder relied closely on the parties' pleadings and it was carefully noted that the application of the *Twinsectra* test would give no different result than an application of the third limb of *Derry v Peek*; the test in which was furthermore not explicitly disavowed. It may be very briefly observed here that if the rule applied to fraudulent claims is said to be the "common law rule", a rule resulting from case law, it would seem appropriate that the generally applicable subjective test in *Derry v Peek*[185] be applied, not least because of the pervasiveness of that test but particularly for reasons of logical coherence and consistency. *Twinsectra v Yardley* was a case about constructive trust, an equitable remedy.

[184] *The North Star* [2006] EWCA Civ 378, [2006] 2 Lloyd's Rep 183, at [49]
[185] (1889) 14 AC 337.

Respectfully, it would seem that a test with its roots in the common law would be more appropriate in the circumstances than a test with its roots in equity.

3.4 Remedy

As will be set out in the following,[186] the key remedy is forfeiture. Before going into detail, A few introductory words on the legislative history of the Insurance Act 2015 are apposite. Until this point, there has been perhaps surprisingly little reference to the Insurance Act 2015. That is because that piece of legislation steered clear of the definition of fraud, with provisions confined to the remedy; including the remedy in relation to good faith. The responsible Law Commissioner said in evidence to the House of Lords' Special Bill Committee:

> "In a nutshell, it is an attempt to clarify the remedies that apply when there has been fraud. We do not touch on what the law on fraud might be; we have left that entirely to the courts to decide."[187]

The enactment of the Insurance Act 2015 has now resolved the never directly litigated issue of the effects of a fraudulent claim on the contract. According to section 12(1)(c),

> "the insurer may by notice to the insured treat the contract as having been terminated with effect from the time of the fraudulent act."

The law thus enacted constitutes no great leap. The remedy for fraudulent claims has crystallised slowly but surely. Express terms have for centuries been the main method of regulating fraudulent claims; to the extent that the law may be said to have suffered from a lack of case law and development as a result. That said, it is perhaps surprising that the clauses in use are not as detailed and clear as might be expected from a clause covering such an important contingency. Marine insurance policies often fail completely to regulate the issue, apart from the International Hull Clauses 2003 cl 45.[188] An effective clause must stipulate what is to happen to the fraudulent claim and to any prior and subsequent claims, if applicable. It must also provide for any pre-conditions for termination of the policy or stipulate that termination is to be automatic, as applicable.

The parties to the contract may apply any remedies they consider appropriate – provided they do so in unambiguous terms. Following the introduction of the Insurance Act 2015, it remains the case that the

[186] See 3.4.1.

[187] Unrevised transcript of evidence taken before The Special Public Bill Committee Inquiry on Insurance Bill [HL], Evidence Session No. 1 Heard in Public, Questions 1 – 14, Tuesday 2 December 2014, 10.20 am, available at http://services.parliament.uk/bills/2014-15/insurance/stages.html (accessed on 27 January 2016) at pages 19-20. The final part of the quote is a clear reference to *Versloot Dredging* ; at the time pending in the Court of Appeal.

[188] See under 3.2.1 Source of the rule: contract clauses, above.

parties are free to regulate the position between them as they wish. A contract term permitting the insured to submit a fraudulent claim is not affected by s 16(2) because it is not to the disadvantage of the insured, and it therefore does not need to comply with the transparency requirements in s 17. It is of course the case that contracting out of the provisions of the Act is likely to meet with practical difficulties: the insurer is unlikely to accept a negotiating position on the part of the insured that entails permission to defraud the insurer at a later stage. Meanwhile the introduction of a stricter remedy for insurers for fraudulent claims, for instance by adding damages to forfeiture and termination, would be subject to section 17 of the Insurance Act. The same would arguably apply to a wider or narrower definition of what constitutes a fraudulent claim.

Up until the entry into force of the Insurance Act 2015, it was, in the absence of a contract clause, the common law that must apply. It was therefore important that the state of the common law should be clear and unambiguous. Having considered the current state of the law, the Law Commissions suggested in Issues Paper 7[189] that legislative reform was desirable for three reasons: there was a need for clarification of the common law rule on fraudulent claims; legislation was necessary to clarify the position of UK law to European and other partners; and deterrents and penalties ought in principle to be clearly set out in law.[190]

The author expressed her respectful disagreement with all three points: first, the common law rule following especially *Agapitos v Agnew*[191] is a clear and incontrovertible part of English insurance contract law; second, it is not legislation that is necessary to clarify what the law is, it is practitioner works, text books and university and practitioner education for those who use the law – particularly since the law – whether enacted or case law – will undoubtedly be further developed in its details;[192] third, while criminal or regulatory penalties ought always to be set out in law or written guidelines, there is no particular reason why a contractual remedy foreseen by the law must be set out in enacted legislation, particularly when the parties have the opportunity to set out even more rigorous penalties (such as automatic termination) in a contract clause.

The Law Commissions further asked the questions whether policyholders should be under a statutory duty not to make a fraudulent claim, and whether the definition of fraud should be left to the courts, going on to discuss the current remedy of forfeiture of the whole claim, the effect of the fraud on

[189] Issues Paper 7: The Insured's Post-Contract Duty of Good Faith (July 2010) ,
[190] the Law Commissions in paragraph 2.8 of the document Summary of Responses to Issues Paper 7: The Insured's Post-Contractual Duty of Good Faith, available at http://www.lawcom.gov.uk/docs/IP7-responses_summary.pdf (accessed 15 December 2010)
[191] [2002] EWCA Civ 247, [2002] 2 Lloyd's Rep 42.
[192] This point was quoted from the article at Johanna Hjalmarsson, (2010)10 STL 3 – 5 by the Law Commissions in paragraph 2.8 of the document *Summary of Responses to Issues Paper 7: The Insured's Post-Contractual Duty of Good Faith*, available at http://www.lawcom.gov.uk/docs/IP7-responses_summary.pdf (accessed 15 December 2010).

previous claims and finally the precise mechanics of termination, which remained undetermined by case law. Such issues have now received their statutory resolution – no doubt with further developments to follow.

3.4.1 Effects on the claim

The remedy is simple, insofar as it concerns the claim itself: the whole claim is forfeit. There is an intentional punitive element to this: insurance fraud is thought to be discouraged if the insured cannot recover for the genuine part of a claim that is only partially fraudulent. It also saves insurers the trouble of distinguishing and debating with the insured which parts of the claim are genuine and fraudulent. It may be observed that considering the typology of fraudulent claims set out above,[193] a blanket forfeiture rule is most punitive to the smallest fraud: for a wholly invented claim to be forfeit is not quite as punitive as where a partly legitimate, partly exaggerated claim is forfeit in its entirety. Thus the forfeiture remedy may be designed as punitive, but it is in fact harsh only on the honest customer who is temporarily tempted astray. The habitual fraudster and confirmed moral hazard will not be deterred by simply losing the claim, especially if it was non-existent to begin with.[194]

As concerns prior claims, the law before the entry into force of the Insurance Act 2015 is clear: logic dictates, and *Axa v Gottlieb* confirms that claims accrued before the submission of the fraudulent claim remain valid and unassailable. The same case also decides that interim advance payments made on the fraudulent claim, before the fraud took place, will have to be repaid by the insured. The position following *Axa v Gottlieb* is confirmed by the Insurance Act. According to section 12(1)(b), the insurer may recover from the insured any sums paid by the insurer to the insured in respect of the claim (but not sums paid, or due, in respect of prior claims). According to section 12(3), the insurers' statutory right to terminate the policy does not affect the rights and obligations of the parties to the contract with respect to a relevant event occurring before the time of the fraudulent act – if the termination remedy does not affect prior claims, the strong implication is that the fraudulent claim itself does not affect earlier claims either.

While it was, even before the statute, reasonably clear what would be the fate of the fraudulent claim itself, the fate of subsequent as well as contemporaneous claims would depend at least partly on the fate of the contract itself; see below. Nevertheless, in *The Captain Panagos DP*,[195] there were two contemporaneous claims for fire and grounding respectively. One was genuine and one was false – the court considered them closely connected so that the claimant could not recover for either. This

[193] *Supra*.
[194] As explained by eg Aysegul Bugra & Robert Merkin in , '"Fraud" and fraudulent claims', (2012) 125 *Journal of the British Insurance Law Association* pp 3-22; James Davey & Katie Richards, 'Deterrence, human rights and illegality: the forfeiture rule in insurance contract law' [2015] LMCLQ 314.
[195] [1989] 1 Lloyd's Rep 33.

presumably remains the position under the Insurance Act 2015, which does not mention claims contemporaneous to a fraudulent claim, only events having taken place prior to the fraudulent act.[196]

As emphasised above, the rule is intended to have punitive effect. In Australia, some of the punitive value of the common law rule has been mitigated in that there is discretion for the court to allow the genuine part of the claim.[197] This author is not in favour of purely judicial discretion, the result of which on a technical level predicates the outcome of a legal issue upon whether or not the parties choose to go to court. The law ought to provide for the same outcome, irrespective of whether the judicial system is engaged for the solution of the problems of the parties. The objection is admittedly a procedural technical one but one need only consider a statutory provision for judicial discretion, such as in the Australian Insurance Contracts Act 1984, s 56, to see the absurdity. In Australia, section 56 of the Insurance Contracts Act 1984 is an oddity in the strict, narrow context of the contract itself, as judicial discretion adds a layer of subsequent uncertainty, allowing parties to plead as once would have been done to the courts of equity that a non-contractual assessment be added to the first, contractual assessment. It might be said in favour of the provision that from a judicial policy perspective and considering problems of wasting court time, the rule probably prevents some litigation by preventing the parties from taking non-deserving cases to court as the judge will recognise them as such.

3.4.2 Effects on the contract

Perhaps the most surprising gap in the law was the uncertainty as to the effect of a fraudulent claim on the insurance contract itself.[198] It is surprising, because the discovery that the insured has submitted a fraudulent claim may quite naturally constitute a strong impetus for the insurer to immediately end the contractual relationship. This state of affairs prevailed for a number of reasons – many insurance contracts are limited to one year and renewed annually, meaning that once a claim had been detected, it made more sense simply not to renew the policy. Another factor was that there would frequently have been a term in the contract permitting insurers to terminate the policy without any particular reason, simply by giving reasonable notice. Finally, litigation costs in this context would in the vast majority of cases not have been money well spent. We now have certainty, insofar as new legislation can be said to provide certainty until practice has had its say, deriving from section 12 of the Insurance Act 2015, which codifies a right for the insurer to terminate the policy:

[196] Section 12(3) of the Insurance Act 2015.
[197] Insurance Contracts Act 1984 (Cth), section 56.
[198] Apologies to any attentive reader for the tempus confusion in this segment. Writing about historic, but current law in the period between enactment of new law but before its entry into force is proving a challenge.

> "the insurer may by notice to the insured treat the contract as having been terminated with effect from the time of the fraudulent act."[199]

In addition, following the entry into force of the Insurance Act 2015, the remedy set out in section 17 will be repealed by truncating the section after the initial stipulation that the contract is one of good faith.[200] Up until 12 August 2016, the law was at best confusing. While theoretically section 17 of the Marine Insurance Act 1906[201] stipulated a right to avoid, legal analysis had moved on from the period following *The Litsion Pride* during which academics and judges wrestled with the idea that the remedy must legally be that set out in s 17 of the Marine Insurance Act 1906, namely avoidance *ab initio*:

> "17 Insurance is uberrimæ fidei
>
> 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."[202]

The remedy referred to in the final clause of the section is taken to be avoidance *ab initio*, which is unproblematic in the event of pre-contractual misrepresentation, but given its retroactive effect entirely unsuitable for something that occurs *after* the inception of the policy and when the policy has perhaps run for a period, and other, perfectly legitimate claims have been settled thereunder. While it was confirmed by the House of Lords in *Banque Financiere v Westgate* that no other remedy was available either, it had on the other hand for some time not been seriously doubted that the right to avoid *ab initio* was not a remedy available to the insurer following the submission of a fraudulent claim by the insured. Whether such is the right of the insurer depends largely on the terms of the policy itself – while the insurer may well be able to terminate the policy, there is not much case law in this regard and the right to terminate as of the date of the claim is not automatic. Contract clauses on fraudulent claims generally stipulate that the contract is to be "void", but do not provide the further details that one might expect, such as a notification procedure.

However, the Court of Appeal in *Agapitos v Agnew* declined to apply this remedy to the contract, thereby concluding the discussion that arose from *The Litsion Pride*.

[199] Insurance Act 2015, section 12(1)(c). No time limit was adopted to limit this right of the insurer to terminate for breach. It is therefore wise to continue the practice of regulating this issue by means of a clause in the contract clarifying especially the remedy.
[200] Insurance Act 2015, section 14(3)(a).
[201] This remedy was omitted through the insurance Act 2015.
[202] The Insurance Act 2015 places a full stop after the word 'faith' and omits the rest of the section, with effect from 12 August 2016.

The main intellectual as well as practical obstacle was the pervasive effect of avoidance as a remedy, making the provision a singularly blunt instrument: it would serve also to negate any claims made prior to the fraudulent claim and would therefore notably leave the forfeiture rule without space for operating, unless the two rules operate quite separately and the insurer opted to continue the contract, while wishing not to pay the fraudulent claim itself. Alternative analyses whereby a post-contractual duty of disclosure would be an implied term of the contract had not found judicial favour and it is particularly worth noting that an implied contract term carrying remedies other than those normal under wider contract law would do little to clarify confusion and impart consistency.[203]

There had also been judicial attempts to recognise the availability of the remedy of avoidance in principle but to limit the scope of its application. It has been noted that the outcome in *The Mercandian Continent*, whereby the right to avoid was limited to instances analogous to a repudiatory breach of contract, lacks the merits of consistency and historical basis:

> "to limit the post-contractual duty of good faith to repudiatory breaches of contract, one would be depriving the insurer of any real remedy in the event that the post-contractual fraud is not sufficiently serious to amount to a repudiation (unless of course damages were available). Indeed, if the suggested limitation were to be read as implied in the language of s. 17 , one would be left with the undesirable position that the same statutory provision would have to be read in two different ways , depending on whether one were looking at the assured's pre-contractual duty or post-contractual duty (to say nothing of the insurer's duty)."[204]

It will be noted that theoretically, under an analysis of good faith that adopts the moral hazard as the origin of the doctrine of good faith, avoidance at the "post-contractual" stage is either nothing unexpected or immoral, but a direct consequence of the insured's failure to observe its duties; or a proscribed result because the insurer has in the process of making the contract sufficiently assessed the insured's moral proclivities and has not found them wanting. As observed above, *The Mercandian Continent* and other modern case law fails to embrace this analysis.

Once section 17 could be productively disregarded, general contract law provided a simpler, more attractive solution to the consequences on the contract of a fraudulent claim. The question to ask was whether the fraud could be regarded as a breach of contract so serious that it would, as a matter of general contract law, entitle the insurers to terminate the contract. Mance LJ in *Agapitos v Agnew*

[203] Best explained in Howard N. Bennett, 'Mapping the doctrine of utmost good faith in insurance contract law' [1999] LMCLQ pp 165-222.
[204] Peter MacDonald-Eggers, 'Remedies for the failure to observe the utmost good faith' [2003] LMCLQ 249-278 at [263].

approved reasoning to this effect by Rix J (as he then was) in an earlier case,[205] wherein Rix J said that the insurer would be entitled to terminate the contract, provided that the fraud amounted to a breach that would have entitled the insurer to accept the insured's repudiatory breach and terminate the policy.

Fortunately, we can now hopefully abandon these rather inward-facing complications and focus on correctly applying the statutory remedy of termination.

3.4.3 The premium

The Insurance Act 2015 provides that in case of termination for fraud, the premium need not be returned. While it might appear reasonable that if the insurer's liability under the policy should cease for some reason, say, six months into the duration of the policy, the insured should be entitled to the return of half of the premium, this is not in conformity with the principles of insurance law. As a matter of principle, the premium is considered earned by the insurer as soon as the risk incepts and therefore not usually returned thereafter. However, where there is avoidance *ab initio*, the premium is returned for lack of consideration, and the Court may consider a failure to offer to return the premium an indicator that the insurer does not genuinely consider the contract avoided.[206] The provision to this effect in the chapter *Return of Premium* of The Marine Insurance Act 1906, is s 84(3)(a) entitled *Return for failure of consideration*, which provides as follows.

> 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:
>
> …
>
> (emphasis added)

The provision refers to the policy being void or avoided – ie a situation where there is a clear logic to the need to return the premium, and the permission to decline to return the premium forms part and parcel of the punitive effect sought. Marshall explains that the provision is based on the insurance

[205] *Royal Boskalis Westminster NV v Mountain* [1997] LRLR. 523

[206] In *Argo Systems FZE v Liberty Insurance (PTE) & Anor* [2011] EWHC 301 (Comm), [2011] 2 Lloyd's Rep. 61, the judge at first instance, declining to permit insurers to avoid, said: "The absence of an offer to return the premium is of itself not determinative but it is a powerful factor" (at [41]). The case was decided on other grounds upon appeal.

having been taken out fraudulently from the inception.[207] It will be seen that for this particular provision to apply to fraudulent claims, the policy must be void or avoidable, which is the case only if section 17 of the Marine Insurance Act 1906 were to apply during the currency of the contract. The premium would in such a case be retained even though the contract were avoided, which would of course normally mean that everything performed under the contract should be reversed. Given that section 17 can now with certainty be said not to apply, it section 84(3)(c) may effectively also have lost its effect. That said, the effect of the amendments of the Insurance Act 2015 in that part are that while contract is not avoided by a fraudulent claim, it can be terminated and the insurer is entitled to decline to return the premium.

3.4.4 Co-insureds and group insurance

The final issue related to fraudulent claims now resolved by statute is against whom the insurer is to have a remedy in the context of policies involving more than one insured. According to section 13(2), the insurer does not have a remedy against honest claimants, where another claimant has been dishonest. Assuming the fraudulent insured is not acting as agent of an honest insured, the honest insured will be able to recover and the policy cannot be terminated insofar as their cover is concerned. The issue of fraudulent and honest co-insureds was considered by the Law Commissions which did note the situation where the fraudulent insured acts as agent of the innocent insured, causing that fraud to be attributable to the innocent party.[208] This situation is not clarified in the Act but the appropriate conclusion may well follow from first principles. Previously, if there was no situation of agency, the question was whether the insureds were joint insureds or whether upon close scrutiny they in fact had separate (composite) policies with severable interests. In the latter case the innocent insured could recover. This thorny question is now resolved in what appears to be a straightforward and just fashion. There may linger an issue on the burden of proof that the innocent insured was innocent: this is a fact that could be proven by the innocent insured as claimant (having been put to proof by insurers), or by the insurer seeking to reject the claim.

3.5 Conclusions

As is seen from this description of the current state of the law, fraud has emerged as a rule operating entirely separately from pre-contractual moral hazard; a very satisfactory development but nevertheless one that arguably lacks in theoretical, historical or principled foundation. Does the 'common law rule' ultimately derive from the *ex turpi causa* maxim? Or is it a rule *sui generis* in law? If the latter is it perhaps founded on the good faith nature of the insurance contract? If so, the introduction of section 14(1) of the Insurance Act 2015 and the truncation of section 17 of the Marine

[207] Samuel Marshall, Treatise on the law of insurance, 2nd ed (London: Butterworth, 1808) at page 649.
[208] See the Law Commissions' Issues Paper 7: The Insured's Post-Contract Duty of Good Faith, page 46 onwards.

Insurance Act 1906 are only superficially of assistance, and a coherent framework is still lacking that could underpin the rule and assist its further development. However, the highly specific remedies now set out for fraudulent claims in the Insurance Act itself, based on rules developed by case law, mean that for fraudulent claims at least the need to refer back to good faith as an interpretive principle may well be unlikely to influence the law's approach to fraudulent claims at all. It remains to be seen what influence good faith may come to have as an interpretive principle outside fraudulent claims rules.

However, the view of this author is that in any event modern law is not so concerned with principle. The author feels that a strong trend can be discerned in modern conceptual thinking to divorce fraudulent claims from both good faith and the moral hazard, and to consider it completely separately – this is so much so that a recent influential article on the subject on fraudulent claims does not at all mention moral hazard.[209] The authors endeavour to "examine the meaning of the word "fraud" as it is applied in the context of fraudulent claims" and advise against excessive rigidity in attempted reform. That is indeed the direction the law appears to be taking. While in the short term, this has proven highly beneficial in creating clear remedies founded on the existing law, and a solution for fraudulent claims that has rendered it mostly unencumbered by the spectre of good faith, at least in practical terms, there is also an accompanying risk of losing sight of the overall picture, including the original roles of moral hazard and information asymmetry considerations. In line with insurers' inherent incentives in shaping the law on insurance fraud, a need for legal certainty as well as forceful action has borne out in terms of a gradually expanding scope for application of a deterrent fraudulent claims rule. There is very little in the modern shape of the law that favours the insured – the fraudulent claims rule has been introduced with significant scope and a punitive remedy. This has taken place with little attention to the overall picture of the moral hazard – its original equilibrium in the insurance underwriting situation and subsequent developments of the law and information asymmetry.

Should it really have done so? Was the risk of subsequent fraud really an element of pre-contractual disclosure that should have been discovered, achieved, dealt with and done before the contract was entered into, and then a closed matter? Could it be that the modern concept of insurance fraud is a poor fit for the original balance of powers within the contract, and that the law has been distorted beyond recognition in severing the link between pre-contractual disclosure and post-contractual fraud, and that an important equilibrium has been disturbed? Such questions are of greater scope than can be fully resolved by this thesis, but form an important backdrop to parallel developments in the law to be addressed in subsequent chapters, many of which also generally favour insurers.

[209] Aysegul Bugra & Robert Merkin, 'Fraud' and fraudulent claims, (2012) 125 *Journal of the British Insurance Law Association* pp 3-22.

4 Pleading fraud – thoughts from a minefield

In the above, the ambition has been to set out the substantive law on fraud as clearly and unambiguously as possible, but it is hopefully transparent that the law has not been the sharp, readily available tool that it ought to have been until perhaps very recently. In such circumstances, it is hardly surprising that insurers have avoided a plea of fraud wherever possible.[210] However, there are further reasons why a plea of fraud has historically not been a valid course of action, even where fraud was patently at hand or at last strongly suspected, and a plea concerning pre-contractual failure to disclose or breach of warranty was much the preferred option. A brief mention of those other contributing causes is in order.

Following a few initial notes, the main discussion of the chapter[211] concerns the burden and standard of proof as they apply to cases of insurance fraud, where there have been some important historical developments in the law. It is appropriate to start with a few words about the burden of proof, in order then to move onto the standard of proof which is the more complex question and will be set out in greater detail. The tremendous importance of the burden and standard of proof arises from the fact that fraud by its very nature is something that the perpetrator will wish to conceal. The insurer may easily find itself bringing complicated circumstantial evidence as to such elusive matters as the insured's general financial situation; the reasonableness of the valuation of the ship;[212] or the communications that took place between the insured and third parties, perhaps requiring extensive procedural disclosure.

4.1 Procedural considerations

Questions of proof will be dealt with below,[213] but it is appropriate to mention here that a case based on an argument of fraudulent devices requires comparatively little evidence. It may be a matter of simply comparing conflicting documents or records to demonstrate a discrepancy. Indeed, Mance LJ suggested in *Agapitos v Agnew* that questions of fraudulent devices to promote a claim could be

[210] That this has been the approach is evident from the relative dearth of fraud cases throughout the 20th century and should require no evidence.
[211] An earlier version of this chapter was published in the International Journal of Evidence and Proof: Johanna Hjalmarsson, 'The standard of proof in civil cases: the insurance fraud perspective', *International Journal of Evidence and Proof*, (2013)17, (1), 47-73 .
[212] This is a very complex matter since a ship will have a completely different value if she is unchartered compared with if she is under a lucrative time charterparty or has been specially converted for a particular purpose, in which case her resale value may be very low, but the repurchase value to the insured may be very high. For different examples on the related assessment, see *O'Kane* v *Jones* [2003] EWHC 3470 (Comm), [2004] 1 Lloyd's Rep 389 and *North Star Shipping Ltd* v *Sphere Drake Insurance Plc* [2005] EWHC 665 (Comm), [2005] 2 Lloyd's Rep 76, at first instance [169]–[170] and [201]–[204]. This issue was not discussed in depth upon appeal (*North Star Shipping Ltd* v *Sphere Drake Insurance Plc* [2006] EWCA Civ 378, [2006] 2 All ER (Comm) 65).
[213] See chapter 4, especially 4.3.

resolved as a preliminary issue or by summary judgment. In a subsequent case, *Interpart Comerciao e Gestao SA v Lexington Insurance Co*,[214] a claim under a certificate of cargo insurance was supported by a certificate of inspection from Bureau Veritas. This certificate was said to have been issued with falsified dates, for the purpose of securing correspondence to bill of lading dates and in turn with letter of credit and sale contract dates. In considering whether to give summary judgment for insurers, the judge did take note of the guidance provided in *Agapitos v Agnew* but cautiously declined to give summary judgment, saying that the law on the promotion of claims by fraudulent means and devices was insufficiently developed and that the case therefore ought to go to a full hearing. The judgment in *Interpart Comerciao* came soon after *Agapitos v Agnew*; a few years on, the law is better settled or has at least to some extent 'sunk in', and courts might now be expected to be more inclined to give summary judgment – at least if there is incontrovertible written evidence of the fraud.

There is another possible route for insurers faced with a difficult situation on evidence.[215] Fraudulent insurance claims will inevitably also affect the decision on costs. In *Esure*, insurers did not seek to prove that Mr Quarcoo was making a fraudulent claim, but instead successfully put him to proof that the car in question had in fact been stolen. According to the Court of Appeal, this finding at first instance necessarily also entailed a finding that Mr Quarcoo had been dishonest and insurers were therefore held to be entitled to indemnity costs rather than just costs on a standard basis, "not just because of the extra cost they may incur in defending such a claim – though that is considerable – but so that others are discouraged".[216]

In *Yasin v Karim and another* ,[217] a motor accident case where the second defendant was the first defendant's insurer, the insurer put the claimant to proof of every element of the accident, specifically stating that it was not pleading fraud. The Deputy District judge had struck out several paragraphs of the insurer's defence on the basis that they amounted to an allegation of fraud without such an explicit assertion being made. Upon appeal, the judge made a general assertion that "This court, in common with all courts, recognises the procedural and ethical restrictions on solicitors and counsel in alleging fraud."[218] but permitted the paragraphs to be reintroduced. The judge stipulated two categories of pleadings, one being the "fraud category" and one being the "inference category" and emphasised that it will be highly case and fact specific whether a case belongs in one or the other. In the event, the Deputy Judge in *Yasin v Karim* had erred in holding it to be a case in the fraud category and it should

[214] *Interpart Comerciao e Gestao SA v Lexington Insurance Co* [2004] Lloyd's Rep IR 690.
[215] Demonstrated by *Esure v Quarcoo* [2009] EWCA Civ 595.
[216] *Esure*, at [27] per Waller LJ.
[217] Unreported, 17 April 2015, Kingston-upon-Hull County Court, HH Judge Jeremy Richardson QC; available on Lawtel.
[218] At [4].

have been held to be an 'inference case'. The case was decided in heavy reliance upon dicta of Cranston J in *Ahmed v Lalik and Cooperative Insurance Society Ltd*.[219] Cranston J in that case stated:

> "in this type of case (minor road vehicle accidents) it is not necessary for the defence to make a substantive allegation of fraud or fabrication, but it is sufficient to set out the detailed facts from which the court would be invited to draw the inference that the claimant has not, in fact, suffered the injuries or damage alleged. These authorities recognise the procedural and ethical inhibitions on advocates alleging fraud and the realities in this type of case for defendant insurance companies unearthing evidence of it."[220]

The judges in these cases appear to consider this valid guidance specifically for crash-for-cash claims, and the level of relevance of these cases to high value individual business policies (by way of example) has not been settled. Equally, the judiciary is not entirely at one on the point. Disapproving of 'inference category' pleadings, the Court of Appeal in the case of *Hussain v Amin and Charters Insurance Limited*,[221] Davies LJ said as follows

> "this sort of pleading should not be sanctioned. It is in fact something of an irony that the second defendant seeks to criticise the conduct of the claimant's solicitors, when in part at least they were having to deal with an abusive defence. But ultimately it will be a matter for the costs judge to assess what is an amount reasonable to be paid by way of costs having regard to all the circumstances."[222]

The judge in *Yasin v Karim* offered the following.

