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A STUDY OF THE APPLICATION OF UTMOST GOOD FAITH PRINCIPLE
UNDER THE ENGLISH MARINE INSURANCE LAW
Legal Review and Practical Solutions

By

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DECLARATION

I certify that all material in this dissertation that is not part of my own work has been identified and that no material is included for which a degree has previously been conferred on me.

The contents of this dissertation reflect my own personal views, and are not necessarily endorsed by the university.

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IN THE NAME OF GOD, THE MERCIFUL, THE COMPASSIONATE

*In the Name of your LORD Who created;
Created mankind from something which clings;
Read! And your LORD is the Most Noble;
Who taught by the pen;
Taught mankind what he did not know;
(Cited from The Holy Al-Qurán; Surat Al-Alaq, 1-5)*

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ABSTRACT

Title of Dissertation : **A Study of the Application of Utmost Good Faith Principle under the English Marine Insurance Law : Legal Review and Practical Solutions**

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This dissertation analyses the application of the utmost good faith principle under the English marine insurance law and its implication to the benefits of the assured. English marine policy has been used by the assured internationally. An UNCTAD report (1982) said that approximately two thirds of the countries in the world utilizing hull or cargo insurance use the British conditions solely. However, one should aware of a principle of utmost good faith in the English marine policy, because the assured will loss his cover if he breaches it. It seems that principle is being applied mutually, both to the insurer and the assured. But, actually it is more favourable of the interest of the insurer. The situation is more unfortunate and unfair to the assured when such principle would apply to the marine insurance, regardless of the gravity of fault. In addition, the regime only provide a single-draconian remedy, avoidance of the contract. That remedy has retrospective impact legally. Much criticism regarding the disproportionate of utmost good faith application had been exposed. But, the will of revision of the good faith issues, in order to make it more flexible and balance, is less than it hoped. Such reform of the utmost good faith principle, had been recognised by the other European states, mainly civil law system states and some common law states, by reforming their laws related to the utmost good faith application. General notion of the reformation is to provide a fair and balance duty of utmost good faith and provide flexible of remedy based on the gravity of faults. It has a purpose to obtain a justice of the case for the benefits of both assured and insurer. However, a promising change of the good faith issue under the English law, had been obtain from the recent judgement of insurance case which allowed the assured to exclude the duty of utmost good faith including the draconian remedy by the inclusion of a specific clause to the insurance contract. Hoping that it constitutes a promising step taken by the English court in order to change the application of utmost good faith be proportionate and fair than before.

KEYWORDS : Utmost good faith, unfair and disproportionate, flexibility of other jurisdictions, change by contractual approach, exclusion clause of duty.

LIST OF ABBREVIATIONS

MIA	Marine Insurance Act 1906
Lloyd's Rep.	Lloyd's Law Reports (After 1967)
A.C.	Appeal Case
Lloyd's Report. IR	Lloyd's Reports Insurance & Reinsurance
L.I.L. Rep.	Lloyd's Law Reports Insurance & Reinsurance
App. Cas.	Appeal Case
Com. Cas.	Reports of Commercial Cases
All. ER.	All England Law Reports
CA	Court of Appeal
Q.B.D.	Queen's Bench Division
AP	Additional Premium
ICA	Insurance Contract Act

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CHAPTER I INTRODUCTION

In the maritime and related-industry, risks always exist. That is part integrally on the nature of the business itself. It is widely known that the nature of the maritime industry is a high-risky business. So why does the role of risk management has such important function in order to manage the risk as minimally as possible. In risk management, there is a branch called the treatment of risk consisting of four aspects : first, avoiding risk; secondly, controlling by risk reduction; thirdly, spreading risk by the transfer of risk; fourth, accepting risk by risk retention (Donner, 2002).

Insurance is an activity of managing a risk falling under the third aspect as a way of transferring a risk in the business. The insurance method of managing a risk is the “outsourcing” approach upon which the role of the insurance company will compensate the assured if the loss or incident occurs prejudicing to the financial condition of an assured. In the opinion of Donner (2002), insurance neither makes the risk disappear nor avoids or reduces the risk itself. It is simply the person who effects insurance should be compensated financially for the loss, returning the assured to the same financial situation that he would have been in if the loss had not occurred. So then as reward for the insurer who is deliberately taking over the risk, the assured is obliged to pay the premium agreed.

