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Insights

A MISSED OPPORTUNITY – HABERDASHERS AND SUBROGATION

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Earlier this year I found myself waiting for the Court of Appeal to bring the next instalment in a series of interesting decisions regarding subrogation claims in insurance disputes (not a contradiction in terms, I promise!), which I and my colleague John have been taking it in turns to blog about (see Joint insurance and rights of subrogation revisited and Co-insurance and subrogation rights revisited (again!)). Unfortunately (though perhaps not for those involved) the case in question (*Haberdashers' Aske's Federation Trust Ltd v Lakehouse Contracts Ltd and others*) settled.

But it feels as though there's been a missed opportunity to answer a question that was left entirely open in *Gard Marine and Energy Ltd v China National Chartering Company Ltd*: where there is a co-insurance policy in place and a sub-contractor causes loss, if the co-insurance policy (for whatever reason) does not cover the sub-contractor, can the insurer bring a subrogated claim against the sub-contractor or, does it first have to prove the sub-contractor is **liable** for the loss?

What we know so far…

In *Haberdashers* the court held that the sub-contractor was **not** covered by a co-insurance policy (project policy), but, on the facts, caused the damage in question. It was held liable for the losses suffered by the main contractor and the project insurers were entitled to bring a subrogated claim against it.

In *Gard Marine*, the Supreme Court established that there is a strong presumption of an implied term that precludes claims between co-insured parties, even if the contract contains an express warranty from the defendant party to protect the insured property. The presumption is that no subrogation claims are permitted between co-insureds. The contractual tier of the party is seemingly irrelevant in this presumption.

Gard Marine's strong presumption was not challenged in *Haberdashers* and it was taken for granted (or at least not questioned) that while there is usually no subrogation between co-insureds, this is not the position where a sub-contractor is not co-insured (for whatever reason). This makes logical sense.

As Lord Sumption (although in the minority in *Gard Marine*) said:

> "*None [of the previous subrogation cases] raised the question how the principle about co-insurance affects claims against a third party wrongdoer who is not himself a co-insured and is not party to the arrangements between them. There is no necessity to exclude a claim against him and indeed no reason why either of the co-insureds or their insurer should wish to do so. It is impossible to identify any contract whose business efficacy depends upon that result being achieved*."

Haberdashers therefore concentrated on whether the sub-contractor was or wasn't co-insured. Fraser J stated:

> "*In order to avail itself of what is effectively immunity from suit by a co-insurer, [the sub-contractor] has to demonstrate that it is a co-insured in the first place*."

A missed step

In this post I'm not questioning the rationale for deciding that the sub-contractor wasn't covered by the project policy (even if I can't believe it was the intention of the parties). What interests me is that the question regarding the **liability** of the sub-contractor in the first place wasn't examined. It was taken as read that as the sub-contractor, on the facts, caused the damage, it was therefore liable for it. We seem to have missed a step.

The majority view of the Supreme Court is that the effect of co-insurance (between the main parties in that case) is to **exclude liability** as between co-insureds:

> "*The reason why owners have no claim against [the main charterer]… is not that such a claim exists but is at some point discharged. It is that, under a co-insurance scheme… it is understood implicitly that there will be no such claim*."

(Lord Mance at paragraph 122.)

On this reasoning the main contractor itself has no liability; which suggests that there is no basis on which it could pursue a back-to-back claim against the sub-contractor.

The minority in *Gard Marine* came to the opposite view: there is liability but the co-insurance scheme discharges it (part of the rationale being to leave the door open to pass liability down the line). But the majority, including Lord Mance, did not agree and that is how it was left by the Supreme Court. On the question of liability and back-to-back claims down the contractual chain, Lord Mance considered the issue "entirely open" because on the facts of *Gard Marine* it was not tested. The only question before the court was as between the two main co-insured parties (and it was found there was no liability), not the liability of sub-charterers.

Following *Gard Marine*, it seems to me that the key issue is whether, if the co-insurance arrangements exclude liability between the co-insured parties rather than discharge liability (as the majority concluded), on what basis can a subrogated claim be brought against the third party wrongdoer? Applying this to the *Haberdashers* case, if the project policy excluded liability as between the main contractor and the employer, what liability was passed down the contractual chain to the sub-contractor to found the basis of the project insurers' subrogated claim against it? In *Haberdashers* it seems that this "entirely open" question wasn't asked, or even considered.

Final thoughts

In the conclusion of my blog about the Supreme Court decision in *Gard Marine* I (wrongly it would seem) concluded that:

> *"… the majority view that there is no liability to pass down the line to third party wrong-doers possibly raises even more questions… and may make it difficult for insurers to recover from negligent consultants or contractors. The basis of making a claim is now unclear.*"

Perhaps therefore it is for the best, certainly for insurers and for the business efficacy referred to by Lord Sumption in *Gard Marine*, that the basis of liability point didn't arise in *Haberdashers*. I can't help but think that at least the question might have been considered if there had been a Court of Appeal case and that settlement of the claim is a missed opportunity to iron out this point. We shall have to wait for the next case and the next set of facts. John's turn next; I look forward to reading about it!

This article first appeared on the Practical Law Construction blog dated 11 June 2019.

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