> "It is important that the parties place their case on the table for all to see. Ambush and springing points upon opponents at the last minute would not be right. In this case the defendant, by way of the insurance company, placed their cards on the table. They say in clear terms that we have information to cast real doubt on what you are saying that this was a genuine accident. We put you to proof that this was a genuine accident that unfolded in the way that you say it did. If this is a true accident and the claimant has suffered in the way that is asserted, then he need have no fear. His evidence will ring through loud and clear; honest and open."[223]

This balanced guidance seems to translate fully to more complex cases and it might be said that it essentially amounts to a sort of good faith duty in insurance claims proceedings.

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[219] [2015] EWHC 651 QB.
[220] At [24], referring to *Kearsley v Klarfeld* [2005] EWCA Civ 1510 and *Francis v Wells* [2007] EWCA Civ 1350.
[221] [2012] EWCA Civ 1456.
[222] At [19]. The observation was dismissed in *Yasim v Karim* as having been made *obiter* in a costs decision.
[223] At [19].

4.2 Obstacles to pleading fraud – a miscellany

The first brief issue is that of professional ethics. Solicitors[224] and barristers[225] are officers of the court and are as such expected to show restraint as well as courtesy. A plea of fraud against the other party is regarded as a lack of courtesy in adversarial proceedings. Insurance cases are in this respect no different from other cases and this issue need therefore not be discussed in detail here. In the context of professional ethics, it may be noted that it is a common denominator between many of the fraudulent claims dealt with in this thesis that once it becomes apparent that a fraud is being perpetrated, for instance because surveillance evidence has been made available contradicting the claimant's statement, the solicitors usually come off record, so that the insurance claimant must continue as a litigant in person; for example in the early case *Ali v Esure Services Ltd.*[226] There are also examples of solicitors being penalised for pursuing a fraudulent claim: In a recent case from Gateshead County Court, the judge struck out the claim and decided that the solicitors acting for the injured party should pay all the defendant company's costs.[227] One of the final recommendations of the Insurance Fraud Taskforce was that the Solicitors Regulation Authority should take toucher action against dishonest solicitors.[228]

A second issue that has provided an obstacle to insurers pleading fraud over the years, and which was only relatively recently resolved has been described as follows.

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[224] The Solicitors Regulation Agency Handbook contains a Code of Conduct, Chapter 5 of which discusses the solicitor's duties to the client and to the court. It lists among the indicative behaviours that the solicitor has not complied with the Principles "IB(5.7) constructing facts supporting your client's case or drafting any documents relating to any proceedings containing:
(a) any contention which you do not consider to be properly arguable; or
(b) any allegation of fraud, unless you are instructed to do so and you have material which you reasonably believe shows, on the face of it, a case of fraud;
IB(5.8) suggesting that any person is guilty of a crime, fraud or misconduct unless such allegations:
(a) go to a matter in issue which is material to your own client's case; and
(b) appear to you to be supported by reasonable grounds"; SRA Code of Conduct, available at https://www.sra.org.uk/solicitors/handbook/code/content.page (accessed on 11 January 2016).

[225] The current version of the Bar Standards Board Handbook, rule C9.2 reads: "you must not draft any statement of case, witness statement, affidavit or other document containing:
…
.c any allegation of fraud, unless you have clear instructions to allege fraud and you have reasonably credible material which establishes an arguable case of fraud"; Bar Standards Board Handbook, available at https://www.barstandardsboard.org.uk/media/1553795/bsb_handbook_jan_2014.pdf (accessed on 11 January 2016).

[226] [2011] EWCA Civ 1582.

[227] Not the best source but I am hoping to receive the judgment in due course: http://www.bonddickinson.com/insights/publications-and-briefings/fundamental-fraud-qocs-and-opportunistic-claims-tide-turning (accessed on 15 January 2016).

[228] Final Report of the Insurance Fraud Task Force, January 2016, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/492980/PU1817_Insurance_Fraud_Taskforce.pdf (accessed 20 January 2016) at page 9-10.

> "It has long been considered in English law that … an insurer who defends a claim by alleging fraud against the insured is not able to rely upon any other defence, which means that if the fraud of the insured is not actually proven, then the insured will be able to recover under the policy no matter what."[229]

The purported rule was based on the case *Jureidini v National British and Irish Millers Insurance Company Limited*,[230] a case where insurers pleaded arson and insurance fraud. The effect of such a plea was said by the court to be that the policy was repudiated, so that the insurer was no longer entitled to rely on the defences of the policy.

As recently as in 2004, this was held by the Privy Council in *Super Chem Products Ltd v American Life and General Insurance Co Ltd & Ors (Trinidad and Tobago)*[231] to be incorrect, along with the doctrine of fundamental breach; the Privy Council commenting that "Viscount Haldane's statement has bedevilled our commercial law for too long".[232] In *Super Chem*, a manufacturer of chemically based products had taken out a policy for loss and damage to stocks and stores at the premises. The policy contained claims co-operation provisions of which the insured was allegedly in breach. The argument of insurers was that failures to provide documentation and information in breach of the claims co-operation clause precluded liability under the policies. On this point, the insured argued that once the insurers had alleged that the claims were fraudulent, they could no longer rely on any conditions in the policies dealing with matters of limitation or claims co-operation. The insurers' conduct in alleging fraud amounted to a repudiation of the contracts of insurance and precluded any reliance on any conditions precedent to liability. The Privy Council dismissed the insured's argument, holding notably that a plea of arson was not properly to be construed as a repudiation of the policy, but as a defence in reliance on the terms of the policy.[233]

Although the issue is now historic, the *Jureidini* case was for a long time a contributing factor to insurers avoiding a plea of fraud, for fear of not being able to rely on the other terms in the policy.

The presence of fraud in the proceedings is sometimes relative. In the personal injury claim *Aziz v Ali and others*,[234] the insurers (who were second defendants to both claims) alleged that not only had the motor vehicle accidents to which the claims pertained never happened, the insured under the motor policy was a wholly invented person – a fraudulent claim from beginning to end. In the judgment

[229] David Morse, and Lynne Skajaa, *Tackling Insurance Fraud: Law and Practice* (London: Informa, 2004) at page 7.
[230] [1915] AC 499.
[231] [2004] Lloyd's Rep IR 446.
[232] At [13].
[233] The Privy Council also discussed the wider issue of repudiation with reference to *Photo Production v Securicor* [1980] AC 827.
[234] [2014] EWHC 1846 (QB).

completing the civil proceedings, the judge noted that proceedings for contempt of court were likely to be forthcoming. However he went on to emphasise that he must not allow himself to be influenced by that fact – the evidence before him was in respect of the civil claims only and the applicable standard of proof was civil standard. The issue to be proven was one of negligence[235] so that while the spectre of fraud was certainly present, and the insurer had already resurrected a defunct part of the claim in order to later proceed with contempt proceedings, there was no direct issue of explicitly pleading or alleging fraud. The claims were dismissed.

A final development to be noted is in fact from a much cited insurance fraud case. In *Kearsley v Klarfeld* [236] the Court of Appeal distinguished between the situation where a defendant puts the claimant to proof of the claim, and one in which a positive case of fraud is pleaded and proof thereof is presented. In the former, there was no obligation on the defendant to explicitly plead fraud:[237]

> "There was no burden on them to prove fraud. It was sufficient that they set out fully the facts from which they would be inviting the judge to draw the inference that the plaintiff had not in fact suffered the injuries he asserted."[238]

These cases have between them changed the circumstances in which fraud might be pleaded so that it is now on the whole not entirely unlikely that a plea of fraud would be a relatively undramatic event. Pleas of fraud nevertheless remain relatively uncommon.

4.3 *The burden and standard of proof in insurance cases*

Arriving thus at the main topic of the chapter, the third obstacle to pleading fraud in insurance cases is more idiosyncratic and in some ways specific to insurance, and will be reviewed in greater detail. It concerns the burden[239] and standard[240] of proof as they apply to cases of insurance fraud. There have been some important historical developments in the law as well as recent developments which the author would – possibly controversially – argue are not universally well understood.

The tremendous importance of the burden and standard of proof arise in part from the fact that fraud by its very nature is something that the perpetrator will wish to conceal. The insurer may easily find itself bringing complicated circumstantial evidence as to such elusive matters as the insured's general

[235] Namely the failure to exercise due diligence in using the road, that negligence causing damage to another road user; *Aziz v Ali* at [33]. In the event, the insurance claimants failed to prove that any road accident had occurred in the first place, so that there could not have been any negligence either.
[236] [2005] EWCA Civ 1510.
[237] Confer *Cooper v P & O Stena Line Ltd* [1999] 1 Lloyd's Rep 734, where the judge commented that an allegation of fraud would expose a party to the possibility of criminal proceedings.
[238] *Kearsley* at [45]. Nor was there any need to consider, as the judge at first instance had done, the fact that the claimant was a professional man and the allegation might leave a stain on his reputation.
[239] In the following at 4.3.1.
[240] In the following at 4.3.2.

financial situation; the reasonableness of the valuation of the ship;[241] or the communications that took place between the insured and others. It is appropriate to start with a few words about the burden of proof, in order to then move onto the standard of proof which is the more complex question and will be set out in greater detail.

4.3.1 The burden of proof in insurance cases

The basic principle applicable in all litigation applies equally to insurance matters: the party that proposes a hypothesis must prove it. An insurance case on the burden of proof in the context of perils of the sea is generally regarded as a leading authority of wider importance. The House of Lords in *Rhesa Shipping* v *Edmunds (The Popi M)* [242] decided that the party arguing that a ship, the subject-matter of an insurance policy, had been lost by an insured peril must prove that the loss happened in the manner argued. The approach of Bingham J at first instance[243] had been erroneous, in that it was not permissible to limit the potential outcomes to a choice between the various hypotheses presented to the court for how the loss happened. The case addresses the burden of proof in relation to losses by perils of the seas, but is surprisingly often used as broader authority for the general proposition that the claimant must prove its case.

In addition to the 'proponent proves' rule, a further important point has been made in the marine insurance case *Slattery v Mance*,[244] that

> "There is no principle of the common law and no authority that I know of for the proposition that when the facts are peculiarly within the knowledge of the person against whom the assertion is made, the onus shifts to that person."

These dicta derive from a marine insurance case where there was an issue of fraud under a fire policy, but the principle has never been challenged. It naturally poses particularly great challenges in the

[241] This is a very complex matter since a ship will have a completely different value if she is unchartered compared to if she under a lucrative time charterparty; or has been specially converted for a particular purpose, in which case her resale value may be very low but the repurchase value to the insured may be very high. For different examples on the related assessment, see *O'Kane v Jones* [2004] 1 Lloyd's Rep 389 and *North Star Shipping Ltd v Sphere Drake Insurance Plc* [2005] 2 Lloyd's Rep 76, [2005] EWHC 665 (Comm) at first instance, paragraphs 169-170 and 201-204. This issue was not discussed in depth upon appeal (*North Star Shipping Ltd v Sphere Drake Insurance Plc* [2006] EWCA Civ 378).

[242] *Rhesa Shipping* v *Edmunds (The Popi M)* [1985] 2 Lloyd's Rep 1. Distinguishing *The Popi M* for the applicable burden of proof where there are genuinely only two possibilities, see *Milton Keynes Borough Council* v *Nulty* [2011] EWHC 2847 (TCC). In *European Group Ltd* v *Chartis Insurance UK Ltd* [2012] EWHC 1245 (Comm), a so-called 50/50 clause in the policy was designed to alleviate the impact of difficulties in proof by stipulating that where it could not be proven on which of two insurers the loss should fall, the loss should be borne half by each.

[243] Jocularly described by Lord Brandon in the House of Lords as based upon the "well-known but unjudicial dictum" of Sherlock Holmes to Dr Watson: "How often have I said to You that, when You have eliminated the impossible, whatever remains, however improbable, must be the truth?"; *The Popi M* at page 6.

[244] [1962] 1 Q.B. 676 at page 681.

context of fraud where in the very nature of things the true facts will be as well-hidden as is humanly feasible, so that being charged with the burden of proof may mean certain loss.

While *Slattery v Mance* is considered important authority, it is probably not permissible to use it outside the fire loss context. Fire cases operate their own criteria; thus a loss by fire is considered fortuitous whether or not it was set intentionally. This principle goes back to early cases where it was confirmed that "There is no doubt that one of the objects of insurance against fire is to guard against the negligence of servants and others".[245] That being the case, fire was considered an 'automatically' fortuitous event. With fire, the insured must prove that there was a fire, but not whether the fire was accidental or intentional, let alone if it was intentionally started whether the guilty party was the insured or a third party. It is therefore not surprising that any allegation but fortuity must be proven by the proponent of that hypothesis.

While fire insurance arguably operates an idiosyncratic burden of proof, it is nevertheless clear that the approach in *Slattery v Mance* is regarded as appropriate outside marine insurance; *GenesisUK.Net Ltd v Allianz Insurance Ltd*[246]

On the whole, insurance law operates few presumptions, for which reason the basic rule on the burden of proof will more often than not find application. Thus in most insurance cases the burden of proof will be exceedingly simple. The insurance claimant must prove that the loss or damage is proven under the policy, whereupon the insurer must prove that there is some exclusion in the policy which operates to permit it to reject the claim.[247] A recent case demonstrates what may happen next. In *Atlasnavios-Navegação Lda v Navigators Insurance Co Ltd and others (The "B Atlantic") (No 2)*,[248] Flaux J approved this statement of the law:

> "Once the insurers have established a prima facie case that a loss is excluded by reason of an excluded peril, … then the burden of proof is upon the owners to show that [subsequent events operated] in some respect as a new cause covered by the policy, in other words the burden is upon the owners to show a break in the chain of causation…"[249]

It is not explained why a *prima facie* case should be sufficient.

An issue in principle that occasionally arises in practice is the question of whether a fact to be proven refers to the definition of cover, and as such is to be proven by the insured, or is part of the definition of the exclusion, and therefore must be proven by the insurer. It is in such cases that the allocation of

[245] *Shaw v Robberds, Hawkes, and Stone* (1837) 6 Adolphus and Ellis 75, at page 84; see also *Dobson v Sotheby* (1827) 173 E.R. 1091.
[246] [2014] EWHC 3676 (QB).
[247] *Wayne Tank & Pump v Employers Liability Assurance Corp Ltd* [1973] 2 Lloyd's Rep 237.
[248] [2014] EWHC 4133 (Comm), [2015] Lloyd's Rep IR 151.
[249] At [220].

the burden of proof may determine the outcome of the entire case, as it did in the Singapore case *Marina Offshore v China Insurance (The Marina Iris)*[250] where the placement of the burden of proving that the vessel was seaworthy (which she was manifestly not, at least not for the purposes of the very risky voyage on which she sank) determined the outcome at each instance.

In relation to marine insurance, while the above propositions do apply, there is also authority for further, more specific propositions in relation to the burden of proof. [251] In marine insurance, fraud may be committed by intentionally sinking a ship ('scuttling') and claiming for the loss. First, if a claimant shipowner's fraud is that he has claimed for a loss by barratry of master and crew, but it appears that he was himself complicit in the loss, the burden of proof is on the insurer to demonstrate the involvement of the insured. This was established by *The Elias Issaias*.[252]

Absent successful proof by the insurer, where the sinking happened at the sole initiative of the master and crew without any connivance of the assured shipowner, there is of course a bona fide loss by barratry, a covered peril under the hull and machinery clauses currently in use.[253] In such cases, the burden of proof is further determined by the so-called proviso to the *Inchmaree* clause, which provides that the insurance covers loss by barratry by the master or crew, 'provided that such loss or damage has not resulted from want of due diligence by the Assured, Owners or Managers'.[254] The burden of proof for the proviso has now been established. It has been held that due diligence means the absence of negligence, and that it is the insured who must prove that it has exercised due diligence; *The Toisa Pisces*.[255] There are further examples from marine and non-marine insurance of how the contractual clauses may cause the burden of proof to shift.[256]

4.3.2 The standard of proof

The standard of proof is a separate matter to the burden of proof and must always be considered separately. Insurance cases are nevertheless no different in principle from general civil cases in this regard and must apply the same principles. Oddly enough, given that the same judges are at work in

[250] [2006] SGCA 28.
[251] Such as the presumption of loss by perils of the seas: *Green* v *Brown* (1744) Str 1199. The rule concerns ships lost without a trace and is therefore mostly obsolete—nor is it relevant in principle to the present discussion since it does not involve fraud.
[252] See *The Elias Issaias* (1923) 15 Ll L Rep 186 and *Piermay Shipping Co. SA* v *Chester (The Michael)* [1979] 2 Lloyd's Rep 1. In the first case, the master and crew had scuttled the vessel and the only question on appeal was whether there was connivance by the owner. The Court of Appeal rejected the idea of a presumption that the owner was complicit and held that the owner's involvement had to be proven by insurers.
[253] For example, International Hull Clauses 2003 cl. 2.2.5 and Institute Time Clauses Hulls 1983 cl. 6.2.5.
[254] The proviso is present in International Hull Clauses 1983 cl. 6.2.5 and International Hull Clauses 2003 cl. 2.2.5. The differences between the two versions are immaterial.
[255] *Sealion Shipping Ltd v Valiant Insurance Co (The "Toisa Pisces")* [2012] 1 Lloyds Rep 252 (upon appeal this issue was not discussed).
[256] By way of recent example, *Ted Baker Plc and another v Axa Insurance UK Plc and others* (No 2) [2014] EWHC 3548 (Comm).

the insurance cases as in other cases, it appears from the more recent insurance case law that they have failed to appreciate the importance of some of the wider case law on the subject. Thus the recent case *GenesisUK.Net Ltd v Allianz Insurance Ltd* [257] cites as main authorities *National Justice Compania Naviera SA v Prudential Assurance Co Ltd (The Ikarian Reefer)*(No.1),[258] *The Captain Panagos DP*[259] and *The Zinovia*.[260] The standard of proof cited as a result is the balance of probabilities, but 'commensurate with the gravity of the charge'. In the following, the addition of the latter seven words will be challenged by seeking to evaluate the importance of wider developments in relation to the standard of proof for insurance cases.

4.3.3 Introduction

The Law Commissions' Insurance Contract Law Issues Paper 7 on fraudulent claims set out the standard of proof as follows.

> It is often said that as allegations of fraud are extremely serious, cogent proof is required to persuade a court that fraud has occurred. However, a recent House of Lords case has emphasised that 'there is only one civil standard of proof and that is proof that the fact in issue more probably occurred than not'.[261]

This of course does not purport to be the entire story. Indeed, there is a substantial amount of case law beyond the few cases upon which this assertion rests, and it will be appropriate to review the cases in the order in which they led up to the current position.

The quote above tells only the most recent part of the story. Historically, there was manifestly a rule to the effect that the criminal standard should be applied in civil cases, where criminal allegations were being made. That requirement has been incrementally reduced over the past century or so to the current point, which – it is argued - represents a state of some ambivalence. Once the criminal standard rule had been disposed of, there remained for a long time a rule to the effect that where very serious allegations are made against a person, the standard of proof in respect of those allegations is somehow more exacting than otherwise in civil cases. This is usually expressed as the standard being the usual balance of probabilities, but that the evidence must be 'commensurate with the gravity of the occasion'; or indeed that that the evidence must be especially convincing (or 'cogent') to reflect the

[257] [2014] EWHC 3676 (QB).
[258] [1995] 1 Lloyd's Rep 455.
[259] [1989] 1 Lloyd's Rep 33.
[260] [1984] 2 Lloyds Rep 264.
[261] Law Commission and Scottish Law Commission, Insurance Contract Law Issues Paper 7, *The Insurer's Post-Contract Duty of Good Faith* (July 2010) 24, available at <http://lawcommission.justice.gov.uk/docs/ICL7_Insureds_Duty_of_Good_Faith.pdf>, accessed 3 October 2012, referring to *Re B (Children) (Care Proceedings and Standard of Proof)* [2008] UKHL 35, [2009] 1 AC 11 at [13].

seriousness of the allegation. The effect is that it becomes more difficult to prove that the insured has behaved with dishonesty, because the judge will be reluctant to make a finding to that effect. The origins and current state of this rule and its impact on insurance cases will be dissected in the following.[262]

The rule is not well developed or even necessarily logical and there are signs that it is dissolving; more on which below. The wider question the subject of analysis here is whether this dissolution applies only to cases from specific sectors, or under a specific act, or to all civil cases including insurance cases.

4.3.4 The early cases: the criminal standard

Curiously, it appears that developments of the rule on standard of proof for allegations of fraud in civil cases began very recently.[263] There is only a small number of very early cases that discuss or at least evoke issues of standard of proof. Thus, *Thurtell* v *Beaumont*[264] was an insurance case concerning the destruction by fire of goods held in the plaintiff's warehouse. The insurers alleged that the plaintiff had deliberately set fire to the warehouse, which effectively amounted to an allegation of arson.[265] The judge had directed the members of the jury that they must be satisfied that the crime imputed to the plaintiff was as fully proved as would justify finding him guilty on a criminal charge for the same offence. This direction was approved upon appeal.[266] The case was authority for the proposition that instead of the civil burden of proof of 'more likely than not', the *criminal* standard of proof of 'beyond reasonable doubt' should be applied equally in civil cases, where the facts to be proved indicated criminal behaviour. Two further cases from the 19th century, which are worthy of mention, are *Boyce* v *Chapman and Brown*[267] and *Vaughton* v *London & North Western Railway Co*.j[268] The court there applied the civil standard of proof to thefts committed by persons not party to the litigation – an important distinction for reasons which will be discussed further below.

[262] Discussed in Ennis McBride, 'Is the Civil 'Higher Standard of Proof' a Coherent Concept?' (2009) 8(4) *Law, Probability & Risk* 323.
[263] Relevant cases are all from the 20th century. See also Mike Redmayne, 'Standards of Proof in Civil Litigation' (1999) 62(2) MLR 167–95 at 168, n. 3.
[264] (1823) 1 Bing 339.
[265] The fire cases noted above concerned the burden of proof in fire cases, but the allegation there was not that an offence had been committed, just that there had been negligence on the part of a servant; *Shaw v Robberds, Hawkes, and Stone* (1837) 6 Adolphus and Ellis 75; *Dobson v Sotheby* (1827) 173 E.R. 1091. On the separate issue of the influence of criminal law concepts on the interpretation of insurance policies, see Martin Wasik, 'Definitions of Crime in Insurance Contracts' [1986] JBL 45.
[266] The appeal was allowed on other grounds and direction for a new trial was given.
[267] (1835) 2 Bing NC 222.
[268] (1873–74) LR 9 Ex 93.

Interest in the issue was resuscitated as recently as the 1920s – the first being a Court of Appeal judgment in a marine insurance case, *The Elias Issaias*,[269] where the Court of Appeal adopted the description of Bailhache J at first instance of the standard of proof required:

> "This brings me to the real difficulty in the case. Was the scuttling done with the connivance of the owner? So to charge the owner is to accuse him of a fraud of the worst kind, and it is an axiom of English law, alike civil and criminal, that no man ought to be convicted of fraud except upon evidence that leaves no reasonable doubt of his guilt."[270]

The Court of Appeal, unlike the judge, was not convinced beyond reasonable doubt that the shipowner had connived in the wilful casting away of the vessel. Soon afterwards, the House of Lords was again tasked with hearing an insurance case involving issues of proof, namely *Lek* v *Mathews*[271] in which the House of Lords held that the claimant's alleged insurance fraud was sufficiently proven on the balance of probabilities.[272] It will be necessary to return to these cases below when dealing specifically with insurance cases.

There is further early, but valuable, reasoning in the matrimonial cases *Bater* v *Bater*[273] and *Preston-Jones* v *Preston-Jones*.[274] Previous cases were distinguished and matrimonial cases were recognised as a separate category in the case that subsequently came to be viewed as the leading case—*Hornal* v *Neuberger Products*[275] - where it was held that they were to be assessed according to the criteria set out by Denning LJ in *Bater* v *Bater*,[276] where he said:

> The difference of opinion which has been evoked about the standard of proof in recent cases may well turn out to be more a matter of words than anything else. It is of course true that by our law a higher standard of proof is required in criminal cases than in civil cases. But this is subject to the qualification that *there is no absolute standard in either case*. In criminal cases the charge must be proved beyond reasonable doubt, but there may be degrees of proof within that standard. As Best CJ, and many other great judges have said, 'in proportion as the crime is enormous, so ought the proof to be clear.' *So also in civil cases, the case may be proved by a preponderance of probability, but there may be degrees of probability within that standard.* The degree depends on the subject-matter. *A civil court, when considering a charge of fraud, will naturally require for itself a higher degree of probability than that which it would require*

[269] (1923) 15 Ll L Rep 186.
[270] Ibid. at 187.
[271] (1927) 29 Ll L Rep 141.
[272] (1927) 29 Ll L Rep 141.
[273] (1951) P 35.
[274] [1951] AC 391.
[275] [1957] 1 Q.B. 247.
[276] [1951] P 35.

> *when asking if negligence is established.* It does not adopt so high a degree as a criminal court, even when it is considering a charge of a criminal nature; but still it does require a degree of probability which is *commensurate with the occasion*.[277]

This has become the *locus classicus* for the peculiar standard of proof adopted by courts since.[278] It is to be noted that Denning LJ mentions a 'higher degree of probability'. As we shall see, to the extent that there is any academic debate at all about these issues, it focuses on the question that an intermediate standard of proof, higher than 'more likely than not' but not so strict as to approach 'beyond reasonable doubt' ought to be introduced. Such a standard exists in US law, where 'clear and cogent evidence' is required in some situations. It is not clear what Denning LJ may have intended with the words 'higher degree of probability', but he may either have intended some such higher standard, or he may have intended that more evidence would be required to reach the same standard and to make the fact in question 'more probable than not'.