I. 1. Dominance of the English Marine Policy

In the context of insuring an activity or business, England is a predominant state which has an established and well-known reputation in the handling of the insurance business. Specially, the marine insurance activities constitute the are which that state has greater expertise and it is reflected by the application of the English marine policy in the international maritime community. According to an UNCTAD report (1982) approximately two thirds of the countries in the world utilizing hull or cargo insurance use the British conditions solely, or as an alternative to, or in conjunction with local policies. When considering only the developing countries, this figure rises to about three quarters.

I.2. English Marine Policy : How Do We Analysed it ?

Although, the English marine policy has gained greater recognition in the international maritime community, the critical question could be still raised by those who want to effect the insurance cover under the English jurisdiction for a better preventive action, is it really a safe choice legally to use the English marine policy for the benefits of the assured ? Because the English marine policy has its own character legally compared to other policies that one should be aware of, in order to ensure that certainty of indemnification is relatively secured to the assured. Therefore, in author's view, the scope of answer will be limited to certain aspects of the English marine insurance law. Such certain aspect is about the application of the utmost good faith principle which is one of the major principles applicable in the English marine insurance law and practice.

I.3. Is It A Safer Choice Legally to Use the English Marine Policy ?

A marine insurance contract is a contract of indemnity which secures the assured from any consequence of loss or damage in the marine adventure. One of the most important principle under marine insurance law is the utmost good faith principle. The principle or duty can be seen from section 17-20 of the Marine Insurance Act 1906, which stated that a contract of marine insurance is a contract based upon the utmost good faith, and if it is not observed by either party, the contract may be avoided by the other party. Indeed, it covers the features of duty to disclose as well as representation upon which the assured and his insurance broker should comply with.

In addition, the principle of utmost good faith has its own uniqueness which is shown in its application not only to the marine insurance business, but also to the non-marine insurance activities, such as property insurance, and fire insurance. The justification of the broad application of this principle, inter alia, was derived from the judgement of the Court of Appeal in the case of *Lambert v. Cooperative Insurance Society Ltd.* (1975) stating that there was no obvious reason why there should be a rule of disclosure in marine insurance different from the rules in other forms of insurance.

Obviously, the principle has its origin from the Lord Mansfield (Thomas, 1996, pp.32) in 1766 relating to the judgment of the Carter v. Boehm case which stated that “Insurance is a contract of speculation. The special factsis to be computed lie most commonly in the knowledge of the assured only; to mislead the underwriter into a belief that the circumstance does not exist..... is a fraud, and therefore the policy is void. Although the suppression should happen through mistake, without any fraudulent intention, yet still the underwriter is deceived and the policy is void.....” . In other words, there is no difference whether the breach of utmost good faith principle is done innocently, negligently, or fraudulently, the remedy of avoidance of the contract insurance must be given to either party.

It seems clear that the legal formulation of such principle may be interpreted strictly and unjustly, and thereby tends to be more favourable to the insurer. Accordingly, those applicable laws would make the legal position of the insurer stronger than the assured in each claim dispute settlement. In the light of such situation, up to a certain extent, the insurer may avoid the marine insurance contract on the basis of undisclosed information, which is completely disconnected to the causes of the loss or damage (UNCTAD,1982).

Therefore, when the unjust and unfair application of utmost good faith duty has had its full effect on the person effecting insurance contract in the English jurisdiction, it will create higher risk of non-indemnity for the simple breach of that principle against the assured and would result in financial disaster when loss or damage occurs. In that situation, the use of an English marine policy has put the assured in the high-legal risk position when he is deemed to breach of that duty.

As such, there have been increasing criticism levelled to the principle; there are some who believe that it contains opaqueness in its application and unfair treatment to the assured due to distortion inherent in its aim focused to maintain a balance duty of utmost good faith between the insurer and the assured. Others claimed that the strict application of this principle, particularly in terms of draconian remedy of avoiding the contract

including for a simple breach and or breach which is not related the occurrence of loss, was too rigid and that was no longer suitable under this modern time.

In respect to the rigidity and unfair application of such principle, it has been justified precisely when it is compared to the other policies under different jurisdiction of European states such as Norway, France, Germany which are mainly from the civil law system or a state from the common law system such as Australia, which at the beginning of its marine insurance law adopted the similar nature of utmost good faith principle applicable in English jurisdiction. Those states have taken a different and more flexible approach legally when they regulate the issue of utmost good faith duty application to marine insurance. Nevertheless, its rigidity of utmost good faith duty application in the English marine insurance law has been changing apparently by allowing to exclude the implementation of utmost good faith duty to the insurance contract by the assured, if the assured has had specific circumstances which put him in the position of having no relevant situation to observe the duty.

