The problem of identification - attribution of fault and negligence among players in hull and machinery insurance

By Andreas Meidell, Advokatfirmaet Thommessen AS; Dieter Schwampe, Dieter Schwampe, Dabelstein & Passehl; and Alex Kemp, Holman Fenwick Willan In this article the authors consider the extent to which the assured can be held responsible for errors or negligence committed by its employees, co-assureds or agents in a comparison of the Nordic, German and English marine insurance conditions.

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Introduction Marine insurers of hull and machinery risks are very dependent on the assured for information about the nature of the risk and that the assured's duties are fulfilled in respect of the technical and operational safety of the ship. This information is typically known only to the assured and is otherwise known as the principle of utmost good faith. As a result, these duties are specifically addressed in marine insurance conditions and the consequences for their breach are usually comprehensively regulated. The many and various functions involved in modern shipping are often performed by persons or companies who have been employed by the ship owner as servants, sub-contractors or agents. In the context of insurance this means that many of the functions of importance for the insurance contract are performed by a person or entity other than the assured. This leads to a difficult question: to what extent can the assured be identified with the persons or companies engaged by the assured, so that any error or negligence committed by them will have the same result as if committed by the assured?

Under Norwegian insurance law this problem is referred to as *identification* (*identifikasjon*). This Insight explores the issue by comparing its treatment by the Nordic, German and English marine insurance conditions.

Identifying the assured with its servants and agents It is unusual for all aspects and functions of operating a ship to be conducted by a single company or a small group of individuals, therefore compliance with the duties of care in marine insurance conditions will normally depend on actions taken by several companies. However, allocation of responsibility can vary between the different kinds of persons or companies involved with a ship's operating functions.

1. The main rule

Nordic conditions The main rule is stated in the Nordic Marine Insurance Plan 2013 (NMIP), clause 3-36, sub-clause 2:

The insurer may invoke against the assured faults and negligence committed by any organization or individual to whom the assured has delegated decision making authority concerning functions of material significance for the insurance, provided that the fault or negligence occurs in connection with the performance of those functions.

The starting point is that while the actions of another person can be attributed to the assured, this can only be done if two conditions are satisfied:

1. The assured must have delegated authority to that person in respect of functions of material significance for the insurance; and

2. The fault or negligence must have occurred in connection with the performance of those functions.

Making the assured responsible for a third party's actions is therefore based on functional criteria to be applied to the specific circumstances of each case. The Commentary to NMIP clause 3-36, refers to *technical, nautical and commercial operations as well as responsibility for crewing*, so all of these types of function may be of material significance.

Some guidance can be found in the cases of *Hamar-Kapp*[1] and *Midnattsol*[2] under the previous Norwegian Plan of 1964. These two cases held that when overall responsibility for supervision of a ship in layup was delegated to a named company and/or a named person, then the assured will be identified with that company/person, so that fault or negligence in carrying out their duties will be regarded as the fault or negligence of the assured. This is probably also the position under the NMIP.

German conditions Under the German Civil Code an assured is responsible for all persons he engages to fulfil his own obligations (clause 278). In the field of insurance this rule has been held to be too wide, devaluing insurance cover to a large extent. From the beginning of the last century, the German courts have narrowed the persons for whom an assured is responsible to a

group called *Repräsentanten*. The rule is that the assured is responsible only for those persons who, in the business area to which the subject-matter insured belongs, have taken the position of the assured by way of representation or similar legal relationship. Such persons are able to act for the assured independently and to a *not insignificant extent* (German Federal Court, Versicherungsrecht1993, 828). In contrast to the Nordic conditions, the aspect of significance relates to the assured not to the insurer.

English conditions Under English law, the general rule is that the assured can recover for a loss which is proximately caused by an insured peril. The nature and scope of the peril is a question of construction of the policy. As long as the claim is not excluded by law or by a term of the contract, the reason why the insured peril arose or operated so as to cause the loss is irrelevant.

Therefore, an assured can recover if its loss was proximately caused by an insured peril. Institute Time Clauses Hulls 1983 (ITCH) mostly adopt a named perils approach. The perils covered are listed in clause 6 and are split into two categories. The first allows recovery simply where the loss is caused by one of the specified insured perils. The second limits the cover to where the loss is caused by a specified peril *and* the loss or damage has not resulted by want of due diligence by the assured, owners or managers (the *Inchmaree Clause*). A number of exclusions appear in clauses 8, 23, 24, 25 and 26.

Of particular note is that it is no bar to a claim that the insured peril would not have caused the loss but for the negligent act or omission of the assured or his agents or employees.

So it follows that *identification* issues can arise in relation to: persons employed or acting on behalf of the assured; owners or managers; and other cases where a duty is imposed on the assured. This can be for example the duty of disclosure (see below) or duties relating to the operation of the vessel, such as the seaworthiness provision in section 39(5) of the Marine Insurance Act 1906 (the MIA). English law applies the so called *alter ego* principle to companies and other legal persons. The leading case is Leonard's Carrying Co v Asiatic Petroleum Co[3] and the application of this principle in the context of section 39(5) was discussed by Lord Denning M.R. in THE EURYSTHENES.[4] The issue is referred to as being one of "attribution of knowledge" and the approach adopted is a functional one that focuses on the decision making powers of natural persons within the organisation. In other words a similar approach to that of the NMIP, clause 3- 36, sub-clause 2.