While Lord Denning thus thought that the standard of proof in cases governed by the Matrimonial Causes Act 1950 was 'a degree of probability which is commensurate with the occasion',[279] we record from these early cases the vagueness of the expression 'a degree of probability which is commensurate with the occasion'. The law was at this stage far from coherent, and is perhaps best characterised as incipient.

4.3.5 *Hornal v Neuberger*: the civil standard

The leading case generally on the standard of proof in civil cases of fraud was until recently—and according to some judges remains—*Hornal* v *Neuberger Products Ltd*.[280] As will be seen, this case distinguished some, but not all, existing case law and provided a better foundation by supplying extended reasoning on the point. Following *Hornal* v *Neuberger*, the law was considered settled for many years and the case is still applied, although a recent trio of cases from the highest authority casts doubt on the applicability of *Hornal* and recent case law has taken a range of different approaches to the issue. The main proposition as to the standard of proof, supplied by *Thurtell* v *Beaumont*,[281] was

[277] *Bater* v *Bater* [1951] P 35 at 36–7 (emphasis added).
[278] Although Lord Hoffmann in *Re B (Children) (Care Proceedings and Standard of Proof)* [2008] UKHL 35, [2009] 1 AC 11 at [7] pithily dismissed the outcome with these words: 'the Court of Appeal managed to rule that although it was a misdirection for a judge in matrimonial proceedings to say that the criminal standard of proof applied to allegations of cruelty (*Davis* v *Davis* [1950] P 125) it was correct to say that they had to be proved beyond reasonable doubt'.
[279] *Bater* v *Bater* [1951] P 35 at 37.
[280] [1957] 1 QB 247.
[281] Supra.

disapproved by the judge at first instance in *Hornal* v *Neuberger*[282] (on which see further below); an assessment not questioned by the Court of Appeal in that case.

In *Hornal* v *Neuberger*, the plaintiff sought damages for *inter alia* fraudulent misrepresentation, alleging that the director of the defendant company had in the course of negotiations for the purchase of a used capstan lathe[283] stated that it had been reconditioned by a reputable firm of toolmakers. The defendants denied that the statement had been made. If it had been made, the director must have known it to be untrue. The case turned on an alleged fraudulent misrepresentation. There were two issues before the court, both involving the same representation allegedly made by the director – one whether there was a contractual warranty, and the other whether there had been a fraudulent misrepresentation. Had the criminal standard of proof applied, it would have been necessary to decide the same factual issue—the issue of whether a particular representation had been made—in two different ways: once in favour of Mr Hornal, and once in favour of Neuberger Products. The difficulty in deciding the question of fact before the judge at first instance was succinctly captured by Denning LJ as follows:

> If he was to apply the standard in civil cases—the balance of probability—he would hold that the representation was made by Mr. Neuberger: but if he was to apply the standard in criminal cases—proof beyond reasonable doubt—he would hold that the representation was not made.[284]

The judge at first instance held that the correct standard was the balance of probabilities rather than beyond reasonable doubt. He nevertheless rejected the claim because reliance on the fraudulent misrepresentation had not been demonstrated.

Upon appeal, the Court of Appeal unanimously settled on the lower civil standard chosen by the judge, but Denning LJ and Hodson LJ set the bar higher by building flexibility into the rule. The Court nevertheless found that the more exacting standard thus created was fulfilled and the appeal was allowed, or as Denning LJ put it:

> In some of those cases, particularly *Thurtell v. Beaumont* and *Issaias v. Marine Insurance Co Ltd* … the judges have said that the offence of arson or malicious damage must be as fully proved as a criminal charge: but the latest case in the House of Lords, *Lek v. Mathews*, … shows that that is putting too high a burden on the insurance company.[285]

Denning LJ went on to quote and discuss dicta of Lord Sumner:

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[282] [1957] 1 QB 247.
[283] A metalworking machine used for creating the same parts repeatedly.
[284] *Hornal* v *Neuberger Products Ltd* [1957] 1 QB 247, at 256.
[285] Ibid. at 258.

> Lord Sumner said that … 'on a civil issue I do not think more is required than a correct appreciation of the incidence and the shifting of the onus of proof and a reasonable estimate of the weight pro and con of the various parts of the evidence … I am just as reluctant to make the underwriters pay Mr. Lek many thousands of pounds, if he has been guilty of making a false claim, as to find him guilty of it if he has not. The whole question is whether it has been proved; and I think it has.' It is apparent that Lord Sumner considered that proof was only necessary according to the civil standard.[286]

The use of the criminal burden of proof in *Hornal* v *Neuberger* would have given rise to inconsistency: the same statement could be used to support a plea of breach of warranty as well as of fraud. Such a situation might lead a judge to use different standards of proof for the exact same statement, finding it proven on one plea but not on another. As Denning LJ put it, 'That would be bringing the law into contempt'.[287]

However, the civil standard was not an unambiguously clear rule – it was flexible according to the situation. Denning LJ said that the judge at first instance:

> reviewed all the cases and held rightly that the standard of proof depends on the nature of the issue. The more serious the allegation the higher the degree of probability that is required: but it need not, in a civil case, reach the very high standard required by the criminal law.[288]

Morris LJ said simply that the balance of probabilities applied, and although a judge might hesitate in coming to a conclusion that would ruin someone's reputation, he would not let that prevent him from following the evidence. These mixed statements have perhaps contributed to some of the confusion that can be seen in subsequent years. It will be noted that some legal systems employ an intermediate civil standard somewhere above the balance of probabilities. Does the statement of Denning LJ entail the introduction of such a standard? The statement itself is unclear, but fortunately we now know that he did not. But the statement of Denning LJ contrasts sharply also against that of Morris LJ, who appears to have rejected the idea that evidence 'commensurate with the gravity of the situation' was required.

4.3.5.1 The 'third party cases'

The Court of Appeal in *Hornal* v *Neuberger*[289] considered a line of so-called 'third party cases'. According to these, the crime of a person *not concerned* in the action may be established on a balance

[286] Ibid.
[287] Ibid. at 255.
[288] Ibid. at 258.
[289] Ibid. at 261, *per* Hodson LJ.

of probabilities (*Boyce* v *Chapman and Brown*[290] and *Vaughton* v *London & North Western Railway Co*.[291]).

In both cases, the loss arose from the felonious acts of persons employed by the defendant, not parties to the litigation. In *Boyce* v *Chapman and Brown*, a case from 1835, a request for a renewed hearing was declined. The defendant notably objected to the plaintiff's case not meeting the standard of proof required for a felony, but this was deemed insufficient grounds to disturb the judgment. The Court of Appeal pointed out that in a criminal trial, the person whose conduct was allegedly felonious (an employee of the defendant) could not have been called as a witness, but in a civil trial he could have been called by the defendant and the defendant therefore had to accept the ruling.[292]

Third party cases accordingly are cases where neither the defendant nor the claimant are themselves accused of any criminal act. In such cases, the earlier decisions provide authority for the proposition, unaffected by *Hornal* v *Neuberger*, that the standard of proof is the simple balance of probabilities. This is occasionally the situation in insurance cases, such as the marine insurance case, *The Mercandian Continent*,[293] where the insured owner of a shipyard supplied a forged document in order to defend its liability insurers against a third party liability claim from one of its clients.[294] Indeed, in insurance cases, it will often be a question of a fraud by a third party.[295]

Hodson LJ in *Hornal* v *Neuberger* noted with disapproval one existing argument for using the criminal standard:'every man has a right to his character and not to have the presumption of innocence rebutted unless the strict standard were adopted'.[296] He pointed out that such statements made the third party cases look incongruous. In third party cases, if the defendant were to assert that the claimant has relied on a fraud committed by a third party in advancing its claim, caution must (it is said) be exercised in order not to unduly expose a third party to public statements that it has acted fraudulently. While this rule had not been questioned in the third party cases, such a third party had just as little opportunity to defend himself as a claimant or defendant unable to give evidence under earlier procedural rules. Hodson LJ was therefore entirely right in saying that this reasoning 'made the

[290] (1835) 2 Bing NC 222.
[291] (1873–74) LR 9 Ex 93.
[292] In *Vaughton* v *London & North Western Railway Co* (1873–74) LR 9 Ex 93.
[293] *K/S Merc-Scandia XXXXII* v *Lloyd's Underwriters (The Mercandian Continent)* [2001] EWCA Civ 1275; [2001] 2 Lloyd's Rep 563; criticised in MacDonald-Eggers (2003) on the grounds that the right to avoid following a breach of duties of good faith is *sui generis*.
[294] It is noteworthy that in neither *Boyce* v *Chapman and Brown* nor in *Vaughton* do any of the judges mention a *heightened* burden of proof in civil cases involving allegations of a crime.
[295] The master of a ship in a marine insurance case occupies a particular position as the employee of the insured and is not necessarily a third party in the restricted sense intended here.
[296] *Hornal* v *Neuberger Products Ltd* [1957] 1 QB 247 at 261, *per* Hodson LJ, citing *Taylor on Evidence*, 12th edn, vol. 1 (Sweet & Maxwell: London, 1931) 106.

third party cases look incongruous'.[297] Hodson LJ's reasoning on third party cases relates only to the question whether the criminal or the civil standard of proof should be employed, and the conclusion is that it is the civil standard of proof. However, that conclusion is then complicated by the next issue.

4.3.5.2 How to apply the civil standard

While the Court of Appeal in *Hornal* v *Neuberger* did establish the balance of probabilities as the appropriate standard of proof, there was also a suggestion that a higher degree of probability has to be demonstrated, *commensurate with the occasion*. In establishing this approach, the Court of Appeal approved *Lek* v *Mathews*. Hodson LJ best encapsulated this in commenting on Lord Sumner's speech in *Lek* v *Mathews*, saying enigmatically:

> There is in truth no great gulf fixed between balance of probability and proof beyond reasonable doubt. Although when there is a criminal prosecution the latter standard is securely fixed in our law, yet the measure of probability is still involved in the question of proof beyond reasonable doubt.[298]

As shall be seen, this approach was far from sufficiently clear to lead to unequivocal judicial practice. The idea that there is 'no great gulf' between the civil and the criminal standards and that they might be mutually 'involved' does not allow a judge to direct himself clearly as to the standard of proof to be fulfilled. The only really surprising element is the lack of academic debate on the subject.[299]

4.3.5.3 Closing thoughts on *Hornal v Neuberger*

The judge at first instance in *Hornal* v *Neuberger* thus considered that the facts supported a finding of fraud on the evidence, without employing any higher standard of proof. The Court of Appeal had before it the same findings of fact. Statements to the effect that the standard of proof is variable and depends on the matter to be proven, and indeed that it is any higher than the balance of probabilities should therefore arguably be considered *obiter dicta*—if an enhanced standard had been required, the Court of Appeal could not have relied on the judge's findings of facts to allow the appeal. A question which arises is therefore to what extent *Hornal* v *Neuberger* can be used as support for a *refusal* to

[297] There are of course also several ways in which the third party's identity can be protected, should this be considered desirable, for instance by referring to the third party by initials rather than by full name in public reports.

[298] *Hornal* v *Neuberger Products Ltd* [1957] 1 QB 247 at 262.

[299] Although there was criticism of the judgment of the House of Lords in *R* v *Secretary of State for the Home Department Ex p Khawaja* [1984] AC 74 (HL), where the House of Lords adopted the civil standard of proof but considering the gravity of the issues at stake (habeas corpus in an immigration case), relied on the "flexibility of the civil standard of proof" (at [76]) as a means to "ensure that the court will require the high degree of probability which is appropriate to what is at stake" (*ibid*) , also saying that "the choice between the two standards is not one of any great moment. It is largely a matter of words" (at [76]). This reasoning came under immediate fire; see Rosemary Pattenden, 'The risk of non-persuasion in civil trials: the case against a floating standard of proof', CJQ 1988, 7(Jul), 220-233

allow an argument of fraud by the insurer.[300] With these two points in mind, it is evident that further cases must be analysed to assess the full extent of the rule.

In its analysis, the Court of Appeal organised existing cases into four groups: insurance cases, matrimonial cases, third party cases and 'residual cases'. The court then went on to dissolve that categorisation by (1) suggesting that the third party cases are 'illogically' decided; (2) by not including *Issaias* among the insurance cases; (3) by creating the innominate fourth category which is not united by any discernible substantive factor; and (4) by stating that the standard of proof was an issue depending on many factors. The outcome in *Hornal* v *Neuberger* turned on whether the claimant must prove the fraud to the criminal standard—beyond reasonable doubt—or whether the civil standard—the balance of probabilities—was sufficient. The judge at first instance had hesitated between the two and had settled on the civil standard. In each of the three Court of Appeal speeches, emphasis is placed on the notion that solid evidence is required for the impeachment of honest persons such as Mr Lek in *Lek* v *Mathews* who was said to have been a businessman of some standing, but the three judges are not united in their approach to the matter and no clear rule is stipulated, beyond the retreat from the criminal standard.

It is now appropriate to summarise the three important conclusions arising from *Hornal* v *Neuberger*. First, the criminal standard of beyond reasonable doubt was not to be used in civil cases. The Court of Appeal explicitly disapproved *Thurtell* v *Beaumont* on this point. Secondly, although the civil standard was to be applied, it was flexible in character and the degree of evidence required was 'commensurate with the occasion'. In addition, the Court of Appeal also recognised that different standards of proof will apply to different types of cases. The judgment of the House of Lords in *Preston-Jones* v *Preston-Jones* was said to be subject to a different standard of proof, because it was a marital case subject to the Matrimonial Causes Act 1950. We may therefore conclude that we must be open to the possibility that there is not a single rule of standard of proof, but that there are different categories for different types of cases. This in turn raises the question in what category insurance cases belong; more on which later.

4.3.6 The child protection trilogy of cases

While the development of the state of the law today can be traced back to just over a century, the most significant developments were triggered by a 1996 judgment of the House of Lords in *Re H (Minors)*,[301] which concerned the removal of children from parental custody on the suspicion of child abuse. The most important recent developments shaping the civil standard of proof have originated from the unlikely source of the law on child protection. Just as the rejection of a fraudulent insurance

[300] Much like *Carter* v *Boehm* (1766) 3 Burr 1, the case that forms the basis for insurance contracts as contracts of good faith, was a case where the assured was in fact entitled to recover.
[301] [1996] AC 563.

claim, the cases involve a civil law consequence of a criminal fact. The three cases are *Re H (Minors),*[302] *Re B (Children)*[303] and *Re S-B (Children).*[304] The House of Lords and the Supreme Court shed fresh new light on the standard of proof, but at the same time raised crucial questions that remain unanswered; while these cases provide valuable guidance, they could also be taken to confirm that child protection is a separate category unrelated to insurance cases. They provide certainty to one category of cases and valuable reasoning to others, but nevertheless uncertainty is as great as ever in relation to other types of cases, including those concerning insurance.

Thus, the concept of a civil standard of proof 'commensurate with the circumstances' has some unsuitable consequences, best illustrated by the particular facts of *Re H (Minors)*. In that case, a care order was sought in respect of the sisters of a young woman who had accused the mother's husband of rape, but where the man had been acquitted of the allegations.[305] The House of Lords interpreted the Children Act 1989, which provided that a care order may be given if it is likely that a child will suffer abuse, and concluded that the civil standard was appropriate. In addition, Lord Nicholls of Birkenhead approved the dictum from *Re Dellow's Will Trusts*: 'The more serious the allegation the more cogent is the evidence required to overcome the unlikelihood of what is alleged and thus to prove it'[306]. Lord Nicholls went on to say:

> "When assessing the probabilities the court will have in mind as a factor, to whatever extent is appropriate in the particular case, that the more serious the allegation the less likely it is that the event occurred and, hence, the stronger should be the evidence before the court concludes that the allegation is established on the balance of probability. Fraud is usually less likely than negligence."[307]

While this rule of proof might appear to make sense, it is entirely incongruous in its effect, as can be seen quite clearly in care order cases. The strikingly inappropriate rule of proof provides in effect that the worse the abuse, the less likely that the child can be protected by removal from its parents, because more evidence, or more cogent evidence is needed! It will be argued in the following that while the outcome is certainly not as offensive in insurance cases, the rule itself is still illogical and inappropriate.

Both the House of Lords and the Supreme Court have subsequently retreated from the statement of Lord Nicholls – but arguably, not far enough. In *Re B (Children)* [308] and *Re S-B (Children)*[309] (both

[302] [1996] AC 563.
[303] [2008] UKHL 35, [2009] AC 11.
[304] [2009] UKSC 17, [2010] 1 AC 678.
[305] The standard of proof in that case being 'beyond reasonable doubt'.
[306] *Re Dellow's Will Trusts* [1964] 1 WLR 451 at 455, *per* Ungoed Thomas J.
[307] Ibid. at 586.
[308] [2008] UKHL 35, [2009] AC 11.

child abuse cases), the standard of proof of the balance of probabilities was emphasised.[310] In *Re B (Children)*, Lady Hale, giving the leading speech, concluded that

> "the standard of proof in finding the facts necessary to establish the threshold under section 31(2) or the welfare considerations in section 1 of the 1989 Act is the simple balance of probabilities, neither more nor less"[311]

This conclusion followed a discussion which acknowledged that *Re H (Minors)* and, in particular, the speech of Lord Nicholls had, perhaps unintentionally, left open the possibility of a 'heightened civil standard', indistinguishable from the criminal standard. The House of Lords in *Re B (Children)* adopted the dicta of Lord Lloyd in *Re H (Minors)*, to the effect that the standard of proof ought to be the simple balance of probability, however serious the allegations involved. Lord Lloyd there said as follows:

> "There remains the question whether anything should be said about the cogency of the evidence needed to 'tip the balance'. For my part I do not find those words helpful, since they are little more than a statement of the obvious; and there is a danger that the repeated use of the words will harden into a formula which, like other formulas (especially those based on a metaphor) may lead to misunderstanding"

This notion that more serious allegations required more cogent proof, considered by Lord Nicholls in *Re H (Minors)* , was said in Re B (Children) to be a misinterpretation of the latter's words. Lady Hale's further explanation is worth citing in full:

> "the standard of proof … is the simple balance of probabilities, neither more nor less. Neither the seriousness of the allegation nor the seriousness of the consequences should make any difference to the standard of proof to be applied in determining the facts. The inherent probabilities are simply something to be taken into account, where relevant, in deciding where the truth lies.[312]

This must be interpreted as an intentionally diffident way of phrasing the matter, designed to avoid it turning into a formula. Lady Hale went on to emphasise that the seriousness of the consequences of making a finding that an offence has been committed should not be overstated, because the consequences, are serious either way: "A child may find her relationship with her family seriously disrupted; or she may find herself still at risk of suffering serious harm. A parent may find his

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[309] [2009] UKSC 17.
[310] The question as to whether these cases, although they relate to decisions in respect of the statutorily mandated removal of children from parents suspected of child abuse, can be properly viewed as authoritative for other civil cases is considered further below.
[311] [2008] UKHL 35, [2009] AC 11 at [70].
[312] At [70].

relationship with his child seriously disrupted; or he may find himself still at liberty to maltreat this or other children in the future."[313] This observation translates perfectly into the insurance context, where the result of a finding of fraud will be either that the reputation of the insured is tainted, or that the insurer is unjustly relieved of upholding its bargain. Finally, as to the seriousness of the allegation, Lady Hale pointed out that there is no logical or indeed necessary connection between seriousness and probability. "Some seriously harmful behaviour, such as murder, is sufficiently rare to be inherently improbable in most circumstances. Even then there are circumstances, such as a body with its throat cut and no weapon to hand, where it is not at all improbable."[314] Again, this translates perfectly well to the insurance situation. There appears to be no logical or humanly realistic reason to stipulate or presume that insurance fraud is in any way unlikely to be committed. Lady Hale went on to elaborate the point as follows. "It may be unlikely that any person looking after a baby would take him by the wrist and swing him against the wall, causing multiple fractures and other injuries. But once the evidence is clear that that is indeed what has happened to the child, it ceases to be improbable. … The inherent improbability of the event has no relevance to deciding who that was. The simple balance of probabilities test should be applied."[315]

The rule enunciated in *Re B (Children)*, while deriving from a case of care proceedings, is therefore entirely appropriate also for insurance cases. Indeed the reasoning of Lady Hale does not indicate that she intends to limit the rule to care cases. The precedent should therefore carry just as much weight in insurance cases.

In the last of the three cases, *Re S-B (Children)*,[316] Lady Hale gave the judgment of the court. The case addressed the adverse outcome mentioned above of a heightened requirement of proof. Two propositions were drawn from existing case law;[317] first, from *Re H (Minors)*: 'if the case is based on actual harm, the court must be satisfied on the balance of probabilities that the child was actually harmed'.[318] The second proposition was that 'if the case is based on the likelihood of future harm, the court must be satisfied on the balance of probabilities that the facts upon which that prediction was based did actually happen'.[319] The court again dismissed the 'heightened standard of proof' as a judicial tool other than in specifically prescribed cases. The question to be addressed was that of inherent probabilities: namely that it was inherently less likely that a serious offence would be committed than a less serious one, and that this would influence the approach of judges to the

[313] At [71].
[314] At [72].
[315] At [73]
[316] [2009] UKSC 17, [2010] 1 AC 678.
[317] The case in fact discusses three propositions derived from *Re H (Minors)*, but the third is not relevant for present purposes: it holds that the risk of future harm need not be found on the balance of probabilities but the lower standard of "a real possibility, a possibility that cannot sensibly be ignored" is sufficient; para 8.
[318] *Re S-B (Children) (Care Proceedings: Standard of Proof)* [2009] UKSC 17, [2010] 1 AC 678 at [8].
[319] Ibid.

evidence. The main issue addressed by the court in this case was the so-called 'whodunit' problem, neatly encapsulated by Lord Hoffmann in *Re B (Children)* :

> If, for example, it is clear that a child was assaulted by one or other of two people, it would make no sense to start one's reasoning by saying that assaulting children is a serious matter and therefore neither of them is likely to have done so. The fact is that one of them did and the question for the tribunal is simply whether it is more probable that one rather than the other was the perpetrator.[320]

Thus, the question in child care cases splits into two issues: first, whether on the balance of probabilities the child has suffered harm and second, which of the two parents has inflicted the harm. The 'whodunit' problem is highly relevant to insurance cases, where it is known from the outset of the claim that the loss has happened. In cases of, for instance, arson or the deliberate sinking of a ship, it will also be known that someone has committed a criminal act, but it will not be known whether it is the insured or a third party who has committed the act. We will therefore return to this issue later. For the moment, it suffices to say that the Supreme Court in *Re S-B (Children)* held that the plain balance of probabilities should be applied both to the issue of whether there had been harm and to the issue of which parent had inflicted such harm.

There is no explicit statement in these cases as to whether the Law Lords intend their reasoning to apply outside the law on child protection orders. Nevertheless, the reasoning is of general applicability and it would not make sense for a cogent analysis to apply in one area of the law, but not in others. The central dicta arguably permit a reading of the cases as of general applicability; not least: 'I think that the time has come to say, once and for all, that there is only one civil standard of proof and that is proof that the fact in issue more probably occurred than not'.[321] Lady Hale cited this dictum in *Re S-B (Children)*, and went on to say:

> "All are agreed that *Re B* reaffirmed the principles adopted in *Re H* while rejecting the nostrum, 'the more serious the allegation, the more cogent the evidence needed to prove it', which had become a commonplace but was a misinterpretation of what Lord Nicholls had in fact said."[322]

Lady Hale herself said in *Re B (Children)* :

> "There are some proceedings, though civil in form, whose nature is such that it is appropriate to apply the criminal standard of proof. Divorce proceedings in the olden days of the

[320] *Re B (Children) (Care Proceedings: Standard of Proof)* [2008] UKHL 35, [2009] AC 11 at [15].
[321] *Re B (Children) (Care Proceedings: Standard of Proof)* [2008] UKHL 35, [2009] AC 11 at [13], *per* Lord Hoffmann, cited by Baroness Hale in *Re S-B (Children) (Care Proceedings: Standard of Proof)* [2009] UKSC 17, [2010] 1 AC 678 at [11].
[322] *Re S-B (Children) (Care Proceedings: Standard of Proof)* [2009] UKSC 17, [2010] 1 AC 678 at [13].

> matrimonial 'offence' may have been another example (see *Bater* v *Bater* [1951] P 35). But care proceedings are not of that nature. They are not there to punish or to deter anyone. The consequences of breaking a care order are not penal. Care proceedings are there to protect a child from harm. The consequences for the child of getting it wrong are equally serious either way."[323]

It is clear from the first words of this paragraph that Lady Hale considers such proceedings the exception, not the rule. The rest of her reasoning, cited above, is clear and principled and there is no reason why it should be confined to care proceedings, although that is the context in which she presents the argument.

Considering the specific type of case at issue, it may be noted that it is immediately apparent that care order cases based on a specific statutory provision are merely the most striking illustration of the adverse consequences of the application of a heightened standard of proof. Care order cases, although just as 'civil' as insurance and other contract cases, involve delicate issues of human rights and child protection.[324] Baroness Hale in *Re S-B (Children)* stated that the European Convention on Human Rights informs the test and the process for intervening in the family lives of children and their parents, and goes on to say that: 'The jurisprudence of the European Court of Human Rights requires that there be a "pressing social need" for intervention and that the intervention be proportionate to that need'.[325] It is submitted that due to this basic quality of the child care cases, and not least the associated difficulty in assessing legal issues affecting vulnerable individuals, caution must generally be exercised in deriving support for a general rule for contract law (including insurance law) cases from care order cases. The rule ought therefore to apply *a fortiori* in cases where no human rights are at issue, and the positive finding can be arrived at with a lighter heart than if the consequence is to deprive children of their parents. Child protection cases, like those concerning sexual abuse, anti-social behaviour orders or immigration, raise issues of human rights and protection of individuals. Where there are no such concerns, i.e. in civil cases, such as insurance cases, where the only matters at stake are a pecuniary sum or occasionally the delivery-up of a particular item, and the reputation of one or other of the two business partners, there is little discernible reason to apply a *more* protective rule than in the child protection cases. This was recognised nearly a century ago by Viscount Sumner:

> "I am just as reluctant to make the underwriters pay Mr. Lek many thousands of pounds, if he has been guilty of making a false claim, as to find him guilty of it if he has not. The whole question is whether it has been proved; and I think it has."[326]

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[323] *Re B (Children) (Care Proceedings: Standard of Proof)* [2008] UKHL 35, [2009] AC 11 at [69].
[324] Ibid. at [6]–[7].
[325] *Re S-B (Children) (Care Proceedings: Standard of Proof)* [2009] UKSC 17, [2010] 1 AC 678 at [7].
[326] *Lek* v *Mathews* (1927) 29 Ll L Rep 141 at 164.