In light of such situation, this research analyses the existing laws applied in respect of utmost good faith principle and how the English court applies it in order to settle the case of breach of the utmost good faith principle. In addition, its development in recent times will be described from the relevant legal cases, and also how the assured should do legally with a purpose of obtaining a better position legally in order to protect his interests when effecting insurance contract in the English jurisdiction. The author assures that the necessity of the English marine policy changes to be more flexible in terms of the remedy and provides a fairer situation for the assured, would bring more benefits than harm for the acceptance of English marine policy in the international market, and with the hope that the harmonisation of marine insurance policy will come true in order to make it much easier for the assured to effect insurance contract without so much legal burden to identify which is a better choice legally for the protection of his interests.

The research is divided into five chapters: Chapter one gives a general description of the topic; Chapter two explains the theoretical background of utmost good faith duty from

the perspective of the civil law system as well as common law system including the English law system, including its legal relationship with the contract and tort law; Chapter three analyses the application of utmost good faith from the view of s statutory law as well as court decisions; Chapter four discusses the legal criticism of the difficulties and uncertainties of the legal approach taken by the English court when settling legal cases in respect of utmost good faith issues and a recent position taken by the English court for similar issues; Chapter five provides a conclusion and the legal solutions that practically could be used by the assured to have a better protection of his interests when effecting marine insurance contract in the English marine policy.

CHAPTER II

THE LEGAL THEORY OF GOOD FAITH PRINCIPLE

In commercial transaction, the involvement of law must be represented by the agreed conditions which is freely made by the parties who have an interest in the accomplishing of the commercial transaction. Such law is commonly called a contract, which might be written as well as unwritten. However, in this modern time and the fact that the commercial transaction itself, which mostly is quite a complicated, so that the contract is strongly recommended to have a contract in a written form. Major benefits of a written contract are exact and strong legal document that will be used as a valid evidence for the existence of the commercial transaction, and relatively easy to be proved.

Furthermore, in contract law perspective, one has a freedom of contract. In other words, when a person has an intention to make a contract, he could make any kind of contract, in terms of its content and form. However, a freedom of contract is mentioned here not an absolute freedom, but the limited freedom under the limitations of the fundamental aspects of law. The basic reason behind such limitations is to secure or maintain the equity or any other values which are deemed as very essential for the continuity of a society. The principle of good faith is one limitation created by the law to maintain the equity between parties involving in a contract. This principle of good faith has a role in the contract law as well as in the tort law.

II.1. Good Faith Principle under Contract Law

Beatson (2002) as quoted from the Section 1 of the American Law Institute's Restatement Second of the Law of Contracts gives the definition of contract is a promise or set of promise for the breach of which the law gives a remedy, or the performance of which the law in some way recognises as a duty. In addition, a contract has several functions in the commercial transaction. And among those functions, English law stipulates that the planning function is of paramount importance by its preference for rules that establish certainty in the commercial transaction. Again, contract law establishes a mechanism of remedy that is imposed by the contracting party in the context

of breach of the contractual duties as well as other duties imposed by the law related to the formation and or performance of contract.

As it has been mentioned above, contract law recognizes the concept of the freedom of contract, which has a twofold meaning; one related to its positive aspect, namely the creative power of the participants in the process to act as private legislators and to legislate rights and duties binding upon themselves. The other meaning was concerned with what may be termed its negative aspect, namely the freedom from obligation unless consented to and embodied in a valid contract (Beatson & Friedman, 1994, pp.7-8). The latter has the implied meaning that there is no liability without the consent stipulated by the parties in a contract. The result of such freedom of contract doctrine is to make the control over contractual terms minimum. Thus, it will lead to the anomaly of a contract which is represented by the establishment of a contract based on the ground of unreasonableness and or unfairness. Similarly when the contractual justice is talked, it has a meaning that an equity in a contract is merely to respect or honour the consent of the parties without considering the contents of the contract itself. In other words, there is no role for public policy to maintain the public interest in the form of supervising over the terms of a contract which meets the equity or justice between the parties involved or not. Or a contract could not be deemed as against public policy, although its content is clearly harsh or grossly unfair.