2. Identifying the assured with the master or crew

Nordic conditions According to NMIP clause3-36, sub-clause 1, the insurer may not attribute to the assured faults and negligence committed by the ship's master or crew in connection with their service as seamen. That said, if for example, the ship's master carries out certain commercial functions on behalf of the shipowner, these would not fall within his service asa seaman and must therefore be considered under the main rule in clause 3-36, sub-clause 2. The position will then depend on whether the assured has given the master decision-making authority in matters of *material significance for the insurance*.

German conditions Under German law, the concept of *Repräsentanten* had not played any significant role in respect of master and crew until the early 1980s. Until then the market was handling duty of care cases exclusively on basis of clause 33 (3) German General Rules of Marine Insurance (ADS), which provides: *The Insured is not responsible for the behaviour of the ship's crew as such*. However, in 1983 the German Federal Court held that a master qualifies as a *Repräsentanten*. Similar judgments followed, though market practice largely disregarded these court decisions. This only changed at the beginning of this century, when a critical case went to court, involving unseaworthiness due to a stability calculation error undertaken by the master. The case settled without a judgment, but as a consequence a clause, widely known as the *Marine Print 12/2003,* was introduced into the market, which states:

If the unseaworthiness was the fault of the captain, the Assured will not be responsible for this if he proves that he did the necessary to send the ship to sea in a seaworthy condition and that he

secured organizationally that also the ship's command could take regard of and fulfil the applicable Provisions and rules of good seamanship.

English conditions Clause 6.2.3 of ITCH expressly covers, loss of, or damage to the subject-matter insured caused by *negligence of Master Officers Crew or Pilots*. This is subject to the due diligence proviso which only allows a recovery when *such loss or damage has not resulted from want of due diligence by the Assured, Owners or Managers*. It is no bar to recovery that the want of due diligence is on the part of a master, officer, crew member or pilot who is the owner or a part-owner of the assured property - even if that person is also the assured. Therefore a loss caused by the negligence of the master, officers, crew or pilot in their capacity as such is an insured peril, even if the negligent person is also the assured.

Identifying between co-assureds Today there can be a multitude of different parties having an interest in the ship (insured object), it is therefore quite usual to co-insure certain third parties and mortgagees. When all these parties have an assured status, they may individually bring claims under the marine insurance policy. The question then arises to what extent *one* assured could be identified with the faults and negligence committed by *another* assured.

Nordic conditions The starting point under NMIP clause 3-37 is that the fault and negligence of one co-assured cannot be attributed to another co-assured:

The insurer may not invoke against the assured faults or negligence committed by another assured…or anyone with whom they may be identified under cl. 3-36, sub-clause 2, unless the relevant assured…has overall decision making authority for the operation of the ship.

The purpose of this rule is to protect other co-assureds where another assured - who does not have overall decision making authority in relation to operation of the ship - has been negligent or at fault. It would be an extraordinary situation if a co-assured, without such authority, should interfere with the operation of the ship, and so it would be unreasonable for the benefit of the insurance cover to be prejudiced for the other co-assureds.

German conditions Under German law the principle of *Repräsentanten* applies to co-assureds. Therefore, if a co-assured fulfils the *Repräsentanten* criteria, the other assureds will be responsible for the fault or negligence of the co-assured. The conditions contain some clauses which deal with particular situations: clause 57 ADS deals with non-disclosure and misrepresentation; and clause 8 of the German Standard Terms and Conditions of Insurance for Ocean-Going Vessels 2009(DTV-ADS) goes beyond this and relates to knowledge and fault generally:

Unless otherwise agreed, where reference is made in these insurance conditions to the Insured's knowledge or fault in respect of certain material facts ("knew", "ought to have known"), this will apply equally to the Assured.

English conditions In England, the courts have consistently treated the co-insurance of separate interests under composite polices so that a breach of obligation by one interest does not affect the other insured interests This is also applicable to the pre-formation duty of utmost good faith. In applying this doctrine in New Hampshire Insurance Co vs MGN Ltd [1997] LRLR 24, the Court held that, "*where an independent interest is separately insured, there can be no question of avoiding the policy for non-disclosure quoad that interest unless the person so insured was privy to the non-disclosure*".

However, whilst a policy cannot be avoided against one co-assured for non-disclosure by another, it may be that the relationship between one co-assured is such that knowledge possessed by one co-assured ought to be known by a second, in the ordinary course of its business, so as to fall within the scope of the disclosure obligation owed by the second co-assured. For example, where co-assureds are member companies of a particular group.

Identifying the assured with the person effecting the insurance When it comes to possible breaches of duty of disclosure when effecting insurance, it is interesting to examine whether the

assured can be identified with the person effecting the insurance.