It is apparent that there is judicial confusion. Recent case law shows considerable divergence on the point. A striking example of where a judge considered that *Hornal* v *Neuberger* still provides the ultimate authority in such cases. The *Hornal* v *Neuberger* analysis was applied as recently as December 2010 in the insurance case *Templeton Insurance Ltd* v *Motorcare Warranties Ltd*,[327] where Simon J said[328] that the elements of the tort of deceit 'must be established by reference to the heightened burden of proof as discussed in [*Hornal* v *Neuberger*]'. He said this without further reflection and in the process of directing himself as to the law on misrepresentation and the tort of deceit, but the reference is relevant because it confirms that courts have not uniformly interpreted the child protection cases as possessing general relevance in civil cases. Insurance cases must therefore, for the time being, be assessed applying the old measuring stick and not the recently revised one. Further, in the personal injury cases forming the basis of insurance claims in the next chapter, judicial mention of evidence 'commensurate with the gravity of the accusation' or some similar form of words is so ubiquitous that it has certainly hardened into the rule feared by Lord Lloyd. Whether this is a desirable state of affairs is the next question.

4.3.7 How should the child protection cases be used in insurance cases?

4.3.7.1 The 'whodunnit' problem and insurance law

Many, although not all, insurance cases are examples of 'whodunnit' problems, situations that may be distinguished from the basic case of proving criminal or fraudulent activity, such as that in *Hornal* v *Neuberger* and many other cases. Instead, the question is not whether the fraud or other criminal activity in fact happened – the activity is in fact known to have happened, but it is not known who caused it. While the court may be reluctant to conclude that the assured himself caused the loss, it may be entirely clear from the situation that the damage was in fact perpetrated by someone, although the perpetrator is unknown.

Before the problem was addressed by the House of Lords in *Re S-B (Children)*[329] it arose in an insurance case. In *Bolton* v *Ing*,[330] Mr Bolton sued Mr Ing as representative underwriter of a Lloyd's syndicate, claiming in respect of his combined cafe and retail unit which had been seriously vandalised over night by unknown perpetrators. The underwriter argued three pertinent defences: (1) the damage had been intentionally perpetrated by Mr Bolton or persons working for him; (2) the burglar alarm had been switched off; and (3) the claimant had failed to use all reasonably practicable

[327] [2010] EWHC 3113 (Comm).
[328] Ibid. at [173].
[329] [2009] UKSC 17, [2010] 1 AC 678.
[330] Unreported (1998) QBD, Simon QC.

means to prevent loss within the meaning of the policy, by writing the alarm code on the panel. In directing himself, the judge cited *Re H (Minors)*[331] as authority for the following proposition:

> "… when assessing the balance of probabilities the Court will have in mind as a factor, to whatever extent is appropriate in the particular case, that the more serious the allegation, the less likely it is that the event occurred and, hence, the stronger should be the evidence before the Court concludes that the allegation is established on the balance of probabilities."[332]

Noting the words 'the less likely it is that the event occurred', the reasoning here would seem to apply to cases where it is unclear whether the alleged event occurred or not. If it is in fact known that the damage event occurred and therefore must have been perpetrated by some person or other, and if there is an insurance claim in respect thereof, it is submitted that it would be wrong to consider it 'inherently unlikely' that the assured had himself perpetrated the damage. One person or other *has* perpetrated the damage, and while it may be 'inherently unlikely' that any given person has done so, the inherent unlikelihood in respect of the assured himself is arguably *lower* than for the general population, given the obvious motive of claiming on the insurance (as well as, usually, means and opportunity). This reasoning was subsequently borne out by the reasoning of the Supreme Court in *Re S-B (Children)*.

The result in *Bolton* v *Ing* was probably nevertheless correct because, having thus stated the rule, the judge went on to make an all-round assessment, including the likelihood of the assured having perpetrated insurance fraud.

4.3.7.2 A lighter burden: following *The North Star*?

An additional perspective to the whodunnit problem arises where the true facts as to whether it is the assured or a third party who has caused the damage cause the damage to be covered under a different policy depending on who has perpetrated it. In *The North Star*,[333] the insured claimed under its war risks policy for a ship sunk by an explosion, caused by an unspecified third party. If instead it was the ship's crew that caused the explosion, the damage would be covered not by the war risks insurance but by the barratry peril in the hull insurance. If the insured had connived in that damage, it would in turn have become a matter of a scuttled vessel and of wilful misconduct by the insured, which (at the time) must be proven by the insurers on the standard of proof in *Re H (Minors)*. War risks insurers were therefore in the somewhat unusual position of having a choice between attempting to prove

[331] [1996] AC 563.
[332] *Bolton* v *Ing*, unreported (1998) QBD at 7.
[333] *North Star Shipping Ltd* v *Sphere Drake Insurance Plc* [2005] EWHC 665 (Comm), [2005] 2 Lloyd's Rep 76, at first instance; *North Star Shipping Ltd* v *Sphere Drake Insurance Plc* [2006] EWCA Civ 378, [2006] 2 Lloyd's Rep 183.

either that the explosion was caused by a crew member, a fact that would normally fall within the burden of proof of the insured, or that the shipowners had conspired to cause the damage.

As it happened, the insurers elected not to pursue the barratry route. At first instance, Colman J nevertheless commented in the following terms:

> "In the present case the insurers' case has always been that the owners were complicit: it has not been pleaded or suggested that, in the alternative, the damage was barratrous. Had it been advanced that the vessel was damaged by or on behalf of the crew for the purpose of injuring the owners, I should have rejected that contention as so intrinsically improbable that it could at once be totally discounted."[334]

The language used brings to mind the proscribed Sherlock Holmes logic of "when you have eliminated the impossible, whatever remains, however improbable, must be the truth?" of *The Popi M*,[335] However, it is apparent that Colman J did not arrive at his conclusion because he considered it inherently unlikely that a crew member would stoop to barratry; but because 'on the night of the explosion all such persons were on board the vessel in or close to the crew accommodation at the after end above the engine room'.[336] The judge went on to say:

> "It is intrinsically so highly improbable that they would have caused a bomb to be detonated adjacent to the hull immediately below where they were spending the night that this possibility can be ignored as fanciful."[337]

Without therefore considering the crew's inherent propensity to commit crime or the potential damage to their reputation that would have been certain to ensue, given that they would have immediately become unemployable, the judge did take into account that the particular crime in question would have placed the crew members personally in significant physical peril, and required no particular standard of proof for that fact. The same reasoning may be extended to apply to other insurance claims situations to arrive at a more realistic and comprehensive view of the facts where the existence of the reward for the insurance is taken into account in the assessment of the situation on the facts. Thus, for instance, the judge's reasoning would accord with the early case of *Lek* v *Mathews*,[338] where a stamp collector submitted a large claim asserting that he had lost part of his collection. It subsequently transpired that this was not true. The House of Lords declined to order the insurers to pay the indemnity. In *Lek* v *Mathews* the claim was not initially fraudulent (as the House of Lords

[334] *North Star Shipping Ltd* v *Sphere Drake Insurance Plc* [2005] EWHC 665 (Comm), [2005] 2 Lloyd's Rep 76 at [84].
[335] *Rhesa Shipping Co* v *Edmunds (The Popi M)* [1985] 1 WLR 948, at p 955.
[336] Ibid. at [84].
[337] Ibid.
[338] (1927) 29 Ll L Rep 141.

found) but it subsequently became so when Mr Lek decided to add to the claim to reach the threshold value that would allow him to succeed. It has subsequently been clarified that this does not matter to the remedy applied to fraudulent claims—a true claim fraudulently enhanced equally attracts the application of the fraudulent claims rule in insurance contract law; see *Agapitos* v *Agnew (The Aegeon)* [339] and there is no reason why other factors such as the assessment of the validity of the policy would be any different. As for Mr Lek's actions and attitude, it would appear that they were directly caused by the insurance claims situation—the very fact that there was insurance encouraged Mr Lek to enhance the description of his loss so as to meet the lower threshold for the claim.

If then an enhanced standard of proof were appropriate where the allegations in themselves and the consequences of a finding of fraud are of a particularly serious nature, an insurance case clearly does not qualify for such an enhanced standard of proof. The consequences of a finding of insurance fraud is simply that the whole claim is forfeit—a punitive rule in the civil setting, but not one involving habeas corpus or other human rights and fundamental freedoms; nor does it involve such serious consequences as the taking into care of children by removal from their parents. A finding of insurance fraud is not even likely to be particularly damaging to a person's business reputation or to raise many eyebrows in a business context - although it is certain to impact the ability to obtain insurance in future. *Re H (Minors)* does not, strictly speaking, decide cases other than child care cases; nor does *Re S-B (Children)* or *Re B (Children)*. Therefore the question arises as to whether those cases or *Hornal* v *Neuberger* provide the leading precedent in civil cases not falling under the Children Act 1989.

4.3.7.3 Divergent judicial practice (or judicial confusion)

The issue of standard of proof has been the subject of judicial attention both in the House of Lords and in the Supreme Court in recent years, but while there is good, clear precedent, the true scope of those cases is nebulous and subsequent case law has not settled into a clear path. More recently, there are cases moving in every direction, usually without reasoning.

On the other hand, the *Hornal* v *Neuberger* rule of the standard of proof has never been expressly disavowed in any cases other than *Re H (Minors)*, *Re B (Children)* or *Re S-B (Children)*. Indeed the case was directly cited in *Templeton Insurance Ltd* v *Motorcare Warranties Ltd*,[340] where Simon J said:[341] 'In addition, all these elements must be established by reference to the heightened burden [sic] of proof as discussed in [*Hornal* v *Neuberger*]'. The judge referred to the heightened standard of proof, but did not indicate whether he considered that he was thereby referring to the flexible standard

[339] [2002] 2 Lloyd's Rep 42.
[340] [2010] EWHC 3113 (Comm).
[341] Ibid. at [173].

(as in *Re H (Minors)*) or to the 'cogent evidence' manifestation of the higher standard of proof. However, the fact remains that in the minds of judges the rule is alive, if not well.

Even more recently, Wyn Williams J in *Goldsmith Williams (a firm)* v *Travelers Insurance Company Ltd*[342] applied this rule to a case involving dishonest conduct. The claim was based on the alleged dishonest conduct of the defendant solicitor in relation to moneys obtained and held by her for the purpose of a property transaction, and thus called into play her professional liability cover. The judge stated:

> "I should record that submissions were addressed to me about the approach I should adopt to the necessary standard of proof given that criminal or potentially criminal conduct was being alleged against both Mr [A] and Ms [U]. As it happens, following the completion of the hearing before me, the Supreme Court considered this issue authoritatively in *S-B (Children)* … The standard of proof is the balance of probabilities."[343]

This judge thus opted for a straightforward interpretation of the rule and did not venture into a more advanced discussion, which would have been interesting given that the case involved the professional integrity of a solicitor and thus that a finding of inappropriate or even fraudulent conduct would have struck particularly severely and at least indirectly have entailed consequences for her at the professional level. Even in the absence of discussion, however, it is noteworthy that the judge adopted the revised approach of the Supreme Court in a civil case without any bearing whatsoever on child protection.

In *Aviva Insurance Ltd* v *Brown,*[344] decided on 25 February 2011, the judge noted[345] that the parties agreed that the burden and standard of proof was as in *Re H (Minors)* , thus applying the first of the child care cases, but omitting reference to *Re B (Children)* and *Re S-B (Children).* Such an approach is arguably unprincipled – if *Re H (Minors)* applies, so too should the two subsequent cases.

Thereafter in *Parker & Another v The National Farmers Union Mutual Insurance Society Limited*[346] the judge again stated the standard of proof in the traditional manner: "The standard of proof in civil matters is the balance of probabilities but the evidence relied upon must have a strength or cogency commensurate with the gravity of the allegations made…"[347] and "the strength or cogency of the

[342] [2010] EWHC 26 (QB).
[343] Ibid. at [26].
[344] [2011] EWHC 362 (QB).
[345] Ibid. at [60].
[346] [2012] EWHC 2156 (Comm), [2013] Lloyd's Rep. IR 253.
[347] Ibid at [6].

evidence relied upon by the NFU, if it is to discharge the burden of proof, must be commensurate with the gravity of that very serious allegation."[348]

It might be added that among the cases discussed in chapter 5, virtually all refer in some form of words or other to a 'cogency of the evidence commensurate with the allegation.' It is therefore obvious that clearer guidance will be necessary on the rule on the standard of proof.[349]

4.3.8 Insurance claims—a category apart?

The higher standard of proof has arguably caused problems in the development of the law of insurance contracts. Other jurisdictions have rejected the model.[350] It is time to ask the question whether England and Wales should follow the same route. If it should, the next step is to ask on what basis this should be done. In the following we will outline two hypotheses on which insurance cases may be considered different from other cases.

There are various ways of arriving at a workable model of the standard of proof for insurance claims cases. The first option is to state that the only (or predominant) factor in insurance claims cases is the rule of law that insurance policies are contracts of good faith. This option however is barely arguable where good faith has been relegated to a 'doctrine' or 'character' of an insurance contract, fraudulent claims are dealt with under a common law rule of uncertain origin and *The Star Sea* has drawn a line in the sand where good faith duties cease to apply at the start of litigation. To allow the standard of proof employed to be influenced by good faith requirements would be quite absurd where judges are otherwise left to rely on procedural tools at their disposal.

The second option is to accept that different rules of evidence apply to different categories of cases (as per the reasoning in *Hornal* v *Neuberger*), thus establishing that insurance claims cases are a category apart which requires a specific standard of proof, and to seek out a precedent to be applied specifically to such cases, for instance *The Ikarian Reefer* or T*he Captain Panagos DP*. If so, a coherent manner of interpretation of existing cases is required.

Case law has not been consistent in the insurance context. The decision in *The Elias Issaias*,[351] a case of scuttling where the Court of Appeal held that the standard of proof in such a case was 'beyond

[348] Ibid. On the evidence, the judge found some allegations proven, others not.
[349] It had been hoped that *Gale* v *Serious Organised Crime Agency* [2011] UKSC 49, [2011] 1 WLR 2760 would provide some further guidance. However, the Supreme Court stuck narrowly to the case before it in holding that in civil proceedings to recover the alleged proceeds of crime, where unconnected criminal proceedings abroad had resulted in an acquittal, a civil standard of proof of the balance of probabilities should be used. Although the nature of the standard of proof was apparently argued, there was no helpful *ratio* on the point.
[350] P. J. Schwikkard and S. E. van der Merwe, *Principles of Evidence*, 3rd edn (Juta: Cape Town, 2009).
[351] (1923) 15 Ll L Rep 186.

reasonable doubt', may be contrasted with *Lek* v *Mathews*.[352] The prospects of this claim in respect of a stamp collection essentially turned on whether the insured, a successful businessman, could be taken at his word or if the court ought to doubt his version of events.[353] Viscount Sumner in the House of Lords demonstrated no hesitation in holding that the claimant's status as a successful businessman was a mere circumstance and that the court must find that he had been dishonest, provided the evidence compelled it to do so. This early case is, it is submitted, sufficient authority for disregarding any subsequent case law on proof 'beyond reasonable doubt' or on a 'heightened standard of proof', or indeed a requirement of 'cogent evidence commensurate with the situation'.

The child care cases, *Re H (Minors)* , *Re B (Children)* and *Re S-B (Children)*, do not formally distinguish prior contract and insurance cases such as *Lek* v *Mathews* or *Hornal* v *Neuberger*. Those earlier cases can therefore arguably underpin a discrete rule to be applied in insurance contract law cases. The advantage of this would be to permit the law to develop independently and not to be affected by the quasi-administrative and constitutional cases involving human rights and personal security claims. However, such a position disregards the fact that we are now in possession of a series of cases from the highest judicial authority setting out a clear rule for the standard of proof, in favour of a rule to be developed, given that existing insurance cases do not exactly form a coherent line.

4.3.9 Policy

A common argument is that a heightened standard of proof should be employed where the consequences of the case are very serious, particularly in fraud (including insurance fraud) cases—because it would be very serious for an innocent person to be found to be fraudulent, even in civil proceedings. The usefulness of the idea is open to doubt. In insurance cases, in particular, there is a clear opposing social or policy interest which is just as valid as the protection of an individual person and his or her reputation. That opposing interest is the legitimate social need to limit the number and combined size of fraudulent insurance claims and to prevent that guilty individuals get away with fraud, because successfully executed insurance fraud exacerbates the position of insurance companies and thereby indirectly of other insureds in a society that relies heavily on insurance to spread and share risk.

A rare commentator on the difficulty involved in balancing the various interests writes:

> "Judges in certain civil cases have the laudable desire to adopt a more rigorous approach before finding proved serious allegations that could ruin those against whom they are made. But, rather than bite the bullet of classing all such cases as quasi-criminal and requiring the ['beyond reasonable doubt'] standard of proof, judges try to find a half-way house by using

[352] (1927) 29 Ll L Rep 141.
[353] For the further facts, see 4.3.7.2 above.

> the ['on the balance of probabilities'] test while requiring an increase of some mythical element, be it 'cogency' or 'scrutiny', which is not related to probability. The difficulty then is that the flexibility then achieved is either entirely trivial (such as 'unlikely things are unlikely to happen'), non-existent (such as the 'careful as opposed to careless scrutiny' test) or subject to the whims of hard reality (which may result in the standard of proof being unattainable or too easy to attain or simply unmeasurable)."[354]

He concludes (unlike this author) that all civil cases where criminal allegations are made should be consistently dealt with as quasi-criminal, with the criminal standard of proof. [355] However, in this author's view there are good reasons why the standard of proof in insurance cases should remain the balance of probabilities.[356]

Most importantly, an insurance case is not a matrimonial case or a child protection case. No fundamental rights or freedoms are at stake in an insurance case—merely the reputation of the person and their opportunity to recover the indemnity. The battle in court is an adversarial one and there is no humanitarian reason or particular need to give either party the upper hand. The standard of proof, unlike the rules of substantive law, is a rule not to determine the relationships between the parties, but to guide the judicial assessment of cases – it is a rule for judges, whose function is to be arbiters in civil matters assessed in the context of an adversarial procedure. The effect of a judge's adoption of a heightened standard of proof - of whatever description - even if by mere implication of special circumstances, is to implicitly side with one of the parties.

4.3.10 Conclusion

The courts have over the years appeared to half accept a rule of evidence, or perhaps rather a notion of evidence for the standard of proof that is at best unprincipled and at worst unpredictable. It might be said that if modern English Courts have steered clear of the Arthur Conan Doyle trap of the Sherlock Holmes fallacy, they have nevertheless adopted a quote by an author of works of fiction as the guiding light:

> "I believe in evidence. I believe in observation, measurement, and reasoning, confirmed by independent observers. I'll believe anything, no matter how wild and ridiculous, if there is evidence for it. The wilder and more ridiculous something is, however, the firmer and more solid the evidence will have to be."

[354] See Ennis McBride, 'Is the Civil 'Higher Standard of Proof' a Coherent Concept?' (2009) 8(4) *Law, Probability & Risk* 323.
[355] Ibid.
[356] For an evaluation of the procedural side of the arguments, see Adrian Zuckerman , 'Must a Fraudulent Litigant Be Allowed to Think: If the Fraud Is Successful, I Will Gain Much; If It Is Not, I Will Still Recover My Legitimate Claim?' (2011) 30(1) *C*JQ 1.

The second and third sentences of this quote are remarkably apt to illustrate an intellectual yoke shouldered by contemporary judges, who have shown themselves singularly reluctant to cast it off even in the presence of Supreme Court precedent.

4.4 Conclusion

The substantive law on fraudulent claims has crystallised only relatively recently. As for the procedural side, it may be ventured that the importance of the precise application of rules on the burden and standard of proof is generally underestimated in English law. Attention to the burden and standard of proof is surprisingly scarce or superficial, not least in insurance cases. For a recent example, see *Sharon's Bakery (Europe) Ltd* v *Axa Insurance Plc*[357]. Here, the judge simply stated, with reference to *Re H (Minors)*[358] that the burden was on the insured—a trite legal rule surely requiring no support from the House of Lords for its application—and supplied no discussion at all of the standard of proof.[359] The explanation for this awkwardness and reluctance in tackling the burden and standard of proof was provided by Lord Brandon in *Rhesa Shipping* v *Edmunds (The Popi M)* ,[360] when he said:

> "No judge likes to decide cases on burden of proof if he can legitimately avoid having to do so. There are cases, however, in which, owing to the unsatisfactory state of the evidence or otherwise, deciding on a burden of proof is the only just course for him to take."[361]

This judicial attitude to the burden and standard of proof as a solution of last resort is arguably the very reason why the most fundamental rules of any justice system are still in the process of crystallising.

Although the law on fraudulent claims has now, at least to a certain extent, become settled, some of that clarity came only at the turn of the 21st century, after hundreds of years of insurance practice both at Lloyd's and in the extended insurance markets, that is in commercial and consumer markets alike. However, the rule on the standard of proof has still not been fully developed or manifestly established judicially, and it is submitted that it remains in an unsatisfactory state.

How then does this matter? For insurers, the implications are obvious: they must always hesitate to reject a claim on the basis of fraud. The most fundamental effect of this is that the punitive effect of the rule on fraudulent claims is entirely deprived of its value and effect. A further consequence is that

[357] [2011] EWHC 210 (Comm), [2012] Lloyd's Rep IR 164.
[358] [1996] AC 563
[359] *Sharon's Bakery (Europe) Ltd* v *Axa Insurance Plc* [2011] EWHC 210 (Comm), [2012] Lloyd's Rep IR 164.
[360] [1985] 2 Lloyd's Rep 1.
[361] At p 6 col, 1.

there has been a great deal of uncertainty on the law of fraudulent claims, and that the cases establishing the rule on fraudulent claims are very recent. There is no doubt whatsoever that if litigation of cases of insurance fraud had been perceived as potentially rewarding, case law would have been forthcoming —given the prevalence of insurance fraud, it is unlikely that there has ever been a shortage of potential cases to litigate**.**

Most seriously, the unsatisfactory state of the law on the burden and standard of proof will have had a continuing effect on the state of the law generally. Litigants must always be reluctant to proceed with a court case where the standard of proof is against them or, indeed, where there is a risk of the burden of proof shifting onto them. This is precisely the position of insurers who may fear that the case is made out against them on fraudulent grounds, and that they will face either moving goal posts or an uphill struggle on the back of the rules on fraudulent claims and the standard of proof in insurance claims. At the same time, insurers have the strongest possible business incentives for not allowing insureds to 'get away with' insurance fraud, and will always continue to monitor and crack down on fraud to counteract counterproductive practices. As a result, insurers will be particularly keen to pursue cases where there is a suspicion of fraud. However, it appears likely that uncertainty in the law has to some unknown extent caused insurers to opt for defences other than fraud, even where a fraud argument might have been available to them. This situation is likely to have resulted in distortions in the substantive law which, while unquantifiable, are likely to have contributed to the need for comprehensive reform of insurance contract law.

A clarification of the standard of proof in insurance claims, more precisely that it is the balance of probabilities without any reference to a standard of proof commensurate with the occasion would therefore also have been an essential component to the Law Commissions' current insurance law project and an element to be considered for insertion into the Insurance Act 2015. Without it, the reformed law – not so much that of fraudulent claims, as the coherent new system of remedies for failure to disclose and breaches of contractual terms may be subject to continued distortions if insurers continue to avoid pleading fraud in cases where their true defence is one of fraudulent claims. This author would therefore recommend a clarification in some form of the standard of proof for insurance claims, whether by way of case law or statute.

That said, insurers have found other strategies to counteract fraud – some at the investigatory stage or even entirely extrajudicial, some employing other parts of the justice system for the same ends. This will be reviewed in the following. The great virtue of these alternative strategies is that they free up the contract to fulfil its essential function of regulating the relationship between ordinary parties with honest intentions – true good faith relationships.

5 Insurer strategy and approach to fraudulent claims

As demonstrated above, the substantive law on fraudulent claims has come on in leaps and bounds in the current century. However, a claim in litigation is not affected by fraudulent conduct. In *The Star Sea*,[362] the House of Lords drew the line at the commencement of litigation, holding that fraud taking place at the litigation stage did not give rise to the remedy of forfeiture of the claim.[363] As a result, the insurer technically lacks a contractual remedy for fraud post-dating litigation. Nevertheless, while insurance contract law duties may end at the start of litigation, that is only the start of the enforcement of those duties, whether under the insurance contract itself, under the law or in the wider context of society, in the shape of social policy. Simple *horror vacui* on the part of the justice system dictates that there must be a remedy in some form or another for frauds committed under its very gaze. Accordingly, insurers have sought further involvement of the justice system to counteract insurance fraud, beyond the two-dimensional contractual relationship. This chapter explores developmental milestones in the emergence of further, extra-contractual remedies for insurance fraud, in the absence of, or indeed in addition to the fundamental, contractual remedy.

5.1 Introduction – defining the materials

This chapter[364] takes a step back from technical aspects of insurance contract law as well as of reform policy, and observes claims remedies in context. Having reviewed the state of the so-called common law rule on fraudulent claims, and its current state of flux with statute law yet to be applied and awaiting Supreme Court definition of the rule itself; and explored the procedural difficulties with which an insurance claimant or defendant are faced; as well as the technical obstacles to a successful plea of fraud, the next step is inevitably to address the insurers' response to the situation. It is intrinsic to the insurer's business model that moral hazard must be eschewed, and if it has failed to do so before entering into the contract, it must seek to enforce that same principle by other means. One option always available to insurers in the primary litigation is to sit back and put the claimant to proof of the element of its claim, and to allow the judge to draw the inference of fraud without any such pleading – but the wider context provides a powerful impetus for taking positive action, not confined

[362] *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea*) [2001] UKHL 1, [2001] 1 Lloyd's Rep 389.

[363] Instead, the insurer must rely on procedural remedies such as orders for disclosure and rules surrounding perjury.

[364] In writing this chapter, the author was greatly inspired by a lecture given at Southampton on 19 February 2014 by Professor Mark Button, University of Portsmouth, entitled "From 'Shallow' to 'Deep' Policing: 'Crash-for-Cash' Insurance Fraud Investigation in England and Wales and the Need for Greater Regulation". The interested reader is referred to the article *of* Mark Button & Graham Brooks *(2014): From 'shallow' to 'deep' policing: 'crash-for-cash' insurance fraud investigation in England and Wales and the need for greater regulation* in the journal *Policing and Society, DOI: 10.1080/10439463.2014.942847* for an insight into how the insurance industry has tackled the need for investigations without police involvement by setting up organisations and registers and investigating claims privately.

to the four corners of the insurance contract. Financially, large numbers of fraudulent claims are an unacceptable *status quo* to the insurers: it represents a threat to the very insurance business model which relies on low advance premiums and few large pay-outs only to particular unlucky insureds. It is also a socially undesirable phenomenon on which the government has seen fit to take action in the form of the Insurance Fraud Taskforce.[365] Therefore a situation with large numbers of insurance claims must be curbed one way or another[366] – whether by improving the safety culture or conditions, by ceasing to offer cover for such risks or by ensuring that there is no duty to pay. Insurers have therefore been more or less compelled by duties to shareholders as well as premium payers to seek to reduce the size and frequency of fraudulent claims, lest their very existence should come under threat.