The regime of freedom of contract which created a nearly absolute right of parties` consent in a contract, has classified the contract law into two types: a classical and modern contract law. Beatson and Friedman (1994, pp. 9-10) that the classical contract law entails generally several characteristics; namely, the supremacy of the parties` intention which has described above, the marginal role of judicial discretion over the contract and the a very minimum pre-contractual duties. However, in practice, the classical contract law has its paradoxical situations, which exist in the context of relationship between the supremacy of parties` consent and the question of certainty of law in a contract, so that if the parties` consent was not “real”; for example if it was vitiated by the elements such as mistake, misapprehension or duress, that contract should

be avoided. Furthermore, under English contract law, the objective theory established a situation of no matter what parties` real intention is, if he so conducts himself that other party reasonably believes that he assents to the terms of the contract, he would be bound as if he actually agreed to them. From the “as if” regime under the objective theory, a person may be under a binding obligation to which he never consented, simply because he acted as if he did consent.

On the other hand, the modern contract law contains a different nature which is mainly characterized from its dominant role to control over the contract. Such control is implemented through the judicial discretion as well as legislative intervention by imposing statutory duty to the parties of a contract. This scope of control under the modern contract regime embraces equity of content in a contract and its contractual remedies. When looking it from the judicial discretion point of view, the court feels free to reshape the law and or develop a principle which should be applied to the contract. In the context of legislative intervention, the introduction of statutory undue influence gives the right to an injured party to rescind the contract. In addition, the modern contract law also recognizes the economic duress as vitiating factors to repudiate a contract. Conclusively, the modern contract law largely to dilute formal requirements and to attach greater weight to substantive fairness.

II.1.1. The Nature of Good Faith

The principle of good faith is a public policy interest which was established from the perspective of modern contract law. Historically, good faith has its origin in the Roman Law. And another name of this principle in the Roman Law is *bona fides*. It gained its influence as a result of a specific standard clause, inserted at the request of the defendant into the procedural formula which defining the issue to be tried by the judge. Ultimately, it gives the judge discretion to decide the case before him in accordance with what appeared to be fair and reasonable (Zimmerman & Whittaker, 2000).

At present, mainly under the law regime of the continental system, the notion of good faith comes from the establishment of a theory of *culpa in contrahendo* by the Rudolf

von Jhering in 1861. The theory addresses the specific problem presented by a contracting party, who has taken the initiative to enter into a contract, then sought its nullity on the grounds that he had been in error. The theory has an objective to protect the co-contracting party who had relied on the appearance of a valid contract and had suffered a prejudice flowing from the fact that his legitimate confidence had been deceived or misled. The legal concept in Von Jhering's theory fully resemble the regime of pre-contractual duty in the formation of contract. Therefore, the principle of good faith originated from the Roman law and the theory of *culpa in contrahendo* was adopted primarily in the German, French and Italian contract laws (Mussy, 2000).

For the common law system, particularly the English law, the notion of good faith principle is linked to the *doctrine of caveat emptor* which was established in the 16th century. It means that the buyer should be aware of fraud and or abuses of the seller/manufacturer. The purpose of this doctrine is to provide an out for the buyer/merchant against defects that are plainly and obviously the object of one's sense and attributed liability to the seller only for a defect that can not be discovered by sight and is a matter of skill or collateral proof.

According to Gordley (2000) the legal concept of good faith is very difficult to define. The jurist can only list different situations or pitfalls upon which courts have found this requirement to be violated. Nevertheless, considering the importance of good faith principle as an instrument to control over the contractual terms and its application, it is mainly better to refer several definitions about the good faith. The Uniform Commercial Code article 3-103 (a)(4) defines the good faith as honesty in fact and the observance of reasonable commercial standards of fair dealing. Thomas (1996, pp. 29) added that a good faith principle demands or may demand honesty, candour, openness, equal bargaining, fair dealing, assistance, cooperation, protection and disclosure of material facts. The definition of good faith principle is not a fixed one, but more flexible, broader and growing concept. It also has its meaning that a party must keep his word, refrain from deceit and overreaching and honour obligations that are only implicit in his contract. And neither party should mislead or take advantage of the other. It has been understood that

the legal concept of good faith principle has various elements. Among those elements, several main aspects that are thought will play dominant role in observing the good faith principle; namely, honesty, not to mislead, disclosure and fair dealing.

Under the perspective of German contract law, the principle of good faith has three basic functions : First, legal basis of interstitial law-making by the judiciary. Second, it forms basis of legal defence in private lawsuit. Third, it provides statutory basis for reallocating risks in private contracts (Ebke & Steinhaver, 1994, pp. 171). Those functions will give a broad basis for the court to establish a new cause of action where no cause of action existed in the statutory law. At the same time, it enables the plaintiff to seek remedy for unwanted contract and undesired contract or fundamental change in the contractual relationship between the time the contract was entered into and the agreed upon time of performance. For example, when one buy a defective product without knowing that such product was defective, the buyer may sue the seller for remedy under the regime of poor performance, not non-performance. Although, at the time of suing the seller, no statutory basis is applicable.