Nordic conditions NMIP clause 3-38 states that the actions of another person can be attributed to the assured:

The insurer may invoke against the assured faults or negligence committed by the person effecting the insurance.

The person effecting the insurance could be a commercial manager or a technical manager responsible for providing marine insurance cover. In these cases it is quite natural that the assured is identified with the person effecting the insurances- Furthermore, the assured will also be held responsible for breaches committed by servants of the person effecting the insurance, for example employees of a commercial or technical manager, or a broker engaged by a person effecting the insurance. As long as the assured has delegated the task of effecting marine insurance to another company or person, there will remain fully responsible with regard to the duty of disclosure under NMIP Chapter 3, sections 1 and 2.

German conditions In Germany, the general rule of the assured's responsibility for his *Repräsentanten* applies. There is a specific provision relating to contracts, clause 22 ADS provides:

In case of a contract being effected by an agent of the Assured it is not only the knowledge of the Assured, or what the Assured ought to have known, but also the knowledge of the agent, or what the agent should have known, which is decisive.

The last sentence of clause 22.1 DTV-ADS provides:

In case of a contract being effected by an agent of the Assured and in case of the agent's knowledge of a material fact, the Assured himself will be deemed to have had knowledge of this himself.

For cases of insurance taken out for the benefit of a third party, clause 57 ADS provides:

In the event of non-disclosure or misrepresentation of material facts the legal consequences shall depend on what was known or ought to have been known not only to the Proposer who effected the insurance, but also to the Assured.

English conditions Under the English conditions, it is the broker's duty to do his best to see that the assured's obligations of disclosure and absence of misrepresentation are fulfilled and he must not prejudice the assured by making misrepresentations to the insurer. If he fails in his duties, the insurer has a remedy against the assured and the broker will be liable to the assured. As a broker is not an agent of the insurer, under ordinary circumstances, he will not liable to the insurer in respect of honest but erroneous statements.

The MIA, section 19 provides further guidance on the obligation of disclosure:

Subject to the provisions of the preceding section as to circumstances which need to be disclosed, where an insurance is effected for the assured by an agent, the agent must disclose to the insurer:

(a) every material circumstance which is known to himself, and an agent to insure is deemed to know every circumstance which in the ordinary course of business ought to be known by, or to have been communicated to, him; and

(b) every material circumstance which the assured is bound to disclose, unless it comes to his knowledge too late to communicate it to the agent.

In the event that the broker breaches his duty to the assured, the broker is liable to the assured only for such loss as the assured can prove to have been caused by the breach. The broker may

allege, that, notwithstanding the broker's breach of duty, the assured is no worse off, either because the risk was in any event uninsurable or because the insurer had an additional basis for declining to pay, for which the broker was not responsible.

Conclusion The issue of whether the actions of another person can be attributed to the assured is addressed differently by the Nordic, German and English conditions. This may or may not lead to a variance in the way the issue is resolved under the respective marine insurance conditions.

When it comes to errors and omissions of the servants of an assured, the Nordic requirement is that the servant must have *decision making authority concerning functions of material significance for the insurance*. This seems somewhat parallel to the German concept of *Repräsentanten*, though the possibility cannot be excluded that considerations may be different when these concepts are applied in practice. The English conditions do not appear to have a concept of identification at all. However, the Inchmaree clause requires the exercise of *due diligence by the Assured, Owners or Managers*, which probably amounts in most cases be the same group of individuals or companies as those having *decision making authority* or *Repräsentanten*. Given this difference in approach, there is therefore potential for varying outcomes when adjudicated under the different regimes.

The concept that the actions of the master or the crew cannot be attributed to the assured seems to be more universal. Errors and omissions committed by these individuals are, in general, coverable under the insurance conditions. However, the principle that fault or negligence of the master is no bar to the insurance cover, seems somewhat more firmly rooted in the English conditions - and codified in the MIA, section 55(2)(a) - compared to the Nordic and German. The possibility exists under both the Nordic and German conditions for the fault or negligence of the master to have a detrimental impact on the insurance cover when the master has decision making authority or is a representative.

With regard to cover among co-assureds, the starting point under all three Nordic, German and English conditions is that errors and omissions committed by one co-assured is no bar to cover for other co-assureds. But also here, the Nordic and German conditions seem somewhat more open to exceptions when one co-assured has a decision making authority or a role as a representative. Under the English conditions, exceptions to the general rule seem to be more limited.

Finally, it seems to be a general principle under all three regimes that the actions of the person effecting the insurance must be identified with the assured, so that disclosure made by that person is regarded as made by the assured

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Questions or comments concerning this Gard Insight article can be e-mailed to the Gard Editorial Team.

1 ND 1973 p.428

2 ND 1991 p.2143 [1915] A.C. 705.4 [1977] Q.B. 49. See also THE SEA STAR [1997] 1 Lloyd's Rep. 360 CA and Arnould: Law of Marine Insurance and Average 17th Edition, pages 20-32.