Armed as explained in previous chapters with the forfeiture rule, with a clear deterrent approach and punitive in nature, it might have been thought that the law was properly and sufficiently weighted in favour of insurers to make insurers content. That said, there is clear judicial authority from the highest level to the effect that any contractual remedies flowing from insurance fraud cease upon the commencement of litigation.[367] The basis for this cessation was stated to be that procedural tools and duties take over upon the commencement of litigation – most obviously the exposure to accusations of perjury and the disclosure duties upon a party to litigation.

The lack of defined content to the good faith concept itself, as identified not least by Rose[368] and Butcher,[369] creates an imperative to identify and define the precise duties giving rise to a cause of action. That being the case, a blanket negation of the existence of any post-litigation duties has the virtue of clarity but are things really so clear cut? It will be shown in this chapter that insurers appear to have perceived the need for an enforcement tool at the post-litigation stage, and have developed that tool independently from the forfeiture rule. Moral hazard does not appear to enter into the equation. However, how is the balance of powers throughout the insurance contract affected by this additional tool?

Existing case law – some of which unreported – will be reviewed with a view to describing current practice of insurers in taking the next step of punitive action against insurance fraud. This definition of the source materials is methodologically important, because it permits variety while nevertheless operating a clear restriction and delimitation. Many of the claims to be discussed in the following are rooted in a personal injury situation and are therefore originally tort claims, but pursued by an insurer

[365] The Taskforce released its Final Report with recommendations in January 2016.
[366] Incidentally this observation applies equally to claims legitimate, hopeful or fraudulent.
[367] The Star Sea [2001] UKHL 1, [2001] 1 Lloyd's Rep 389.
[368] Francis D. Rose, *Informational Asymmetry and the Myth of Good Faith: Back to Basis* [2007] LMCLQ 181.
[369] Christopher Butcher, *Good faith in insurance law: a redundant concept?* (2008) JBL, 375-384.

who has perceived a whiff of fraud.[370] Other claims are pure insurance claims where the direct insured under an indemnity policy submits forged evidence. Each type of claim is subject to forfeiture in the substantive proceedings albeit under very different frameworks and on different conditions – insurance claims under good faith rules, and tort claims under the CPR following *Summers v Fairclough Homes*.[371] The derivation of the original claim is of reduced importance in this chapter, because the analysis here is based on an investigation into all reported contempt cases with an insurance connection. The lowest common denominator of those cases is not related to the original claim in insurance or tort, although there will always have been an insurance claim of some description at the outset – whether under a liability policy with the fraud aimed at the policyholder and perpetuated against its insurer, or under a property policy with the insurer as contractual defendant. Instead, the denominator is quite simply that an insurer is the contempt applicant/claimant. This lowest common denominator is not unimportant: the insurers have the initiative at this stage and have, in these particular cases, seen fit to add to the fraudulent claims remedy in the first set of proceedings by further action.

The cases are necessarily a motley crew. The defendant will variously be the insured under a contract with the insurer, or some kind of insurance beneficiary, or a witness in proceedings concerning the insurance claim. The single unifying factor, however, is that insurers – whether under a property policy or a third party liability policy; whether faced with fraud by the direct insured, by a claimant third party or by a witness – are the initiators of the action. Having at their disposal the punitive remedy as set out in Chapter 3, which operates solely against the contractual insured, the insurers nevertheless seek further relief, going on the offensive against fraudsters. To what extent does the law add to the deterrent fraudulent insurance contract remedy by providing routes of action against the contractual claimant and other defendants? And to what extent do insurers seek to shape their business climate by penalising fraudulent claimants with the various consequences arising – imprisonment sentences for perpetrators and negative media exposure?[372]

Habitual fraudsters instigating insurance claims rings by deceptive practices are less commonly defendants in these cases, simply because they are after all likely to instead be prosecuted by the authorities for a criminal offence under the Fraud Act 2006, the Proceeds of Crime Act 2002 or some other statute, or indeed for conspiracy to commit a crime of fraud.[373] The source materials the subject

[370] For an example of use in personal injury claims cases: see *Brighton & Hove Bus & Coach Co Ltd* [2011] EWHC 2504 (Admin).
[371] [2012] UKSC 26, [2013] Lloyd's Rep. IR 159.
[372] A full account with not only legal but also sociological and criminological ambitions would have to add to this an exploration of the investigative machinery developed by insurers in response to police authorities downgrading the priority of insurance claims investigation, as well as social perceptions of insurance fraud insofar as measurable; however, such an investigation would necessitate the adoption of sources much beyond the identified circle of insurance-related contempt cases which is the scope of this research.
[373] By way of example of an early prosecution, *R v McKenzie* [2013] EWCA Crim 1544.

of this chapter are the relevant judicial decisions issued in the past ten years or so, since insurers first sought to identify a tool other than the contractual remedy to attempt to curb fraudulent practices, and the decisions will be reviewed with a view to identifying the emerging law as well as significant judicial attitudes in evidence in the decisions. Between them, these cases represent a trend, not least because they have arisen suddenly and multiplied in a brief period of time. The questions to be asked concern the insurers' strategy and purpose with litigation of this type. The conclusions will consist in part of conclusions as to the law, but more importantly of observations on strategy, purpose and social factors. A proactive approach by insurers to insurance claims, beyond the four corners of the contractual relationship, and the availability of such an approach, help shape the global picture of fraudulent claims.

5.2 Options for insurer action – damages, costs and contempt

In the continuation of the fraud complex of ideas though their procedural aspects, the contractual rights are only the beginning. At the time of loss, rights accrue. At this time, the forks in the potential event tree are dominated by considerations related to negotiation positions and therefore to a great extent to bargaining power. Evidence is exchanged in support of the claim. That evidence may be gathered and held on file for later use in litigation – contractual or other. The issuing of the claim form[374] not only crystallises certain insurance rights including the determination of whether a loss has happened, but also marks the shift from a mere claim to litigation. The process of gathering evidence as well as that of litigation are implicated in the genesis of fraudulent claims: a fraudulent claim per se without any supporting evidence in the first place is unlikely to be paid if of any magnitude or importance. Suspicions about the claim itself may crystallise when evidence, false or inconsistent, is supplied in support thereof. Depending on what evidence is available to the insurer, it may opt to simply reject the claim, taking a passive stance that puts the insured to proof of its validity, or may take proactive steps. In what follows, the proactive steps available to and explored by the insurance industry will be narrated and analysed.

The judgments to be discussed in the following are mostly available on open legal resources, whether reported or not – there may well be further cases available if one delves into the archives of county courts, but a limitation in scope to openly available decisions equally permits valid conclusions to be drawn.

As a preliminary point it should be mentioned that in this chapter, there are invariably different sets of proceedings at issue so that one person will first be the claimant or indeed a witness in the insurance contract action, then the defendant or respondent in the contempt proceedings. The insurers will be first the defendant in the civil action, then the applicant in the permission to pursue the contempt

[374] The terminology appointed in the procedural law of England and Wales for 'writ'.

proceedings. To avoid confusion it will be expedient to refer to them not by their procedural role but by their substantive or 'real' role, therefore, as insurance claimant and insurer; or indeed by name.[375]

5.2.1 Damages a remedy for fraud - exemplary damages

Damages have been held not to be an available remedy for fraudulent insurance claims[376] – but recent developments cause us to modify that stance, albeit in a technically different context. The focus is on damages calculated based on the costs incurred by insurers as the result of having to investigate a fraudulent claim, such damages would ordinarily be a matter to be addressed in the original proceedings, not in the contempt proceedings which are by definition a new set of proceedings. The award of such damages has been mooted occasionally; not least in the context of the work of the Law Commissions. By way of example:

> "Furthermore, we propose that in some circumstances the insurer should be entitled to claim damages from a fraudulent insured for the costs of investigating the fraud."[377]

However the Law Commissions stopped short of legislating for such reform. In the context of civil proceedings, a claim for investigation costs was indeed made and awarded in *Parker v National Farmers Union*.[378] The claim was not disputed and Teare J was therefore not compelled to consider the theoretical foundations for awarding such damages, and had no particular incentive to do so in the context of a judgment of 219 paragraphs.

However, following a decision establishing that a fraud has been perpetrated, a somewhat different picture has emerged in fairly recent developments. In two early test cases, French insurance giant, Axa, led the way in attempting to extract special and exemplary damages in proceedings against insurance claimants whose fraud was also, separately, the subject of attention from the criminal justice system: *Axa v Thwaites*[379] and *Axa v Jensen*.[380] The criminal justice system has historically not listed insurance fraud among its priorities, resulting in comprehensive insurer action at the investigative and prosecution stage. For the criminal justice system therefore to be involved, the fraud

[375] Judges also come across this problem. See footnote 1 in the judgment in *A. Barnes v Seabrook* [2010] EWHC 1849 (Admin), which sets out the correct terminology: "There seems to be some confusion about the correct nomenclature for the person making the application (claimant/applicant) and the alleged contemnor (defendant/respondent). I have used claimant and defendant. But see Practice Direction to RSC Ord. 52, paragraph 2.5."

[376] *Banque Financiere de la Cite SA v Westgate Insurance Co. Ltd* [1990] 3 WLR 364 - this case was the more traditional and expansive vision of the post-contractual duty of good faith and has been criticised; eg MacDonald Eggers , P., Remedies for the failure to observe the utmost good faith [2003] LMCLQ 249 .

[377] The Law Commission Consultation Paper No 201 and The Scottish Law Commission Discussion Paper No 152 Insurance contract law: post contract duties and other issues - A Joint Consultation Paper at para 1.21.

[378] [2013] EWHC 2156 (Comm).

[379] *Axa Insurance Co Ltd v Thwaites*, unreported, Norwich County Court 8 February 2008, available on Lawtel.

[380] *Axa Insurance UK Plc v Jensen*, unreported, Recorder Lochrane, County Court at Birmingham, 10 November 2008, available on Lawtel.

had to be quite important. The developments outlined here form only a small element of a broader movement towards policing of insurance fraud by the authorities supported by the insurance sector, rather than by the latter independently. Those developments are an interesting phenomenon but much beyond the scope of this work.[381]

In the first case, *Axa v Thwaites*,[382] the insured had been convicted of deception in the Magistrates' Court and the judge was asked to award special and exemplary damages.[383] It appears that the special damages in question were the costs of investigating the insurance claims. The claimed and awarded amount was GBP1,314. The insured disputed the amount on the ground that some of it referred to overheads – but the judge awarded the full amount including overheads. The amount fraudulently claimed by the insured had been GBP10,584, and that claim being ineffective, insurers sought that amount again as exemplary damages. The claim as described in the judgment was an entirely false one, the car the subject of it being of no or very little value and some items being found in the insured's home. If not wholly fabricated, the exaggerated part appears to have been the lion's share.[384] The judge was required to decide whether exemplary damages could be awarded in this situation; whether there was a risk of double penalty. On the latter issue, the judge decided that there was a need to be mindful and although somewhat reassured by the fact that the Magistrates' Court had given a suspended prison sentence only and no fine, the judge declined to award exemplary damages on the reasoning that it would in effect be to add to the criminal penalty. The judge did award the insurers' costs of investigation as special damages although this was disputed by the insured. In view of the relatively small amount of money at stake, it might be an explanation for the insurers going to the trouble of a separate suit that it was hinted, if not explained or detailed, that the conduct of the insured was systematic or habitual. Furthermore, the case is likely to have been regarded as a test case by insurers, given the very small amounts at stake.

In *Axa v Jensen*, the insured had sold a caravan but not been paid and sought to cover her losses by – at first successfully – claiming for it as stolen.[385] She was arrested but cautioned by the police rather than charged with the fraud. Insurers sought repayment of the indemnity paid for the caravan plus exemplary damages. The judge considered unspecified passages from Clark and Lindsell on Tort[386] and equally unspecified precedent from the House of Lords,[387] as well as *Axa v Thwaites*. The need to

[381] See further eg Mark Button et al. See also the Final Report of the Insurance Fraud Taskforce, Chapter 4, Tackling Insurance Fraud: The Story so far, pp 43-54.
[382] *Axa Insurance Co Ltd v Thwaites*, unreported, Norwich County Court 8 February 2008, available on Lawtel.
[383] The parties will be referred to as insurers and insured, although by the time of the judgment those descriptions were quite inapposite, because there were two litigations with different claimants.
[384] On a side note, counsel for the insurers had been called to the bar in 1992.
[385] The sale was unsuccessful as she was not paid the monies.
[386] At [6]. The author considered guessing at the passages but has refrained.
[387] At [6]. Idem.

avoid double punishment was dismissed by the judge as inapplicable in this case where the defendant had merely been cautioned and not charged. He further cited

> "the obvious nature of this offence, the not insignificant amount of money involved in the fraud, the deliberate nature of that fraud and the general policy idea of providing a deterrent against such activities, both by the offender and by others before the courts, that the imposition of a caution in this case really does not amount to punishment of any significant nature at all."[388]

The judge decided that exemplary damages were an available remedy and went on to comment, idiosyncratically, that "[i]t is obviously important for the proper functioning of the financial services of this country that the relationship of uberimae [sic] fides between insurers and insured is one that is preserved and enforced by the law".[389] This appears as a comment in passing with no elaboration or indication as to what might be intended or how the *uberrima fides* might fit into the bigger picture of moral hazard, and should probably not be given any legal weight. The damages ultimately awarded, GBP4,000, fell short of those pleaded by the insurers and represented a 50 per cent uplift on the sum fraudulently claimed by the defendant. The defendant had left the country with a last recorded address in Belgium and it appears unlikely that insurers ever received the compensation to which they had been held entitled.

Following *Axa v Jensen*, there is a remarkable dearth of reported cases. This may be either an opportunity to recall the archaeological maxim "absence of evidence is not evidence of absence", or an indication that insurers considered this route a dead end in spite of scoring a somewhat Pyrrhic win in *Jensen*. That case was nevertheless cited in the recent case *Churchill Insurance Co v Shajahan* which must be chalked up as a success for insurers.[390] This undefended claim for exemplary damages concerned an inflated third party motor claim following what appeared to be a deliberately engineered accident. The claimant insurer was held by the County Court to be entitled to recover compensatory damages[391] covering the costs of investigation at GBP1,200[392] as well as exemplary damages of GBP7,500 from the two defendants.[393] The cases cited to the judge do not appear to include *Axa v Thwaites*, but do include *Axa v Jensen*[394]. The judge in *Churchill v Shajahan* considered House of

[388] At [7].
[389] At [8].
[390] Unreported - County Court, Birmingham, Recorder Tidbury, 11 September 2015. Available on Lawtel, ref AC0148750.
[391] Covering the sum paid for the defendants' car and solicitors and for the insurers' costs of investigation.
[392] The judge makes reference to figures reported to him from other similar cases, possibly referring to *Axa v Jensen* where GBP1,300 were awarded for this head.
[393] Insurers had sought a sum of GBP20,000 by way of exemplary damages.
[394] Misspelled as Jenson with no citation details given but it may be assumed that it is the same case.

Lords guidance[395] permitting exemplary damages in cases of fraud, deceit or conspiracy to defraud and – notably – satisfied himself that no criminal prosecution had taken place or was contemplated.

A common factor in two of the three cases outlined here[396] is that insurers have already paid out a sum, which they were seeking to recover through the proceedings. These are cases where the indemnity has been paid, and only at a later stage is a fraud discovered (insurers having incurred costs for the investigation of the claim), as opposed to where insurers first carry out a full investigation and uncover the fraud. Where no indemnity has been paid, there is naturally no need for recovery proceedings. However where such proceedings are in any case warranted, insurers are perhaps reasoning that where they are forced to seek judgment to recover the monies anyway, they may just as well request additional damages. It is unlikely to be worthwhile to commence proceedings with a view only to securing exemplary damages, not least since they were calculated in whole or in part, both in *Jensen's* and *Shajahan's* cases, as a percentage of the indemnity paid and adjudged.

While as noted above there is a dearth of reported cases involving exemplary damages, there are also examples of analogous cases where exemplary damages would probably have been appropriate. *Cirencester Friendly Society Ltd v Parkin*[397] was a very short judgment in an undefended case of avoidance *ab initio* for misrepresentation, where action was triggered by a subsequent insurance fraud. The defendant had become a member of the claimant friendly insurance society and in doing so had given erroneous answers to a number of health questions of a wide nature. As a result of misleading the insurer, he became a member and received income protection insurance. He almost immediately claimed under the insurance on the basis that he was unable to work. Claims by Mr Parkin in respect of two separate periods and illnesses were upheld by the Financial Ombudsman Service, which ordered the insurer to pay significant sums in awards dated in 2010 and 2012 respectively. In both cases, the judge asserted, the awards were a direct result of false information provided by Mr Parkin. The judge stated that "I am satisfied that it is appropriate for me to rectify the injustices which have been perpetrated by the misleading of the Ombudsman, resulting in the awards which I have mentioned"[398]. That rectification involved avoidance of the insurance contract (on the basis of initial misrepresentation), setting aside of the FOS awards and an order for repayment of sums paid to Mr Parkin. Given the judge's forceful disapproval of Mr Parkin's methods as well as the fact that proceedings were brought anyway to prevent payment of the FOS awards and to recover monies already paid, the case is in stark contrast to *Banque Financiere de la Cite v Westgate* and provides food for thought on the issue of exemplary damages for fraud.

[395] This time cited as *Rooks v Barnard* [1967] AC 1129 followed by *Kuddus v The Chief Constable of Leicestershire* [2002] 2 AC 122, see *Churchill* at [5].
[396] *Axa v Jensen* and *Churchill Insurance Co v Shajahan*.
[397] [2015] EWHC 1750 (QBD).
[398] At [11].

Although it is well recognised that the forfeiture rule is designed to have a punitive effect,[399] it is worth noting that these cases bear no relation whatsoever to the contractual forfeiture rule. Although there is much discussion of the need not to add by way of a civil case to a criminal sanction, the contractual sanction is not at issue in the proceedings in question which therefore in themselves provide no answer to whether the punitive forfeiture rule can be compounded with special damages or other civil procedure sanctions. However, the combination of a fraudulent claims rule of a punitive nature alongside the availability of the exemplary damages remedy should at least give pause.

In sum, it appears that judges will be willing to award exemplary damages in line with more general guidance for non-insurance cases and that a crucial factor is whether the insurance claimant has been otherwise sanctioned by criminal punishment, and in this regard a caution can be disregarded. It is perhaps for criminologists or criminal law theorists to further comment on what role should be played by the caution here. From the perspective of insurance law, the key must be a set of sanctions and remedies founded on consistency and principle. On the whole, the route seems an unproductive one – the cases have been undefended and insurers would appear unlikely to achieve satisfaction of the judgments with at least one of the defendants above having left the country without a trace. What might be said on the basis of this small number of cases is that the route appears to have been opened on the basis of the wider principle permitting exemplary damages in cases of fraud, deceit or conspiracy to defraud given in *Churchill v Shajahan* and the House of Lords authority cited therein. This can serve as the foundation for further case law enabling the principle to be developed in greater detail.

5.2.2 Costs recovery

Another strategy attempted by insurers is to seek to penalise the fraudulent claimant in the subsequent decision on litigation costs. Indeed this approach is underpinned by the Supreme Court's reasoning in *Summers v Fairclough*[400] where costs are mentioned no less than 36 times throughout the judgment. It is clear that costs are the preferred way to penalise a claimant, or indeed a defendant, who appears to have been wasting the Courts' time. However the specific question here is to what extent costs recovery is an effective means to seek to repress fraudulent insurance claims.

Prominent is the Court of Appeal's decision on costs in *Sulaman v AXA Insurance Plc and another*.[401] In that litigation, insurers had joined the instigators of a large crash-for-cash fraud ring to the claims to recover sums paid by the insurers. The appellant had not been found to be part of the common

[399] A reminder of the beautiful dictum of Lord Hobhouse in *The Star Sea* [2001] UKHL 1, [2001] 1 Lloyd's Rep 389 at [62]: "The logic is simple. The fraudulent insured must not be allowed to think: if the fraud is successful, then I will gain; if it is unsuccessful, I will lose nothing.".
[400] [2012] UKSC 26, [2013] Lloyd's Rep. IR 159.
[401] [2009] EWCA Civ 1331.

fraudulent design, although she had been found to give knowing assistance to her fraudulent brother. The judge at first instance had penalised the appellant in the costs decision because of specific lies told to the court. Upon appeal, the Court of Appeal held that the judge had not strayed from the discretion available in awarding one-third of the claimant's costs.[402] Lord Justice Longmore took some pains to emphasise that overreliance on authorities is inappropriate in these cases because every case is entirely fact-specific. Four observations impose themselves, and will be made in the following.

In a further Court of Appeal judgment, *Gregson v Hussein CIS Insurance*,[403] on costs, the Court of Appeal took a rather different approach, more friendly to the claimant who on that occasion had been largely successful in the insurance claim itself, although the measure of liability was not awarded in full. The Court of Appeal awarded the appellant claimant a significant proportion of his costs. Insurers had at least at the interlocutory stage asserted that the claim was a fraudulent one. The claim was in the nature of a genuine accident, where the claim has been exaggerated amounting, possibly, to a fraud[404] – the decision of which matter was not before the Court of Appeal. Ward LJ made the point that it was insurers who had moved the case from the fast track procedure by alleging fraud – a measure not designed to endear insurers to the Court – and noted that if insurers were concerned about costs, they should make a Part 36 offer.

A few assertions may be made on the basis of these judgments, most of which really bear out a single conclusion that firm principle is unlikely to be developing on this point. First, the fact-specificity of the assessment makes costs recovery an unreliable tool for insurers in terms of establishing consistent practice of penalising fraud. Second, Lord Justice Longmore's encouragement to judges to disregard authorities and rely on the "feel"[405] they have developed for the case has the paradoxical effect of reducing the value of his own Court of Appeal decision, and any decisions from the Court of Appeal or below, as precedent. Third, the mechanism of making Part 36 offers is designed to help protect defendants such as insurers suspecting fraud from paying excess costs and courts will expect this mechanism to be used – quite appropriately at the post-litigation stage. Fourth, costs calculations are no different in insurance cases than in other cases, taking any further observations that may usefully be made on this point beyond the scope of this work.

[402] Lord Justice Sedley dissenting only to say that a reduction by one-third would be sufficient, at [27] etc.
[403] [2010] EWCA Civ 165.
[404] According to the classification of types of insurance fraud discussed *supra*, where it is also noted that a certain amount of exaggeration by way of negotiation is permissible and will not amount to fraud.
[405] At [10].

5.2.3 Contempt of court – a brief history

The word 'history' here bears the perhaps somewhat idiosyncratic meaning of "from 2006 to 2008". The earliest case, even before *Walton v Kirk,*[406] appears to have been *Humphries v Matthews*, a decision from the Liverpool County Court.[407] It concerned obtaining money by deception, with a discussion of the applicable standard of proof that has been cited in subsequent cases.[408] In a second decision on whether to refer the case to the Attorney General for prosecution for contempt, the judge considered the typology distinguished between fraudulent and fraudulently exaggerated cases:

> "the claimant, on my findings, did not invent an accident. The accident in fact occurred. It is not a staged accident and therefore it is not of the same order of seriousness as those cases where there is a completely staged incident for the purposes of claiming compensation. I accept that there is that distinction, but it by no means diminishes the seriousness of this case"[409]

Accordingly the case was referred to the Attorney-General with a view to prosecution for contempt. Following Axa's unsuccessful first attempt to secure punitive damages, the signal case of *Walton v Kirk*[410] made contempt of court the tool of choice of insurers. It was followed by several more contempt cases, gradually laying out insurer strategy in employing the judicial avenue to reduce the attractiveness of fraudulent claims. Prosecution by the Attorney General would be impracticable for a volume of cases, but reference to a High Court judge in civil proceedings proved to be an available route.

The landmark case in the field was *Walton v Kirk*, resulting in two decisions, one on permission to pursue for contempt,[411] and one on contempt.[412] *Walton v Kirk* was based on a claim for a road traffic accident for which the third party to the insurance policy, Ms Kirk, claimed GBP750,000 but recovered nothing as a result of surveillance evidence. This is the first known case of insurers pursuing the injured third party for contempt. The claimant was nominally the insured under the policy but it is fair to say that the driving force behind the proceedings were the insurers. Perhaps the choice of a test case where insurers were subrogated to the rights of the insured against the third party was not entirely by chance. The law on subrogation permitting insurers to use the cloak of the name of the insured avoids any resulting loss of good will or risk of media exposure. Subsequent cases provide examples of insurers appearing in their own name upon assignment of the rights under the policy or

[406] [2009] EWHC 703 (QB)
[407] *Humphreys* or *Humphries*. Unreported, Liverpool County Court, Recorder Andrew G Moran QC, 16 June 2006. The case is unreported but the decision is available on Lawtel.
[408] Although this author would argue that it has now been superseded by the Child Protection Cases.
[409] At [6] .
[410] [2009] EWHC 703 (QB).
[411] *Kirk v Walton* [2008] EWHC 1780 (QB) .
[412] [2009] EWHC 703 (QB).

using the name of the insured based on their subrogated rights. It is striking that most claims brought by the insurers appear to have been successful. There may well be reporting bias, but the only example of an unsuccessful claim appears to be *AXA Insurance UK Plc v Rossiter*[413] where the judge held that the evidence fell short of proving that the fraud was deliberate.

5.3 The mechanics of contempt of court: application in insurance cases

The rules on contempt proceedings are applicable much beyond the scope of insurance proceedings. The purpose of this chapter is therefore not to give a full review of the theory and practice of contempt of court, but to consider its recent use specifically in the insurance claims context. However, a short introduction is apposite.

Contempt of court proceedings may be commenced under the Civil Procedure Rules against any person who "makes, or causes to be made, a false statement in a document verified by a statement of truth without an honest belief in its truth."[414] The use of statements of truth is equally set out in the Civil Procedure Rules.[415] Procedural matters are set out in Part 81, in particular Chapter III, Committal for Interference with the Due Administration of Justice. Permission from a High Court judge must be sought where the contempt took place before a lower court. The contemnor may be sentenced to an imprisonment of up to two years.[416] Unlike for instance in the context of publication of confidential materials, the proceedings need not be brought with the consent of the Attorney-General.[417] The defendant is entitled to legal aid.[418] Although the foundation of the proceedings is in the Civil Procedure Rules and their origin is in civil proceedings (the insurance claims litigation), and the proceedings have been characterised as civil proceedings,[419] the standard of proof is that applicable to criminal matters – beyond reasonable doubt.[420]

5.3.1 Introduction

Contempt proceedings, just like contractual fraudulent claims proceedings, can be brought for wholly invented,[421] exaggerated,[422] or otherwise fraudulent claims. Contempt proceedings result in purely

[413] [2013] EWHC 3805 (QB).
[414] CPR Part 32 section 14.
[415] Part 22.
[416] Contempt of Court Act 1981, section 14.
[417] Contempt of Court Act 1981, section 7.
[418] Contempt of Court Act 1981, section 13.
[419] *KJM Superbikes v Hinton* [2008] EWCA Civ 1280 at [11].
[420] The standard work on contempt of court is Howard Johnson et al, Borrie & Lowe, The Law of Contempt, 4 ed (London: LexisNexis, 2010).
[421] As in *Aziz v Ali & others* [2014] EWHC 4003 (QB).
[422] As in *Kirk v Walton* [2008] EWHC 1780 (QB).

criminal sanctions,[423] including imprisonment, with an immediate or suspended sentence, or a fine. From the insurers' perspective, this route has the great virtue of being available not just in respect of the insurance beneficiary but also against third parties, witnesses of fact and any other associated persons such as implicated medical or legal professionals. It is therefore an effective tool to address not just individual attempts but also to tackle systemic or organised fraud by targeting individual participants who may think that their own small contribution is unimportant or justified. As remarked in the introduction, these proceedings represent a widening of insurers' active strategy, compared to mere passive resistance of insurance claims.

It should be noted at the outset that the law governing contempt proceedings concerning fraudulent insurance claims is no different from the law governing other instances of contempt of court – therefore the following review of applicable rules and case law does not aim to be a general statement of the law on contempt. The aim in the following is rather to assess the approach and outcomes of enlisting the contempt of court tool in the surrounding context of an insurance claim or insurance litigation. It is also worth noting at the outset that the claims for which contempt proceedings may be considered are in fact much the same as those described as various species of fraudulent claim in a previous chapter, so that the ambit of this chapter coincides neatly with previous chapters, the only added factor being the availability of evidence on which to proceed. HH Judge Robinson's words in *Surface Systems Ltd v Wykes*[424] are worth considering:

> "But crash for cash is not the only sort of insurance fraud known to judges who manage and try personal injury cases. Cases of deliberate exaggeration of the extent of injuries are also well known, as are cases where a person sustains an injury whilst, say, engaged in a sporting or leisure activity but claims it was sustained in other circumstances, such as an accident at work."[425]

The correspondence with the established types of fraudulent claim is striking – there are thus wholly invented claims, exaggerated claims and claims where there would be some defence under the policy.[426] It is also noticeable that the quote, which does not purport to be a complete definition of the concept of fraudulent claim for the purpose of contempt of court, leaves out fraudulent means and devices. Their role is currently ambiguous within the context of fraud and will be broached, without attempting a full discussion, in this chapter.[427]

[423] There is debate about whether contempt proceedings are correctly to be considered as civil or criminal proceedings, but that debate is beyond the scope of this work.
[424] [2014] EWHC 422 (QB).
[425] *Surface Systems Ltd v Wykes* [2014] EWHC 422 (QB). *Wykes* itself was an exaggerated claim where a young man who had suffered a real injury presented a claim on the basis that his arm was now functionally useless.
[426] See further supra under 3.1.1.
[427] The ambiguity results from the appeal of *Versloot* (supra) to the Supreme Court.

5.3.2 How to bring proceedings for contempt

A case cited above, *Kearsley v Klarfeld*,[428] had earlier paved the way for the contempt route in 2005 by clarifying what must be pleaded in such a case; the case is discussed in detail below. However as mentioned the signal case was *Kirk v Walton*,[429] judgment in which was given by Mrs Justice Cox DBE on 24 July 2008. In a third party insurance claim, followed by litigation where the insurers supported Ms Walton's defence of the personal injury claim, Ms Kirk sought damages of in excess of GBP750,000 for injuries purportedly sustained in a minor traffic accident involving Ms Walton in September 2001 as well as past and future loss of earnings, care and assistance. Following video surveillance of Ms Kirk, a settlement was reached for a significantly more modest sum and Ms Walton and her insurers sought permission to transfer the case to the High Court in order to request permission for proceedings for contempt of court. In insurance contract fraud terms, the claim fell squarely in the 'exaggeration' category. Ms Kirk went to some lengths to secure medical evidence of the consequences of an accident that had in fact happened. The proceedings at the second stage became known as *Walton v Kirk*.[430]

The basis for an assertion of a fraudulent claim needs to be some statement by the insurance claimant, which can be verified and brought in evidence. Contempt of court proceedings will often have been preceded by litigation concerning liability under the insurance contract, although this is not a necessity: as will be seen a bold statement of the false fact is technically sufficient. The contempt proceedings themselves consist of two phases: the decision permitting prosecution, followed by the conviction itself.

The applicable legal framework is that under Rule 81.18 of the Civil Procedure Rules, a decision for permission to make a committal application in relation to a false statement of truth in connection with proceedings in the County Court may be "made only with the permission of a single Judge of the Queen's Bench Division or the Attorney General."[431] County Courts – where many personal injury or small insurance claims begin their judicial journey – are accordingly not competent to take decisions on contempt of court; such decisions are reserved to the higher courts. It has been decided with more general application not restricted to insurance cases that this entails an escalation of the County Court proceedings to the High Court for this purpose.[432]

Under CPR 32.14(1), headed "False statements", proceedings for contempt of court may be brought against a person if he "makes, or causes to be made, a false statement in a document verified by a

[428] [2005] EWCA Civ 1510 – more on this case above and below.
[429] [REF]
[430] [2009] EWHC 703 (QB)
[431] CPR 81.18.
[432] *Malgar Ltd v R.E. Leach (Engineering) Ltd* Unreported, High Court, Chancery Division, Vice-Chancellor Sir Richard Scott, 1 November 1999; available on Lawtel .

statement of truth without an honest belief in its truth."[433] The statement in question does not technically need to be one of the documents listed in CPR 22.1, although in practice those documents often form part of insurance litigation and will provide a conclusive and elegant method of proof for insurers.

The correct procedure was determined by the judge in *Walton v Kirk*[434] where the judge referred to *Malgar Ltd v R.E. Leach (Engineering) Ltd* and decided that he had jurisdiction to decide the issue of contempt.[435]

An important procedural question was answered in *Ali v Esure Services Ltd*,[436] namely who has jurisdiction to make a committal order for an alleged contempt of court under CPR 32.14 in proceedings that were commenced in the County Court but transferred to the High Court. In personal injury claims concerning a motor accident, proceedings usually begin in the County Court as proceedings between the parties to the motor accident. If insurers wish to defend the claim and pursue the contempt, they will ask to be joined as second defendant to the proceedings.[437] They will also request the proceedings to be transferred to the High Court so that the single judge has competency to decide on committal. That the judge can do so was decided in *Ali v Esure*, overruling *Brighton & Hove Bus & Coach Co Ltd v Brooks*[438] where it had been held that in County Court Proceedings, the Divisional Court was competent to decide the contempt issue. The issue was whether the statement of truth made in the County Court was a continuing contempt until the conclusion of the proceedings in the County Court, or whether it continued to be a contempt when the proceedings had been transferred to the High Court. In early cases, a Notice of Discontinuance on the part of the insurance claimant was frequently served once the solicitors discovered the fraud, to try to prevent contempt proceedings against the claimant. Insurers then resurrected the proceedings and requested a transfer to the High Court. Following *Ali v Esure*, service of a Notice of Discontinuance is an ineffective measure against insurers determined to pursue committal for contempt.

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[433] In *Kirk v Walton* at [24], CPR 32.14 was cited as follows: CPR 32.14 provides as follow:
"(1) Proceedings for contempt of court may be brought against a person if he makes, or causes to be made, a false statement in a document verified by a statement of truth without an honest belief in its truth.
(2) Proceedings under this rule may be brought only –
(a) by the Attorney General; or
(b) with the permission of the court." [Check for amendments.]

[434] [2009] EWHC 703 (QB) at [8].

[435] *Malgar Ltd v R.E. Leach (Engineering) Ltd*, unreported, High Court, Chancery Division, Vice-Chancellor Sir Richard Scott, 1 November 1999; available on Lawtel. There had been an issue based on RSC 52.1(3) which stipulated that the High Court could deal with contempt arising out of contempt in the face of the Court, but that the Divisional Court was competent to deal with other instances of contempt. The parties did not object to the judge dealing with the matter at hand and the judge relied on the decision of the Vice-Chancellor in *Malgar v Re Leach* for jurisdiction.

[436] [2011] EWCA Civ 1582 – decided under RSC Order 52 (Committal) but the procedure remains unchanged.

[437] For instance in *Ali v Esure*.

[438] [2011] EWHC 806 (Admin).

It will be seen that between the need to transfer to the High Court and the two-stage procedure to be applied once there, the proceedings are not entirely straightforward – although the legal issues are not complex and the evidence is often of a straightforward nature, more on which below. It is also the case that a transfer of the civil claim to the High Court permits the same judge to hear the civil claim and to decide the commitment issue. The evidence will usually be the same (although the standard of proof is not), creating savings for the judicial system. These points are relevant when considering insurer strategy against fraudulent claims, where the cost of pursuing each measure is one of the factors to be considered.[439]

The maximum sentence for contempt of court is two years' imprisonment by virtue of the Contempt of Court Act 1981, s 14(1).[440]

From the revision of the applicable rules through the Civil Procedure Rules and from these early cases, the framework of the law sprang fully formed with subsequent cases adding mere illustrations. However the tests to be applied required some fine tuning.

5.3.3 The tests

There are two stages to the process with to some extent overlapping tests. They must be set out and considered separately: first, we consider the decision to grant permission for contempt proceedings, and we then go on to address the decision itself to commit for contempt of court.

5.3.3.1 The decision to grant permission for contempt proceedings

The test was set out by Mrs Justice Cox in *Kirk v Walton* [2008] EWHC 1780:[441]

> "I approach the present case, therefore, on the basis that the discretion to grant permission should be **exercised with great caution**, that there must be a **strong prima facie case** shown against the Claimant, that I should be careful **not to stray at this stage into the merits of the case**, that I should consider **whether the public interest requires the committal proceedings** to be brought, and that such proceedings must be **proportionate** and **in accordance with the overriding objective**." (emphasis added)

It is worth noting that at this stage, factors personal to the alleged contemnor are not taken into account.[442] The test emphasises the public interest in addressing the conduct involved, not the

[439] Further on this *infra*.
[440] There is debate as to whether an action arising out of civil proceedings such as those considering an insurance claim are different in nature from criminal contempt proceedings. That debate is beyond the scope of this work.
[441] [2008] EWHC 1780 (QB) at [29].
[442] It is appropriate on procedural principle that such factors should be taken into account only at the sentencing stage.

appropriateness of a longer or shorter prison sentence or indeed mitigating factors that may be at hand. Subsequent tests are variants or elaborations of this test, not least the very comprehensive and deliberated expose in *Barnes v Seabrook*,[443] where the court quoted at length from *KJM Superbikes*[444] and drew the following conclusions (at [41]). It serves as an excellent summary, which cannot be improved upon as a starting point for discussing contempt of court.

> "i) A person who makes a statement verified with a statement of truth or a false disclosure statement is only guilty of contempt if the statement is false and the person knew it to be so when he made it.
>
> ii) It must be in the public interest for proceedings to be brought. In deciding whether it is the public interest, the following factors are relevant:
>
> a) The case against the alleged contemnor must be a strong case (there is an obvious need to guard carefully against the risk of allowing vindictive litigants to use such proceedings to harass persons against whom they have a grievance);
>
> b) The false statements must have been significant in the proceedings;
>
> c) The court should ask itself whether the alleged contemnor understood the likely effect of the statement and the use to which it would be put in the proceedings;
>
> d) "[T]he pursuit of contempt proceedings in ordinary cases may have a significant effect by drawing the attention of the legal profession, and through it that of potential witnesses, to the dangers of making false statements. If the courts are seen to treat serious examples of false evidence as of little importance, they run the risk of encouraging witnesses to regard the statement of truth as a mere formality."
>
> iii) The court must give reasons but be careful to avoid prejudicing the outcome of the substantive proceedings;
>
> iv) Only limited weight should be attached to the likely penalty;
>
> v) A failure to warn the alleged contemnor at the earliest opportunity of the fact that he may have committed a contempt is a matter that the court may take into account."[445]

This list was subsequently quoted in *Quinn v Altinas*[446] where the judge saw fit to add that the standard of proof to be applied was the criminal standard.[447]

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[443] [2010] EWHC 1849 (Admin).
[444] *KJM Superbikes Ltd v Hinton* [2008] EWCA Civ 1280.
[445] *Barnes v Seabrook* at [41]; paragraph d) being a direct quote from *KJM Superbikes* at [23].

There is also a matter of proportionality. In *Quinn v Altinas*, it was put to the judge that permitting contempt proceedings would be disproportionate in the case. The judge held that the modest size of the original claim was not the governing factor. The questions to consider were: "is there a strong prima facie case? Does the public interest require that the allegation should be investigated by the Court? Is it proportionate to grant permission?"[448] – essentially a very succinct version of the longer tests set out above.

The judge went on to hold that while the falsity was not "of the gravest kind", especially given that insurers had not pleaded that the whole claim was fraudulent,[449] it was serious enough to require examination in the public interest, and "public interest and proportionality [go] hand in hand".[450]

In *Quinn Insurance Ltd v Trifonovs*,[451] besides the usual observations that false claims are costly to insurers, it was also noted, in the assessment as to whether it was proportionate to permit contempt proceedings, that false motor accident claims are "a major drain on the resources of the legal system". It was therefore very strongly in the public interest that those who committed such frauds should not merely lose their cases, but should also be punished like criminals.[452] The judge described the public interest thus:

> "in the hope first of all that justice will thereby be done and secondly that the message will get out to the people who commit these frauds (often for quite a small amount of money) that they are committing a serious crime and that they will be at real risk of a serious punishment if they are proven to have done so."[453]

He said about Mr Trifonovs:

> "He is precisely the sort of person and this is precisely the sort of case where the civil court needs the backing of the law of contempt in order to protect its processes and protect the public interest."[454]

In the case of *Quinn v Trifonovs*, the judge succeeded in creating the example as there were several newspaper reports of the decision, even though it was not a final decision.[455] There does not appear to

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[446] *Quinn Insurance Ltd v Altinas and another*, unreported, High Court of Justice, Queens Bench Division, Mr Justice Spencer, 26 March 2014 at [24].
[447] At [25].
[448] At [43]. One notes with curiosity the choice of the word 'investigated' over eg the word 'considered'.
[449] Which following *Kearsley v Klarfeld* is no longer necessary.
[450] *Quinn v Altinas* at [41].
[451] Unreported, HH Judge Moloney QC, High Court of Justice, 9 October 2013, at [21].
[452] If proven.
[453] At [21].
[454] At [22].

have been a final decision in the case.[456] The insurers sought permission to make a committal application in relation to a false statement of truth. The claim was based on injuries said to have been suffered as a result of a car door opening while his car passed. The injuries said to have been suffered, which were said to have resolved only three months after the event, were difficult to reconcile with the established fact that the injured person had taken part in a cage fight thirteen days later. The judge in *Quinn v Trifonovs* set out the test as follows.

> "it is accepted on both sides of the Bar that the recent introduction of this rule does not affect the existing practice in that regard as laid down relatively recently by the Divisional Court in the case of *Barnes and Others v Seabrook* 2010 [EWHC] 1849 (Admin) [sic]. From Paragraph 38 onwards of the Judgment of Lord Justice Hooper in that case, he reviews the principles to be applied by a Court when dealing with such a permission application; and he refers at paragraph 39 to a decision from Mrs Justice Cox in *Kirk v Walton* [2008] EWHC 1780 QB where she said that the test should be that a strong prima facie case must be shown, but the judge should be careful not to st[r]ay into the merits of the case. She said one should consider whether the public interest requires committal proceedings to be brought, and that such proceeding[s] must be proportionate and in accordance with the overriding objective."[457]

The 'overriding objective' returns here and it might be commented that reference to the overriding objective was in *Quinn v Altinas*[458] understood to be a reference to the overriding objective of dealing with cases fairly and justly.

The judge in *Quinn v Trifonovs* went on to say the following.

> "In the case of *KJM Superbikes v. Hinton* [2008] EWCA Civ 1280, the Divisional Court gave guidance saying the wider public interest would not be served by the Court exercising the discretion too freely in favour of allowing proceedings of this kind to be perceived by private persons. There is an obvious need to guard against the risk of allowing vindictive litigants to harass persons. The Court should exercise great caution before giving permission to bring proceedings; it should not do so unless there is a strong case both that the statement was

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[455] Exemplified by this one (warts and all): http://www.dailymail.co.uk/news/article-2451773/Injured-policeman-caught-cage-fighting-days-crash.html (accessed 30 June 2015).

[456] As of 30 June 2015; although a hearing was commenced and adjourned according to this report http://m.insurancetimes.co.uk/quinn-insurance-seeks-jail-for-cagefighting-crash-fraudster/1407594.article (accessed 30 June 2015).

[457] *Quinn Insurance Ltd v Trifonovs*, unreported, HH Judge Moloney QC, High Court of Justice, 9 October 2013 at [4].

[458] At [23].

> untrue and that the maker knew that it was untrue at the time he made it. All other relevant facts will have to be taken into account."[459]

In *Barnes v Seabrook*, the judge agreed with the statement of Moore-Bick LJ in *KJM Superbikes* wherein he said notably that "the wider public interest would not be served if courts were to exercise the discretion too freely in favour of allowing proceedings of this kind to be pursued by private persons."[460]

In *Royal & Sun Alliance v Fahad* , the judge cites a strong prima facie case.[461] The judge also states "I bear in mind that if permission is granted the contempt would have to be proved to the criminal standard."[462] This is a single sentence paragraph and is not clear what the judge intends to convey with it. The standard of proof at the later stage should, as a matter of principle, not influence the decision at the first stage.

The exhortation not to stray into the merits of the case while requiring a finding of a strong *prima facie* case against the claimant is mostly managed by judges by stating that the summary of the evidence does not constitute findings, or words to that effect, such as those of Mr Justice Spencer in *Quinn v Altinas*: "I emphasise that I make no finding whatsoever but simply narrate the evidence in summary form".[463]

The decision at this stage is essentially administrative and there is not much to comment on a level of principle.

5.3.3.2 The test in contempt proceedings

As foreshadowed above, the second stage involves essentially a conviction for a criminal offence, and the assessment to be made are to be approached on that basis, notably with the standard of proof being 'beyond reasonable doubt'. The questions to be answered within contempt proceedings have been phrased in slightly different ways in different cases. The first attempt was in *Walton v Kirk*[464] where the judge (quite correctly, and necessarily as this was the first case of its kind) relied on non-insurance cases to set the test out as follows.

> "a) The falsity of the statement in question; b) That the statement has, or if persisted in would be likely to have, interfered with the course of justice in some material respects; and c) That

[459] At [5].
[460] At [40].
[461] [2014] EWHC 4480 (QB) at [23].
[462] At [17].
[463] At [3].
[464] [2009] EWHC 703 (QB).

> at the time it was made, the maker of the statement had no honest belief in the truth of the statement and knew of its likelihood to interfere with the course of justice."[465]

The test was later set out as follows, in *Royal & Sun v Fahad*.[466] This revised version encompasses both the facts to be proven and the standard that the proof must meet.

> "It is for the applicant to prove (if they can) to the criminal standard, that is, so that the court is sure, that the respondent made the false statements alleged and verified, or caused them to be verified, with a statement of truth; that at the time when the respondent made the statements he knew they were false; that the respondent acted with the intention of interfering with the due administration of justice and, that if the false statements had been persisted in, it is likely that it would have interfered with the course of justice. (See *AXA Insurance UK Plc v Rossiter* [2013] EWHC 3805 QB at para. 9)"[467]

The tests for whether permission should be granted for the matter to be assessed by a judge and that for a decision on contempt are quite different; as they must be – one is an administrative assessment of whether the court's time should be taken up with the matter or is best spent on something else, and the other is the basis for a criminal conviction. Although there is no inherent contradiction present, in the interests of justice not just being done but also being seen to be done, it would probably be ideal if after such a balancing act the resulting proceedings were to be managed by a different judge. However this is not the usual way to proceed – in *Royal & Sun v Fahad*, the same judge heard both rounds of the case;[468] an approach which by then had been endorsed by the Supreme Court in *Summers v Fairclough*.[469]

It is not possible to say whether for the purposes of this stage the courts have taken a dimmer view of the driving force behind the fraudulent claim, than of the more incidental friends and acquaintances who support their claims. This was the case in *Quinn v Altinas*; at the later stage, the difference becomes apparent: in the sentencing decision in *Esure v Shah*,[470] the judge mentioned specifically that Mr Shah was not "an organiser" but "in the front line".[471]

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[465] At [8].
[466] [2015] EWHC 1092 (QB).
[467] At [6].
[468] See para [37].
[469] *Summers v Fairclough* at [59].
[470] *Esure Insurance Services Ltd v Shah*, unreported, HH Shaun Spencer QC, High Court Division, Queen's Bench Division, Huddersfield Registry, 14 March 2011.
[471] It is pointless to attempt a thorough assessment of whether this is true without a complete insight into practice and interviews with judges and other stakeholders, so it must remain a research question for another day.

It is also noteworthy that as early as in *Kirk v Walton*, it became clear that contempt proceedings could be brought also after the civil litigation had settled. It was not necessary for the claim to have been dismissed as fraudulent. This is logical for a few reasons. The findings of fact from the first set of proceedings are not binding on the subsequent judge. If insurers are able to establish early on in the first proceedings that the claims are false, and that judgment in their favour is likely, they may nevertheless find that the claimant is unwilling to relinquish the claim (effectively admitting to fraud). If so, the costs equation will point the insurers towards seeking a settlement of the claim and limiting costs, rather than defending the claim to arrive at a dismissing judgment. A favourable settlement may perhaps be reached on terms involving an (implicit) undertaking not to pursue contempt proceedings. It was noted in *Kirk v Walton*, with respect quite rightly, that while the insurance contract action remains current, insurers will risk criticism if they do bring an additional action for contempt, so that the first action must be brought to a close before any contempt proceedings can be considered.[472]

Counsel for Ms Kirk pointed out that she "should have had the opportunity to have her response tested in the substantive proceedings". In response, it might be argued that the claimant is quite free not to settle. The judge instead referred to costs considerations and said:

> "If it were otherwise litigants would have to keep open the substantive litigation, thereby occupying court time and resources, and incur further costs of both preparatory work and of trial, which would be wholly disproportionate and, as it seems to me, contrary to the interests of justice."[473]

It is also the case that once a fraud is uncovered in the primary proceedings, solicitors are unlikely to wish to continue to represent the claimant, and it was in the past common for solicitors to advise that a notice of discontinuance be brought to avoid proceedings for contempt of court.[474]

5.3.4 A 'social evil': the public interest

The perspective of insurers for the public interest test was set out at length in *A. Barnes t/a Pool Motors v Seabrook*,[475] where four-fold grounds were given by counsel representing the insurers' side:

> "**To act as a deterrent**. Insurance fraud is endemic. The reason for that is that many perpetrators perceive it to be a victimless crime for which the penalties of being caught are negligible. The advent of accident management companies and no win no fee lawyers mean that all the fraudsters need to invest in their fraud is a day of their time at trial (if the case goes that far). Hitherto, if their fraud is exposed, they merely walk away from the litigation

[472] *Kirk v Walton* at 37.
[473] *Kirk v Walton* at 36.
[474] See further 5.3.2 above.
[475] *Barnes v Seabrook* [2010] EWHC 1849 (Admin).

unscathed, any adverse costs being met by their ATE LEI. The fact that this fraud was perpetrated by an educated London cabbie indicates the contempt for which the civil justice system is currently held by fraudsters. The perceived unwillingness of the civil courts to punish litigants who abuse their process deceitfully is itself a factor that perpetuates the rise of fraudulent claims.

To raise awareness of the QBD judiciary of the sorts of demands being placed on the Circuit judiciary. I submit that the Lists in Ilford and Central London County Court are clogged up with fraudulent motor claims. Unless and until some of the fraudsters lose more than a day of their time at court, and until that fact begins to filter down to grass roots level where such claims germinate, then the status quo is unlikely to change.

To raise public awareness. This fraudulent claim involved a deliberate attempt to manipulate the civil justice system by lying to all the lawyers and the court. It is important that the public understand that they are paying for the illicit proceeds of such frauds through higher insurance premiums. Compulsory motor insurance is a form of taxation in which insurance companies provide the safety net for society to function in an environment of controlled risks. Raising public awareness that Courts are prepared to protect the public at large from such fraud provides a valuable public service.

Improve the administration of justice. The additional costs of permitting this matter to proceed to High Court Committal proceedings should result in a significant reduction of such claims in the future resulting in a significant global saving in costs and freeing up the Judges' civil lists, enabling meritorious cases not tainted by fraud to get to trial faster."[476]

It must be commented that the courts appear to have 'bought into' much of this reasoning in the context of insurance claims. There appear to be no reported decisions where permission for contempt proceedings was refused. The sentences imposed are usually severe, and there are always comments to the effect that insurance premiums are pushed upwards for honest people, or that the integrity of the justice system requires a significant sentence.

The leading case on public interest is *KJM Superbikes Ltd v Hinton*.[477] This was a non-insurance case but is nevertheless relevant authority. Moore-Bick LJ, giving the leading judgment said that

> "the court should exercise great caution before giving permission to bring proceedings. In my view it should not do so unless there is a strong case both that the statement in question was untrue and that the maker knew that it was untrue at the time he made it."[478]

[476] *A. Barnes t/a Pool Motors v Seabrook* [2010] EWHC 1849 (Admin) at [5].
[477] [2008] EWCA Civ 1280.

The Court of Appeal subsequently reversed the judge's decision, although it was one based on discretion, to permit proceedings to be brought. Mr Hinton's statements had been 'completely untrue'.[479] That was the principal factor to consider, and it did not matter that he was unlikely to serve any sentence, being based outside the UK. While the likely penalty as well as any remorse or contrition shown might influence the decision to permit proceedings some extent, the appropriate time to take such things into account was at the later stage of sentencing. The severity of the conduct and its effect upon the public interest of the integrity of the judicial system was the appropriate factor to take into account.

The deterrent effect should not be neglected, although in *KJM Superbikes v Hinton*, Moore Bick LJ pointed out that it might be limited:

> "It is true that only prominent examples of the kind that are widely reported in the press can be expected to make an impression on the public at large, but that is to ignore the fact that the pursuit of contempt proceedings in ordinary cases may have a significant effect by drawing the attention of the legal profession, and through it that of potential witnesses, to the dangers of making false statements."[480]

In *Royal & Sun Alliance v Fahad,*[481] the judge granted an application to proceed with contempt proceedings, noting in relation to the public interest that:

> "[Counsel] rightly accepts that it must be in the public interest for an allegation of this seriousness to be heard and punished (if proved) as a deterrent to false claims. He submits, however, that committal proceedings in this case will not be proportionate and would not serve the wider public interest. I have reached the firm conclusion that the public interest not only justifies but demands that permission be granted to bring this application for committal."[482]

The courts are plainly aware of and taking into account the compounded serious effect of insurance fraud on society. Most judgments contain either a moralistic statement regarding false claims, or a few facts and figures regarding the prevalence of fraudulent claims. The judge in *Quinn v Altinas* said:[483]

> "In my judgment although this allegation of contempt is by no means as serious as many which come before the courts, there is nevertheless a very real public interest in the allegation of contempt being investigated fully by the Court, and if proved dealt with."

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[478] At [17].
[479] At [3].
[480] At [23].
[481] [2014] EWHC 4480 (QB).
[482] Ibid at [24].
[483] At [33].

By 2014 if not before, it was thus in the public interest to let the insurer proceed. In *Quinn v Altinas*, at [37], the judge said:

> "37. The importance of discouraging fraudulent claims, and making an example of those who indulge in false and lying claims, was emphasised by Lord Justice Moses in *South Wales Fire and Rescue Service v Smith*.[484] At paragraphs 2 to 4 of the Court's judgment, Lord Justice Moses said this:
>
> "For many years the courts have sought to underline how serious false and lying claims are to the administration of justice. False claims undermine a system whereby those who are injured as a result of the fault of their employer or a Defendant, can receive just compensation.
>
> They undermine that system in a number of serious ways. They impose upon those liable for such claims the burden of analysis, the burden of searching out those claims which are justified and those claims which are unjustified. They impose a burden upon honest claimants and honest claims, when in response to those claims understandably, those who are liable are required to discern those which are deserving and those which are not.
>
> Quite apart from that effect on those involved in such litigation is the effect upon the court. Our system of adversarial justice depends upon openness, upon transparency, and above all upon honesty. The system is seriously damaged by lying claims. It is in those circumstances that the courts have on numerous occasions sought to emphasise how serious it is for someone to make a false claim, either in relation to liability, or in relation to claims for compensation, as a result of liability."

The judge commented that the above sentiments apply equally to an invented claim and to a genuine one supported by untruths.[485]

In *Quinn v Altinas*, the falsity of the statement was in that the named witness was not independent but an old acquaintance of the insurance claimant. It was not argued that any substantive falseness had been introduced by way of any misleading statements. This points towards the additional interest being protected by judges in contempt proceedings – not just the insurance industry and its premiums, but also the integrity of the judicial process itself. Small wonder then that insurers have found this an accessible route by which to penalise claimants – the courts are more than happy to be enlisted for this particular purpose.

In *Quinn v Altinas*, the judge concluded in respect of the second allegation: [486]

[484] [2011] EWHC 1749 (Admin).
[485] At [38].

> "If the Court were to conclude that this second statement contained a deliberate falsehood, then it was a falsehood in a witness statement made in response to a very specific order of the Court, following the exposure of a falsehood in an earlier witness statement. That it seems to me is capable of adding significantly to the intrinsic seriousness of the second alleged contempt."

The centre of gravity in these comments is clearly procedural, and aiming at protecting the integrity of proceedings.

The public interest was eloquently and emphatically set out in *Aziz v Ali & others*,[487] concerning a well organised insurance fraud where the defendants in the contempt proceedings were nevertheless not the main organisers. It is worth setting out the judge's thoughts in full, as they are illustrative of judicial attitude:[488]

> "15. First, the system of justice in this country requires and depends upon people who bring claims and make statements in court proceedings acting truthfully and honestly. The dishonest making of false statements undermines that system of justice. It undermines public confidence in the justice system. It strikes at the heart of the fair administration of justice.
>
> 16. Secondly, this type of fraudulent claim imposes great costs and great burdens upon the insurance companies dealing with claims. If fraudulent claims are not detected, money is paid out to persons who are not entitled to that money. The insurance companies have also had to devote considerable resources to identifying claims which are fraudulent and in resisting those claims. The costs arising out of dishonest claims are large. Those costs are, ultimately, passed on to and paid by honest drivers in increased insurance premiums. Further, those who make honest genuine claims will, also, inevitably have their claims scrutinised to ensure that they are genuine and to distinguish their claims from the fraudulent claims.
>
> 17. Thirdly, dealing with fraudulent claims involves the use of considerable public and court resources. These claims involved a five day trial. The application for permission to apply for a committal order took a further day. The committal application itself took two further days. That has meant using up considerable court resources, paid for by the tax payer and the public purse."

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[486] At [51].
[487] [2014] EWHC 4003 (QB).
[488] At [15]-[17].

Illustrative of judicial attitudes more broadly is this quote from a judge commenting on a statement by the insurance claimant regarding the inconvenience and annoyance resulting from the surveillance of the insurers.[489]

> "It is understandable that genuine claimants might feel justifiably aggrieved that insurers should employ persons to conduct video surveillance of them going about their everyday lives, but it is because of people like Mr Wykes that insurers feel they have little option but to seek to identify the fraudsters."[490]

There is judicial perception that an escalation is necessary and in progress in regards to sentencing. In *Denkiewicz v Harrowell*,[491] a judgment dating from August 2013, the judge said "I am inclined to think, that, given the scale of this type of fraud, the sentences would be unlikely to be suspended today."[492]

In *Denkiewicz v Harrowell*, a run of the mill crash-for-cash motor case,[493] the insurers had in fact pleaded fraud but the judge commented that "it is not necessary to deal with the detailed pleadings but to look at the facts"[494] – a somewhat surprising but on the whole helpful approach to adjudication. Insurers were not listed as a party to the proceedings which appear to have been in the nature of third party claims by the (as was ultimately held) unsuccessful insurance claimant against the other party to the crash – that being the case insurers were subrogated to their insured's rights under the policy but litigation was in the insured's name.

In *Denkiewicz v Harrowell*, the conclusion that the alleged accident was planned in advance was reached on the balance of probabilities, the judge commenting that "It even seems to me that it might just reach the more serious criminal standard of proof."[495]

5.3.5 Methods of proof

It was noted above in discussing the definition of fraud that a distinct advantage for the insurers in pleading fraudulent means and devices is that the method of proof is exceedingly simple: the issue may well be entirely transparent from just two separate documents 'proving' incompatible truths. It is much the same with contempt, although the situation will be even clearer as the suspect statements

[489] *Surface Systems Ltd v Wykes* [2014] EWHC 422 (QB) at [p 6].
[490] The issue of to what point insurers may be entitled to inconvenience a surveillance object has not arisen in insurance contempt cases but it is not difficult to see how harassment could potentially be discussed as a mitigating circumstance.
[491] Unreported, HH Judge Mitchell, Central London County Court, 21 August 2013; permission to appeal declined *Denkiewicz v Harrowell* [2015] EWCA Civ 385.
[492] At [8].
[493] Heard, in fact, with seven almost identical cases.
[494] At [13].
[495] At [27].

will usually have appended to them a sworn statement of truth. Indeed, if an insurer suspects the claimant of some untruth as to a particular fact, it has every legitimate opportunity and right to secure a statement of truth in respect of that particular 'fact'.

The existence of the prior proceedings does have its limitations: It follows from first principles that if the contempt proceedings have been preceded by full insurance claims proceedings, the facts as established in that litigation will not be binding on the court in the second round. That point was put – for this author's taste, rather too diffidently - by the judge in *Royal & Sun Alliance Insurance Company v Fahad,*[496] when he said:

> "I have been asked by the applicant's counsel to read the judgment of Deputy District Judge Hay as to which course no objection has been taken by the respondent's counsel. I have done so, but consider that save insofar as that judgment helps me beyond reading the transcript of the evidence at the trial as to the nature of the evidence given by the witnesses at the trial, I should not rely upon the views of the deputy district judge upon the facts of this case. **That is not because of any disrespect for those views but because the issues to be determined by me, being essentially the same as those determined by the deputy district judge, I consider I should form my own views independently of the views of the deputy district judge.**" (Emphasis added)[497]

Conveniently in the context of contempt proceedings, the Civil Procedure Rules require certain documents to be verified by a statement of truth: this follows from CPR 22.1 which it is worth setting out in full here.

> "(1) The following documents must be verified by a statement of truth –
>
> (a) a statement of case;
>
> (b) a response complying with an order under rule 18.1 to provide further information;
>
> (c) a witness statement;
>
> (d) an acknowledgement of service in a claim begun by way of the Part 8 procedure;
>
> (e) a certificate stating the reasons for bringing a possession claim or a landlord and tenant claim in the High Court in accordance with rules 55.3(2) and 56.2(2);
>
> (f) a certificate of service; and

[496] [2015] EWHC 1092 (QB).
[497] At [14].

(g) any other document where a rule or practice direction requires."[498]

Any of the documents listed here can become an invaluable tool in asserting that contempt has taken place, if only the statement can be proven to be untrue. Moreover, any other document fulfilling the conditions in CPR 32.14(1) can be used in place of the documents in CPR 22.1.

In *Quinn Insurance Ltd v Altinas and another*[499], an application for permission to bring proceedings for contempt of court against the defendant, the untruth appeared in a signed witness statement with a statement of truth appended.[500] That untruth consisted of a statement that a witness she had named was independent when in fact they had known each other for some 15 years. In a further witness statement on 2 September 2013 she omitted to mention some previous accidents, mentioning only one previous accident. Further road accidents were registered in the insurers' database. A Section 9 witness statement was made at the police station soon after the accident in question. A section 9 witness statement is made under section 9 of the Criminal Justice Act 1967 and is admissible in evidence provided minor formalities are followed. Although by the time of contempt proceedings, the statement will be used to prove the opposite of what was intended with it (namely that the events which actually did take place have now been established and the statement provides a disparate account), it is still good evidence. Such evidence is ideal for the insurer and the court in much the same way as the fraudulent means and devices tool provides a means of cutting down the evidence part of the hearing to little or nothing.

In *Kirk v Walton*, the signal case, Ms Kirk's statement "was in fact a "home-made" statement, written originally by the Claimant on 20 July 2005, but which was then re-dated and confirmed as true, following a court order of 14 March 2006 that she serve a witness statement with a CPR-compliant statement of truth."[501]

Thus if insurers suspect that untruths are being told, they will be in a position at an early stage, perhaps already in preparation for the original insurance contract proceedings, to secure the assistance of the court to procure the evidence needed for future contempt proceedings.

Other examples of the physical form of the untruths may be drawn from case law. In *Esure v Shah*, the falsehood was appended in a statement of truth signed by the claimant and appended to the particulars of claim regarding a road traffic collision. In *Royal & Sun v Fahad*, the three impugned statements were an allegation in the particulars of claim in the insurance contract action that the accident had been caused by the negligence of the insured; a response to a Part 18 request of the

[498] Civil Procedure Rules Rule 22.1, from https://www.justice.gov.uk/courts/procedure-rules/civil/rules/part22 accessed on 2 July 2015.
[499] Unreported, High Court of Justice, Queens Bench Division, Spencer J, 26 March 2014.
[500] *Quinn v Altinas* at [7]
[501] REF

insurer to the insurance claimant in which he stated that he did not know the person who caused the accident beforehand; and an allegation set out at paragraph 6 of the respondent's witness statement dated 20 January 2012 that he did not know F at the time of the accident.[502]

These statements were not only readily verifiable and ascertainable but were on record with the Court. Accordingly, any difficulties of proof will pertain to the factual circumstances surrounding the insurance claim or designed to cast doubt on the honesty of other factual circumstances. Such evidence would include the past Facebook connections of the various *dramatis personae*.[503] In *Kirk v Walton* itself, the evidence that Ms Kirk's statements were false relied on extensive DVD footage of Ms Kirk. Mrs Justice Cox said in the decision granting permission to proceed with contempt of court:

> "The DVDs are of sufficient length and are sufficiently contemporaneous, representative, and consistent to merit a full investigation of the matter."[504]

That evidence may already once have been the subject of proceedings, wherein a judge has concluded that the balance of probabilities for the claim is not met. While not binding on a subsequent court, insurers will have had excellent opportunity to assess the potential for success of the subsequent case.

Regarding surveillance evidence, the judge in *Walton v Kirk*[505] proceeded with caution, giving the following warning. "discrepancies between a statement verified by a statement of truth, on the one hand, and video evidence on the other, will not automatically give rise to a contempt of court. Some exaggeration may be natural, even understandable, for the reason set out by Bell J in *Rogers*."[506] The judge's words echo the notion that an initial insurance claim can legitimately be exaggerated for the purpose of negotiation, as discussed above, [507] although there is no direct connection other than a realistic approach to claims. The judge's statement rather refers to the state of the evidence provided and the need to apply a human interpretation thereto.

To the above, we must, perhaps surprisingly, add circumstantial evidence. In *Liverpool Victoria Insurance Co Ltd v Thumber*,[508] the judge considered the matter before him "the plainest possible case of a fraudulent claim"[509] where the case consisted mainly of a very close series of dates on which the policy had incepted for the insurance claimant, he had become the owner of the car and the

[502] *Royal & Sun v Fahad* at [11].
[503] *Royal & Sun v Fahad* [2014] EWHC 4480 (QB) at [11*]*; *Quinn v Altinas*.
[504] *Kirk v Walton* at [33].
[505] [2009] EWHC 703 (QB).
[506] *Walton v Kirk* [2009] EWHC 703 (QB) at [13]. The reference to *Rogers* appears in expanded form earlier in the judgment as "*Rogers v Little Haven Day Nursery Limited* (30th July 1999, unreported)".
[507] At 3.1.1 above.
[508] [2014] EWHC 3051 (QB).
[509] At [14].

accident had taken place, to which must be added the very inflated nature[510] of the claim which exceeded the pre-accident value of the car by 20 times, a link through a third person between the insurance claimant and the person alleged to have driven the insured vehicle, an improbable account of the accident and a series of prior claims. The judge noted: "Mr Thumber then discontinued his claim and was ordered to pay costs on an indemnity basis to the insurers. A clearer implicit admission that the claim was bogus would be hard to find."[511]

5.3.6 Standard of proof

The standard of proof is quite naturally different at the stage of deciding to give permission to bring contempt proceedings, compared to at the later stage of actually deciding whether there has been contempt. The two stages will be dealt with in chronological order in the following. Both standards of proof are different from the balance of probabilities in civil cases.

When considering whether to give permission to bring contempt proceedings, the standard of proof is that the insurer must provide a 'strong case', illustrated here by a quote from *Quinn v Trifonovs*:[512]

> "It is not for me here to decide whether I am sure that a contempt has been committed or whether the Judge who ultimately hears the application will certainly be sure of it. It is for me to decide whether the applicant is putting forward a strong case that the Judge who ultimately hears the committal will be made sure of Mr Trifonovs' guilt."[513]

The judge went on to state, by way of decision, that:

> "I am satisfied that the evidence as it stands at the moment (and of course Mr Trifonovs has not filed any evidence in reply as yet) shows a sufficiently strong case that that Judge will be persuaded of guilt so that he is sure that it is right to allow the application to proceed."[514]

The standard of proof in the contempt proceedings is the criminal standard, beyond reasonable doubt. Unlike in insurance contract proceedings, where there has been a general reluctance to plead fraud, this does not appear to trouble insurers or put them off. It must be borne in mind that the contractual proceedings may have been conducted on the basis of putting the insured to proof; so that the civil standard applied to the claimant's entitlement to be indemnified on the facts as proven. Nevertheless if there are clear sworn records of the incompatible facts, a criminal standard of proof will not be a problem in criminal proceedings any more than in civil proceedings.

[510] Termed "ludicrous" at [13].
[511] At [4].
[512] *Supra*.
[513] *Quinn v Trifonovs* at [17].
[514] At [19].

What this seems to prove quite conclusively is that insurers are not troubled by an elevated standard of proof. It may of course be that the judicial legacy of the historical stringency has influenced insurers in taking the alternative procedural route, due to the simplicity of the means of proof in the shape of the statement of claim. This is justified by the apparent success rate – although there are likely to be unreported cases skewing the numbers, the reported cases demonstrate a success rate for insurers that is close to 100 per cent.

One failure in a prosecution for contempt is on record, and the failure was attributable precisely to the insurers failing to prove their claim beyond reasonable doubt. In *Zurich Insurance v Kay and others*,[515] the claimant Mr Kay had sustained injuries in a fall while on holiday abroad but submitted an insurance claim against Zurich contending that the accident had taken place in a car park in St Helens as a result of a slipping hazard.[516] The car park was the responsibility of a cleaning services company insured by third party liability by Zurich. Zurich brought proceedings for contempt of court against Mr Kay and his wife and stepson who had supported his claim with witness statements. Permission was granted. In the nomenclature of Mance LJ, this case would qualify as an entirely false claim in that although the injuries were real, the insurer was not on risk for the event that – per insurer's presented argument – actually took place.

In *Zurich v Kay*,[517] unusually, the body of evidence was characterised by conflicting statements as to the origin of the insurance claimant's injuries. The claim was made upon the basis that it had taken place in a location managed by the insured, whereas the insurers were submitting evidence that it had taken place earlier, in a different location. It was therefore not a matter of the nature and extent of injuries, but of whether the location of their origin was covered under the policy. The evidence therefore consisted of contradictory statements by the insurance claimant, his work colleagues and his former employer not least in the course of employment proceedings which had taken place following the termination of Mr Kay's employment, in the period between the injury (on either view) and the contempt proceedings. The individual items of evidence were therefore circumstantial in character and of such a nature that the full evidence needed to be weighed up against the burden and standard of proof. Indeed, the insurers were unsuccessful in this case, the judge weighing up the evidence and finding it to fall short of the standard of beyond reasonable doubt. The pivotal point appears to have been the evidence of Mrs Kay, which the judge found to be reliable. On behalf of the insurers, there were a number of witness statements which the judge said added up to a *prima facie* case but nothing more. Because the narratives of the three contempt defendants were linked, the reliability of Mrs Kay had the effect of casting doubt upon the case against all three defendants alike. The judge concluded by the following comments regarding the standard of proof.

[515] [2014] EWHC 2734 (QB)
[516] It will be noted that the injured party, Mr Kay, was a third party in relation to the contract of insurance.
[517] *Zurich Insurance v Kay and others* [2014] EWHC 2734 (QB) .

> "The discrepancies in the evidence of Mr Kay's work colleagues combined with the passage of time and the risk of cross contamination curtail the confidence with which I may otherwise have approached their evidence. I may well have concluded, had I been trying his personal injury claim, that Mr Kay had failed to satisfy the civil burden of proof on the issue of the location of the injury but the demands of the application of the criminal burden require me to be careful not too readily to find contempt where the supporting evidence is impaired by the features such as those which I have identified."[518]

A complex case such as this one with evaluation of witness evidence long after the events in question is a regular occurrence in criminal proceedings and the standard of proof to be met by the insurers and the prosecutor respectively is the plain, familiar 'beyond reasonable doubt'. It might be that the same evidence will appear more reliable when presented by a prosecutor than by an insurer, with its own agenda at the heart of the proceedings rather than simply the public interest as would be the case with a prosecutor. This is not in principle something that the judge should take into account – the question before the judge is what the evidence can be held to demonstrate. Nor is there any indication in currently existing case law that the fact that insurers are acting in a private capacity is held against them.

5.3.7 Timing and procedural nature

It is of some interest to consider the timing of inception of proceedings. As held in *The Star Sea*,[519] any post-contractual duty of good faith must come to an end when proceedings begin. Thereafter, the principles of an adversarial relationship apply between the parties, procedural tools are available in place of good faith 'duties' and the court may use its own tools of perjury, disclosure and contempt.

Irrespective of timing, a section 9 witness statement, even if made before the issuing of the claim form, must surely be considered a procedural statement rather than a statement made before proceedings and therefore arising out of the good faith context. However, it is nevertheless unlikely that *The Star Sea* can be called upon as authority for the proposition that such a statement cannot be used to defeat a fraudulent claim contractually. On the contrary, a false, sworn statement in support of a claim is likely to be considered at least a fraudulent device.

On the other hand, a witness statement following the issue of the claim form should in principle not be subject to the good faith doctrine according to *The Star Sea* – but there have been cases where that was the issue and which were discussed on an insurance contract law footing.[520] It may well be asked

[518] *Zurich v Kay* at [72] .
[519] *The Star Sea* [2001] UKHL 1.
[520] *Agapitos v Agnew*.

if it is entirely natural that the parties' duties under the contract, which may well remain in force for other purposes, should come to an end for the particular issue under litigation.

Using contempt proceedings gives significant flexibility to insurers. Statements made at any given time can be introduced into proceedings and will be an 'effective' untruth capable of leading to an order for contempt. No contempt decisions have thus far given any consideration to issues of timing and this must therefore remain a mere reflection.

5.3.8 Withdrawing the statement and remorse

Contempt proceedings have the virtue over fraudulent claims statements that the fraudulent statement can be effectively withdrawn. It was noted above that in this aspect, the forfeiture rule is entirely unforgiving. If for no other reason but practical and tactical ones, insurers are unlikely to pursue a defendant who has made timely efforts to correct an earlier false statement, such as Miss Yurtseven, the second defendant in *Quinn v Altinas* against whom the charges were dropped.[521] Miss Yurtseven had in support of Mrs Altinas' claims stated that she did not know the claimant, but Facebook materials revealed that they were well known to each other. In respect of this statement, insurers dropped the charges against Miss Yurtseven when it transpired that she had "written to the solicitors within two weeks of making that witness statement asking to withdraw it."[522] Insurers are under no obligation to drop charges, but if they do not, they risk the wrath of the judge for failing to recognise justice-minded and contrite behaviour.

The contractual principles are different, as pointed out above.[523] Thus the retraction of a false statement has been held not to be effective to negate the falsity of the claim: once made, such a statement cannot be unmade.[524]

Insurers are not always impressed by remorse; nor are judges as demonstrated by the contempt case *Esure v Shah*.[525] The claimant was a mere 'footsoldier', albeit quite a proactive one, in an organised motor claims fraud and had made his statement in the particulars of claim but was left without solicitors when the insurers' line of defence became apparent. At the time of sentencing he showed remorse but was nevertheless given a six months sentence.

[521] *Quinn v Altinas* at [21].
[522] At [21].
[523] See fn 129.
[524] *Direct Line v Fox*, *supra*.
[525] *Esure Insurance Services Ltd v Shah*, unreported, HH Shaun Spencer QC, High Court Division, Queen's Bench Division, Huddersfield Registry, 14 March 2011.

In *Zurich v Kay*,[526] it was pleaded by the insurers as a relevant fact that Mr Kay had discontinued his insurance claim. However, following waiver of the claim file on the advice of the judge, in possession of further evidence, declined to find that it was. He said:

> "privilege has been waived on counsel's advice. This document demonstrates that the author's assessment of Mr Kay's prospects of success had fallen to no more than 40-45% which effectively deprived Mr Kay of the ability to continue to run the case on a conditional fee basis. There is no evidence, therefore, that Mr Kay actually initiated or encouraged the process whereby the claim was discontinued whether out of fear of exposure that his whole claim would be exposed as being fraudulent or otherwise. His claim that there was simply no economic alternative to discontinuance is plausible. I also think that it is entirely possible that the personal injury claim was actually worth far less than the schedule figure and that he knew it."[527]

Germane to withdrawal is intent. In *Esure v Shah*, the judge appears to have accepted that Mr Shah did not know or understand that signing the statements would amount to contempt of court. He commented however that "I do not think that takes us very far" without developing the thought. This is reasonable – even a genuine lack of knowledge of the law is not akin to lack of criminal intent here. He knew that he was signing the statements, and – as the judge found – would have pursued the claim anyway if his solicitors had not got cold feet upon seeing the defence.

5.3.9 Sentencing

Although what insurers are seeking to do by pursuing fraud cases under the contempt umbrella is to set an example to others, the sentences imposed are by no means symbolic. Indeed as noted by the judge in *Mitsui Sumitomo v Khan*,[528] "If your conduct was to be dealt with by way of a criminal charge in a criminal court, the likely maximum sentence to which you could be exposed would be up to 10 years' imprisonment. Because you appear before this court for contempt of court, that possible maximum is 2 years' imprisonment."[529] Sentencing guidance for fraud, although not directly applicable, appears generally to inspire judges in contempt cases and there are consistently dicta regarding the effect of higher insurance premiums on honest members of society as well as on the need to safeguard the integrity of the justice system.

[526] *Supra*.
[527] *Zurich v Kay* at [72] .
[528] [2014] EWHC 1054 (QB).
[529] Ibid at [18].

In *Liverpool Victoria Insurance Company v Bashir and others*,[530] although the defendants admitted contempt, terms of immediate custody were imposed.

> "The detection of such fraud is very difficult. The diligence of the insurers in this case is to be highly commended. We were told that, until relatively recently, the police did not have the resources to investigate this type of fraud. Although, as this case illustrates, this type of fraud involves relatively small sums of money in each claim, together such claims give rise to the very large figures to which we have referred. At the beginning of this year the City of London Police have been funded by the insurance industry to set up a Motor Insurance and Insurance Fraud Enforcement Department which has the capacity to deal with 100 cases per month."[531]

Referring to this passage from *Liverpool Victoria*, in *EUI Ltd v Hawkins and another*,[532] the two defendants were sentenced for an admitted offence of contempt of court in respect of a motor insurance claim. The judge used the quoted passage to give initial emphasis to the scale of motor insurance fraud, before moving on to the usual and person-specific factors such as previous encounters with justice, family situation and genesis of the untruth.

Liverpool Victoria v Bashir was followed, in a manner of speaking, in *Liverpool Victoria v Thumber*,[533] where the judge noted that the court would have imposed a sentence of 12 months' imprisonment were it not for the insurance claimants' "admissions and provision of helpful information",[534] sentencing Mr Thumber accordingly.

Mr Aziz in *Aziz v Ali*[535] had had no prior encounters with justice, was of good character and a modest lifestyle and appears to have been the breadwinner for his wife and four children. He was the first of the defendants in the contempt proceedings to admit all counts of fraud. He had demonstrated regret and shame. Nevertheless the judge imposed a custodial sentence of six months. Such a sentence is not merely symbolic or a warning, it has real punitive effect not least in the case of the breadwinner of a large family with no previous experience of the criminal justice system. It demonstrates clearly that

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[530] [2012] EWHC Admin 895.

[531] Ibid at [11]. For an academic overview of the policing aspects of insurers' pursuit of fraud investigations, see the work of Mark Button, in particular Mark Button & Graham Brooks *(2014): From 'shallow' to 'deep' policing: 'crash-for-cash' insurance fraud investigation in England and Wales and the need for greater regulation, Policing and Society, DOI: 10.1080/10439463.2014.942847*. See also the Final Report of the Insurance Fraud Task Force, January 2016, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/492980/PU1817_Insurance_Fraud_Taskforce.pdf (accessed 20 January 2016).

[532] Cardiff County Court, Judge Jarman QC, 16 June 2015; available at http://www.bailii.org/ew/cases/Misc/2015/B15.html (accessed 27 June 2015).

[533] [2014] EWHC 3051 (QB).

[534] *Liverpool Victoria v Thumber* at [18].

[535] *Aziz v Ali & others* [2014] EWHC 4003 (QB).

insurers as well as judges mean business in enforcing their values. In the same case, the standout honest witness was Mrs Kazmi, originally a participant in the fraud who had repented, clearly impressing the judge.[536] She was the only participant in the fraud to receive a brief suspended sentence rather than a term of imprisonment. The basis for this lenient sentence appears to have been, in the words of the judge, her 'genuine remorse' rather than her responsibilities as a single parent to three children without any social network. The other three participants in the fraud received sentences of six to eight months, half of which to be served.[537]

While actual prosecutions for insurance fraud[538] are different in nature from prosecutions, the sentencing considerations are not different in kind and may be considered for guidance in contempt cases. Thus in *R v Barwood*,[539] the Court of Appeal was heavily influenced by the danger and inconvenience caused by the victim of the fraud, Ms L. Ms Barwood had reversed a large heavy car into Ms L's small car causing risk of injury as well as actual injury and significant subsequent inconvenience, along with Ms Barwood's active participation and multiple lies and active pursuit of Ms L in the courts for a replacement car hire claim.[540] Mitigating factors such as dependants and participation in "only" two counts out of 87 in the organised fraud ring in question did not weigh heavily in Ms Barwood's favour in such circumstances. The Court of Appeal pointed out that crash for cash frauds are not victimless crimes. All of these observations apply equally in contempt cases, albeit that some of the considerations are indirect in nature in that the criminal action itself is not a violent or dangerous one. The Court of Appeal approved the judge's approach in taking the guidelines applicable to money laundering and other fraud offences[541] as a guide, but pointed out the need to take into account the vicious and dangerous nature of the criminal act itself.[542]

If contempt proceedings are more commonly deployed against participating witnesses, it may not be correct to take into account the dangerous nature of the criminal act; however the Court of Appeal also reiterated the issue of rising insurance premiums and the social effects of this category of offences; considerations that do apply to contempt cases and arguably a fortiori given the unnecessary costs to the justice system involved. It is therefore also a clear pointer that the judicial system is not merely tackling a general social evil in agreeing to hear and decide contempt cases. The insurance

[536] In both the civil litigation and the contempt proceedings, the judge was Mr Justice Lewis.
[537] *Aziz v Ali & others* [2014] EWHC 4003 (QB) at [27].
[538] Also becoming increasingly common; viz the recent cases of *R v Barwood* [2015] EWCA Crim 1674 or *R v Claire Anne Davis* [2015] EWCA Crim 845.
[539] [2015] EWCA Crim 1674.
[540] "The harm in question here is not the financial harm of £50,000, but rather the devastation caused to Mrs Lawrence." *Barwood* (CA) at [16].
[541] *Sentencing Council Guidelines for Fraud, Bribery and Money Laundering Offences 2014*; technically not directly applicable.
[542] Having given consideration to personal mitigation circumstances, the Court of Appeal in *Barwood* reduced the judge's three-and-a-half year sentence to 30 months.

fraud cases form a part of the judicial system's self-preservation mechanisms – lying to the court needs to be a very serious matter for the justice system to be capable of operating properly and the fact that the lie arises from an insurance case, essentially a private matter, is not the prevailing factor in assessing the cases.

5.3.10 The costs equation

Mention of costs has been made several times in this chapter. It is appropriate to draw the strands together with a view to understanding strategy considerations applicable to the use of the contempt of court tool. Depending on perspective, contempt of court proceedings could be said to be very costly, or relatively cheap. They are of course very costly, in that cases that would otherwise be litigated before a District Court must be escalated to the High Court and judicial permission must be sought for the proceedings. They are also very costly by reference to the original premium income from an average consumer insurance policy. However, contempt proceedings are distinctly on the cheap side in comparison with fully-fledged civil proceedings involving a QC and several days of witness evidence. The evidence is often clear and straightforward in that it consists of a sworn statement and selected surveillance evidence, presented, in a straightforward case, by a relatively junior barrister.[543] Such proceedings are also cheap in the context of a large-scale commercial insurance fraud, on – say – a construction or marine insurance policy for a field of oilrigs or a fleet of cruise ships.

In *Zurich v Kay*,[544] Zurich's costs for the original proceedings had been covered by Mr Kay's legal expenses insurers, so that Zurich was not out of pocket as a result of the earlier proceedings.[545] This is likely often to be the case;[546] a point that serves to underline the separate and distinct purpose of contempt proceedings. It is appropriate to add that there may be scope for insurers to recover costs resulting from the contempt proceedings as such, but that issue appears not to have been judicially tested.

The costs equation leads to three distinct propositions with a tactical bearing.

The first is that insurers will be very selective in the proceedings they pick to take forward. Although among the cases are represented an ordinary father of four without a criminal past and other such non-conspicuous figures, the defendants also count among them a cage fighter and a model/football

[543] Although that is not always the case. In *Brighton & Hove Bus & Coach Co Ltd v Brooks & ors* [2011] EWHC 2504 (Admin) the insurance claimant had made statements to medical professionals who were evaluating the personal injuries at issue. Those statements were shown to the insurance claimants who made admissions in respect of some of the statements; but in respect of other statements, the insurers brought the medical professionals in question as witnesses to refute the statements of the insurance claimants.
[544] *Supra*.
[545] *Supra*, at [18].
[546] Regarding damages for costs incurred by insurers as the result of having to investigate a fraudulent claim, see under 5.2.1 above.

player.[547] The latter, more high profile type of character are suitable defendants from the perspective of insurers as they have the potential to be reported in the news at least locally and have a deterrent effect on others.[548] While there are only a few such high profile defendants until this point, and the first few cases that were still in the nature of test cases involved mainly ordinary folk, the balance of benefit is so clear given especially the modest premium income from each individual policy[549] that it should be expected that any person with potential for media coverage would be dealt with decisively if they were to be discovered to have made a false insurance claim.

A general strategy of pursuing high profile offenders however needs to be complemented with a selection of ordinary breadwinners, home makers, students, war veterans and grandmothers,[550] in order to demonstrate that the targeting is not so narrow as to be exclusive to comparatively high profile deterrent cases. Among the ordinary folk appearing in case law to date, most have played a minor part in the performance of some large scale criminal strategy as incidental witnesses. The ring leaders and fraudulent medical professionals issuing large numbers of certificates are probably better dealt with by the police as part of a wider counter-fraud strategy,[551] but a generally honest witness in financial straits, who has been roped in and tempted by criminals with what may appear to be a victimless act, failing to appreciate the bigger picture; or an (perhaps otherwise honest) claimant has time and again proven a suitable candidate for the contempt of court measure.

By way of prediction, it might also be expected that contempt of court proceedings will be undertaken in the context of a fraud under a large commercial insurance policy. The characteristics of such proceedings, should they materialise, will be quite specific. The selection criteria would have to be very narrow in order not to damage desirable business relationships or deter high-end clients. The case would have to be a very strong one, virtually guaranteed to succeed, so as not to put off honest

[547] As seen in the apparently unreported judgment described at http://www.horwichfarrelly.co.uk/miss-england-contestant-jailed-for-contempt/ (accessed on 9 September 2015).
[548] There are also examples of news reports of false claims without the accompanying litigation, such as http://www.theguardian.com/business/2016/jan/07/aviva-puts-breaks-mass-whiplash-claim-46-passengers (accessed on 11 January 2016). This claim was 'newsworthy' in the modern attention-seeking sense, involving a party bus and as many as 46 claimants, and a very minor prang, creating an overall sense of ridicule.
[549] Which is likely to be less than the indemnity sought but very importantly also quite insignificant compared to the litigation costs, so that no pursued case can per se ever represent a net profit.
[550] In *Barnes v Seabrook*, the two defendant insurance claimants in the joined cases against whom the application was successful were respectively a taxi driver and a fireman turned taxi driver. The application against the third defendant, whose profession was not stated in the judgment, was dismissed due to delay on the part of the insurers in bringing proceedings. In *Zurich v Kay*, *supra*, Mr Kay was employed as a contracts manager and his wife, the key exonerating witness, was a nurse.
[551] While investigating and prosecuting frauds was for several years a private matter for the insurance sector through the Insurance Fraud Bureau, operating since 2006, there is now also the Insurance Fraud Enforcement Department at the heart of the City of London Police, supported by the Association of British Insurers with the aim of investigating larger insurance fraud schemes. The recent insurance fraud prosecution *R v Barwood* [2015] EWCA Crim 1674 is a sentencing test case in an insurance fraud ring prosecuted by the authorities, not the insurer.

clients by giving the impression that the insurer had embarked on a policy of frivolous prosecutions. For the same reason, the ideal defendant would be the director or other liable person of a mostly defunct company, perhaps already marginalised from mainstream business and with a tainted reputation.[552] The prosecution would have to be a joint venture by several insurers underwriting the same policy, demonstrating that there is industry backing for the proceedings and eliminating doubt as to the future actions of individual insurers: the directors of high end corporate insureds with comprehensive insurance advice services will immediately be put off renewing their insurance with a company that were seen as frivolously prosecuting directors and putting them in prison.

The costs equation plays a second part too. The cost of proceedings is sufficient that insurers will not wish to take forward cases where there is any doubt as to the outcome.[553] Unless there is some important question of principle that absolutely needs to be tested, as in the early cases involving low profile ordinary persons as defendants, it simply does not pay to pursue minor league fraudsters on cases with an uncertain evidentiary position. In assessing whether a case should go forward or not, insurers will be looking exclusively at the slam-dunk cases. That means having not only a clear evidentiary situation but also featuring some highly blameworthy conduct well worthy of the judge's censure.

And a third and final implication of the costs equation is that the use of contempt of court proceedings is unlikely to be rolled out on a broad front to pursue any and all fraudulent defendants as a matter of course. Unless fraud were more or less abolished as a social phenomenon of importance,[554] and the number of fraudsters were to become so small as to be manageable within the income-expenditure equation of insurance companies, rolling out the pursuit of the contempt of court prize to all 'eligible' fraudulent insurance claimants would simply be too costly a strategy to be feasible.

The conclusion is that while the contempt of court continues to be a useful and accessible tool, there will be a clear, highly selective bias for figurehead defendants of whatever description, with a few ordinary folk thrown in for good measure, where the outcome is highly predictable. However, it is worth adding that it is not beyond the means of insurance as an industry to achieve systemic cost reductions, by lobbying for simplifications of the procedure that would facilitate access to court; for instance by removing the need for a separate decision on permission to bring proceedings and by permitting immediate proceedings where these can be done on the documents only.[555]

[552] Issues of corporate liability and the liability of corporate officers and directors for the actions of the company are well beyond the scope of this work.
[553] This is reinforced by proof issues: the burden of proof is on the insurer and the standard of proof is the criminal standard.
[554] And in such a utopia, counter-insurance fraud measures will hardly be necessary in the first place!
[555] While this author would deem such reforms likely to be within the realms of possibility, especially under the current government, there is no suggestion that this is in progress.

It is likely that this auto-selectivity on the part of insurers chimes well with the requirement implied by the public interest assessment at the permission stage. The effect of the reminder of Lord Justice Moore-Bick in *KJM Superbikes*,[556] noted in *Barnes v Seabrook*,[557] that the public interest limits the scope for granting permissions, will also doubtless play a part in limiting the number of prosecutions. It will not be possible to say which has the greater influence and it is perhaps not necessary to do so.

5.3.11 Conclusions

It is worth noting once and for all the complete absence of mention of good faith or moral hazard in these cases. Judges assessing insurance contempt cases do not refer to good faith or moral hazard as a factor. They do refer to widespread and costly fraud in the insurance services sector as a factor in sentencing – one of the factors plays into arriving at a firm penalty.

A unique feature of these contempt litigations is that the defrauded party is always an insurer – a category of party that does not suffer a financial disadvantage and financial constraints on litigation; besides the natural constraints on a business in terms of seeking to reduce legal costs and optimising strategy to achieve desired aims. One might perhaps therefore expect a hint of bias in favour of the insurance claimant – but no such benefit of the doubt can be read into the compilation of cases to date, whether at the permission stage or the contempt stage.

On a more technical level, it might be noted that while in civil insurance litigation, the burden of proof shifts according to the terms of the contract, in contempt proceedings the burden of proof is entirely on insurers for the elements of fraud. This is distinctly different compared to in civil insurance litigation, where the insured must prove the elements of its claim and the burden then shifts to insurers who must prove the existence of elements of some exclusion.[558]

The standard of proof for the elements of fraud, which is the civil standard in civil proceedings, is the criminal standard in contempt proceedings – a fact that until now has not deterred insurers, not least because the evidence is fairly clear and rarely circumstantial by this point. However, the fact that the standard of proof is the criminal standard presumably serves to restrict the cases that insurers will put forward for permission to try putative defendants for contempt. Where there is doubt as to whether the fraudulent act has been committed in the first place, that doubt has the immediate effect of placing insureds at a disadvantage where their proof must reach the standard of beyond reasonable doubt. While the evidence may sometimes be clear and unambiguous, such as in the case of a clear statement contradicted by clear medical evidence, or clear surveillance evidence showing, say, a purported paraplegic playing golf, a case can be made. However, where the evidence is complex and subject to

[556] [2008] EWCA Civ 1280; *supra* 5.3.3.1.
[557] [2010] EWHC 1849 (Admin), supra 5.3.3.1.
[558] *Wayne Tank & Pump v Employers Liability Assurance Corp Ltd* [1973] 2 Lloyd's Rep. 237.

evaluation, such as in the case of competing medical evidence or where the identity of the person in the surveillance footage is plausibly contested, insurers are unlikely to proceed. This is the case not least because a main purpose of contempt proceedings is to create social awareness of the risks involved in making fraudulent claims. If the defendant is successful, adverse media exposure is the likely result.

6 Conclusion

The topic of the present thesis is the law on fraudulent claims, placed in its enforcement and procedural context. The substance of the law, which had only just begun to crystallise at the beginning of this investigation, has been substantially clarified and developed in recent years. It continues to be under development and it is quite possible that as we await clarification from the Supreme Court on fraudulent means and devices as well as the entry into force of section 12 of the Insurance Act 2015, this may well be only the beginning. However, the law encompasses not only the substantive rules, but also the way they are followed or indeed avoided[559] or disobeyed. The full picture would include the effect of the rules in a sociological and psychological perspective – but that is a step too far for this project. The ambition here instead has been to discern, once the substantive rules are generally identified, the place of those rules within the wider context of insurers' enforcement strategy,[560] good faith, the moral hazard, as well as the effects of any uncertainty as to the contents and operation of the rule. This is where the associated rules on the burden and standard of proof become relevant: while the burden of proof has been straightforward, except in some idiosyncratic piracy cases, the insurer has historically been burdened with an elevated standard of proof for fraud and there remains some uncertainty as to the rule. It has been argued that the standard of proof should be the general civil standard without reference to the nature or inception of the underlying loss – the author feels that the arguments for this are convincing, but that there is no evidence of judicial practice having adopted the rule that flows from the child protection cases.

The current status of the law on fraudulent claims has in recent case law been decisively detached from the general concepts of good faith of moral hazard. As is seen from the description of the current state of the law in chapter 3, the current trend is to divorce fraudulent claims from the moral hazard and to consider it completely separately.[561] Today the law on fraudulent claims has been severed from its historic identity as an intrinsic part of the moral hazard and good faith. It is instead in the process of finding its place as a part of the law on fraud: first, the common law rule on fraudulent claims was established by the apotheosis of a near ubiquitous contractual clause into a common law rule, possibly but not entirely explicitly on the back of the *ex turpi causa* maxim. The judiciary having thus given the rule its place as a feature of the law, the next issue was the perfection of the rule itself and its conformity to the general law. This process has arguably not reached its conclusion given that the scope of the concept of fraudulent insurance claim is currently before the Supreme Court, with the likely outcome of determining whether a genuine claim submitted by fraudulent means and devices should attract the same remedy as a wholly fraudulent claim, and possibly also firm guidance on a test

[559] Not in the contractual sense, but in the ordinary sense of the word.
[560] Insurers' not insureds, because it is the insurer who enforces the substantive law on fraudulent claims.
[561] See not least Aysegul Bugra & Robert Merkin, supra fn 194.

on the subjective element along the lines of *Derry v Peek*.[562] Recent statute is to be welcomed but goes no further than to provide a remedy, so that all else remains subject to future case law. The law must crystallise into further answers, whether by legislation or by judicial development. A further consideration remains whether the concept of fraud arising from this context is consistent across various forms of tortious claims, in litigation and outside and whether insurance law ought to adapt to that. This latter question requires a broader-based investigation and would necessitate a second thesis for a thorough response, so the ambition here has been solely to develop the arguments in the light of awareness of this issue.

The author's view is that while the forfeiture rule on fraudulent claims has been disassociated from a more principled framework in the shape of, in turn, *ex turpi causa*, good faith and moral hazard, it is a clear and simple rule perfectly capable of liberating itself and standing on its own two feet. Whether it should be permitted to do so without taking into account the wider ramifications of severing it from its original framework is a thought process that has arguably not taken place thus far, or has at least not been completed, by the Law Commissions or the legislator. The process of reducing the scope of pre-contractual considerations of moral hazard so as not to encompass the risk of post-contractual fraud – whether this risk is latent or manifest at the pre-contractual stage – should involve an overall recalibration of the equilibrium whereby the advantages and opportunities lost are compensated by the introduction of other advantages and opportunities to rebalance the parties' bargaining positions. In other words, the Law has long been more favourable to insurers, for reasons of disclosure and moral hazard, and it may well be argued that the codification of a punitive fraudulent claims rule continues further along that path.

At the end of the nineteenth century, insurance fraud was difficult to discover, challenging to investigate and impossible to prove: there were technical obstacles to pleading fraud, not least of which was that proof was at the standard of beyond reasonable doubt. Fraud was considered an ungentlemanly affair to which supposedly no business man would stoop and was therefore rarely litigated in commercial courts. This was not a state of affairs that could last. Insurance fraud is a costly matter and insurers were always likely to include the litigation tool among the various means employed to attempt to stop fraud.

Subsequent developments have been very much in favour of the insurers. A rule separating out the insurance fraud from the good faith and prescribing the remedy of forfeiture, and probably also contract termination has crystallised in recent times. That rule applies not only to fraudulent claims tainted with invention, falsification or exaggeration, but also to authentic and valid claims supported by fraudulent evidence – in fact it has its greatest effect as a deterrent against fundamentally honest claimants. With the addition of fraudulent means and devices as a species of fraud, it became a rule

[562] *Supra*.

that gives insurers the procedural upper hand in that it permits a conclusion based on a simple comparison of documents. It applies not only to what we would recognise as fraud in the Clapham omnibus sense of the word, but to small exaggerations too.[563] The moral guidance quality of the rule is fatally tainted by the fact that a fraudulent claim cannot be withdrawn or corrected. The judgments on the subjective intent required for fraud have provided the first legal development that benefits the insured – but those are in question upon appeal.[564] Perhaps it is a sign of a pendulum shift – perhaps it is just a refinement in the law. If it takes hold, and if the test for subjective intent is ultimately deemed to be something more than awareness of one's actions, the equilibrium will have been re-established and insurers' easy ride to prove insurance fraud will not be quite so smooth. However, the rule did neither Mr Brown nor the claimant in *Versloot* any good.[565]

With the substance of the narrow rule on fraudulent claims mostly developed, meanwhile, on the procedural side, developments have again moved in favour of the insurer. It is now possible to allege fraud without pleading it;[566] a misguided plea of fraud does not annihilate the insurer's other defences and the standard of proof has over time been gradually reduced from beyond reasonable doubt to the balance of probabilities; the rule usually applicable in civil matters, although there is still the perception of a requirement that the evidence be particularly cogent – whatever that may mean in practical terms, and as has been demonstrated above, arguably wrongly. In evidentiary terms, supplementation of the previously existing instances of fraud by the new concept of 'fraudulent means and devices' also supplies a new tool to the insurers' arsenal – a potential avenue to prove fraud on the documents and potentially to obtain summary judgment without a costly full litigation,[567] and not least a means of avoiding evidence-intensive litigation about the financial difficulties of the insured and circumstantial evidence of fraudulent activities, sufficient to establish in the judge's mind the presence of fraud.

Finally, new avenues have been explored by insurers, reversing on a practical level the prohibition against damages for insurance fraud, permitting exemplary damages and going so far as to permit committal for contempt of dishonest claimants and witnesses. This strategy evidences multi-dimensional approach on the part of insurers – they are not restricted to the two-dimensional contractual situation; nor should they be. Insurance is a business and a form of commercial practice, and there is no reason why insurers ought to settle for an established, pro-insurer remedy in the contractual context. Insurers as active pursuers of fraudulent claimants, whether in tort or under an insurance contract, are helping shape the law well beyond the mere contractual matrix that is the usual

[563] *Versloot* .
[564] *Aviva v Brown* and *Versloot Dredging v HDJ-Gerling Industrie Versicherung AG* [2013] 2 Lloyd's Rep 131 and [2015] 1 Lloyd's Rep 32.
[565] Aviva and Versloot.
[566] *Kearsley v Klarfeld* [2005] EWCA Civ 1510, supra.
[567] As suggested in *Interpart Comerciao e Gestao SA v Lexington Insurance* [2004] Lloyd's Rep IR 690.

focus of analysis. Perhaps the main conclusion of this thesis is that it is necessary to look beyond the mere contractual relations for a full understanding of the position of the insurer, as well as the insured. The contractual insurer is no longer restricted to the mere passive remedy of putting the insured to proof of its claim. Instead, it now has a whole battery of remedies to unleash.

Such a shift has been possible for policy reasons: insurance fraud is a large scale industry and the victims are all insureds with policies for motor insurance, home insurance – very much the middle class electorate with its perceived influence on legislative and legal policy. But is this policy aim accurate in the context, or is it shortsighted as to the true nature of insurance law and the good faith doctrine? An endeavour has been to discern the extent to which insurers have embraced follow-up litigation as a tool to stamp out fraud. It has been shown through a review of all reported cases that while judicial attitudes are very much on the side of the insurers in this endeavour, with assertive judicial attitudes and emphatic use of available penalties, insurers are selective in bringing cases to court. Cases brought include egregious assistance to fraud rings, notable or newsworthy cases and cases where there is scope for recovering some damages. It becomes clear upon reflection that consistently pursuing all insurance fraudsters is much too costly an endeavour to pay direct dividends in a low premium business environment. However, this recent trend may well affect how civil litigation is conducted – once evidence of fraud has been secured, insurers are best served by a strategy involving an aggressive argument for summary judgment, or by alerting the insured to the possibility of contempt proceedings. This may well mean that the scope for major civil judgments on insurance fraud in future is reduced. Civil litigation does not serve any purpose for the insurers: the best they can hope for, in the absence of a damages remedy, is simply to not have to pay. While the initial suspicion before the research was therefore that the uncertain rule on fraudulent claims had caused ancillary contempt proceedings such as for contempt to arise, the now well-established judicial willingness to clamp down on insurance fraud in contempt proceedings can also be anticipated to create a feedback loop with effects on the optimal litigation strategy of insurers in the civil proceedings. As a matter of strategy and tactics, the standard of proof, exemplary damages, contempt proceedings and other such matters cannot be ignored when developing the civil proceedings.

Considering the law of the future, comprehensive statutory reform has changed the landscape and we have no crystal ball to know how it will be implemented. A starting point has been to understand the position of good faith and moral hazard in modern law, and the view adopted is that they are poorly understood and developed concepts in modern insurance law; unduly deconstructed and compartmentalised into sets of sub-rules that do not individually represent a coherent vision of the law. The original conception of moral hazard was – arguably – a clear and simple concept. This compartmentalisation and deconstruction have resulted in confusion and delay,[568] assisted by

[568] *Per* the Fat Controller.

contorted rules of proof, contractual lacunae and contrived pleadings. Law reform has resulted in the retention of the good faith rule, in s 17 of the Marine Insurance Act 1906, but with omission of the avoidance remedy. While this is consistent with the reform of the pre-contractual disclosure rules, there is arguably a lack of joined-up thinking about representations at the post-contractual level.

The judicial process is arguably not capable of achieving a single coherent framework, because proper action requires a single mind and directing thought. The Law Commissions have the advantage but have arguably not taken a comprehensive view on the moral hazard issue and the needs of the law on the theoretical and systematic level. Indeed, Issues Paper 7 considering the law on fraudulent claims arguably demonstrated precisely the lack of joined-up thinking and perspective that this author would respectfully recommend in law reform: the Law Commission pointed out that there was (said to be) a need for clarification of the common law rule on fraudulent claims; because legislation was supposedly necessary to clarify the position of UK law to European and other partners; and because deterrents and penalties ought in principle to be clearly set out in law. Instead, the real reason why law reform by means of statute is necessary is another: if the moral hazard is to be confined in practice to the pre-contractual or rather proposal stage, the law needs to be recalibrated in its entirety. This means the creation of consistent remedies and a coherent framework, which take into account the power shift in favour of the insurer that a detachment of the risk of fraud from the underwriting process entails and adequately compensates and protects the insured against abusive practices by insurers.

This work has also sought to demonstrate that while good faith and moral hazard are, as prominently argued, concepts void of principle, useful only as chapter headers in large authored works, social policy is very much a live concern in insurance law. One must look to see this at the wider context of enforcement against insurance fraud. The law, through the judicial system, has adopted an expansive view of what constitutes insurance fraud, recognising the punitive element present in the favoured rule and embracing - thus far – the inclusion of fraudulent means and devices into the concept. The law provides the remedies and sanctions in the shape of new legislation, and the judicial system has been enlisted in the service of combating insurance fraud by means of recognition of the contempt route as valid and justified. The latter point connotes an element of social policy – insurance fraud being cited repeatedly as a scourge of modern society and significant penalties being imposed for the participation in a fraudulent claim.

Nor does insurance law need, in principle, to depend on the punitive effects of a good-faith inspired rule on fraudulent claims. But perhaps the rules are complementary: the common law rule on fraudulent claims has its greatest effect on honest claimants, who stand to lose the most by a blanket forfeiture rule. Engaging the criminal justice system and sentencing offenders decisively is in essence a deterrent for fraud rings and those who think their contribution is trivial and of little importance. The latter are also the appropriate addressees of ubiquitous judicial comments to the effect that

insurance fraud is a social evil that requires decisive judicial action. Yet further measures will be more apt to address the problem of criminal or habitual insurance fraudsters. Thus registers, blacklists and exchange of information about insurance fraud convictions will be a much better deterrent than any contractual remedy.

The question arises: it being the case that insurers have devised a strategy to complement the contractual remedy route by penal means, do we really need a punitive rule as the principal remedy in contract law? Or should further thinking about the post-contractual representations cause us to arrive at normal contractual conclusions not intended to have a punitive effect, but simply to recalibrate the position of the parties according to what would have been the position but for the fraud? Damages were written off by the House of Lords and subsequently by the Law Commissions as a remedy. Perhaps that conclusion needs to be revisited in the context of a comprehensive review of the equilibrium of the law, unencumbered by the contractual injustices that prevailed until the enactment of the Consumer Insurance (Disclosure and Misrepresentations) Act and the Insurance Act 2015, and by the still unpredictable trump card of good faith?

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