II.1.2. The Scope of Good Faith Principle

Each contract has its own specific nature. There is no guarantee that based on the freedom of contract, the party of a contract will feel satisfied and fair for the result of a contract. It is not uncommon that the party may feel that such contract is totally unfair and was formed under the unbalance situation between the parties. This unbalance situation may be arisen out in the form of unbalanced information between the parties, or it could be one party is depending too much on another party, so it creates a condition that the advantageous party has exploited the disadvantageous party.

The existence of good faith principle balances the role of freedom of contract and the question of fairness and honesty in a contract. In the issues of a contract, two main scopes are very important; namely, in the bargaining-process and in the performance of a contract itself. Therefore, the application of the good faith principle is under the scope of

bargaining-process or pre-contractual relationship as well as in the performance of the contract.

II.1.2.1. Pre-Contractual Duty.

A contract is a product of free will of the party. Accordingly, all elements, such as consideration, terms and conditions, and its collateral warranty in a contract, constitute a will of the parties involved. Thus, the pre-contractual duty of the good faith principle is to assure that a freedom of contract still becomes a basis for the validity of a contract. Because no legal system would legitimize use of violence, fraud or other unlawful means in the negotiating or bargaining-process (Cohen,1994, pp.25). If a contract is concluded by use of violence or fraud, it means that such contract is not a product of a free will of the contracting parties. In other words, the freedom of contract in the bargaining-process is limited through the prohibition for the contracting parties not being allowed to act so as to frustrate the pre-conditions for the existence of freedom of contract. In the context of the frustration of pre-conditions, the principle identifies two main aspects which are categorized as defects. Those are in the will of the contracting party as well as in the promises stated in the period of negotiation. For the will of the contracting party, defect is found when one party makes a contract as a result of a mistake, misrepresentation, duress or undue influence. In the second circumstance, the defect exists when breach of a promise given or expectation created in the period of the bargaining-process. However, in this second situation, the promise means something is included as a part of contract in the form of terms and conditions, and or representation; it does not embrace the promise/expectation to negotiate which is deemed legally as no promise at all.

Cohen (1994, pp.33-34) again added that frustration occurs in the will of the contracting party if there is discrepancy between the right will of the party and the real one expressed in a contract. This type of contract is commonly called an unwanted contract. Then, for the second case, the breach of promise happens when expectation given in the negotiation did not materialize in the contract. This is known as an undesired contract. However, in practice, these situations are imperceptible. Although these defects are difficult to differ from each other, the core thing that needs to be confirmed in the context

of application of the good faith principle in the bargaining-process is the influence of those defects to mislead in the formation of a contract. If there is influence on the formation of a contract, the good faith principle under the regime of the German contract law, may be used to seek remedy by the injured party. Finally, in the notion of pre-contractual duty under the regime of good faith principle, the duty of disclosure any material information needed by each party to form a contract is still a major requirement that the contracting party must meet precisely to the benefits of fair dealing.

II.1.2.2. Good Faith in the Performance of Contract.

The demand for the application of good faith principle in the performance of a contract is expressed clearly in several statutory laws. In the US Uniform Commercial Code section 1-203 stated that “ every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement”. Even under the scheme of the international transaction, the duty of good faith in the contract performance has its important position as it mentioned in the article 1.7 of UNDRIT Principles of International Commercial Contracts 1994 stating that each party must act in accordance with good faith and fair dealing in the international trade.

Weitzenböck (2002) states, in German, the notion of good faith principle is linked with the nature of *Treu und Glauben* which is enshrined in the section 242 of Bürgerliches Gesetzbuch (BGB) which provides in general terms that the debtor is bound to perform according to the requirements of good faith. This statutory law has wide effect in the German contract law upon which the court may establish the basis of obligation to ensure a loyal performance of a contract such as a duty of the parties to cooperate, to protect each other's interests and to give information. Furthermore, in her article Weitzenböck also quoted the explanation from the Whittaker and Zimmerman (2000) about the notion of *Treu und Glauben* as follows : “*Treu*....signifies faithfulness, loyalty, fidelity, reliability; *Glaube* means belief in the sense of faith and reliance. The combination of *Treu und Glauben* is seen to transcend the sum of its component and then is broadly accepted as a conceptual entity. It suggests a standard of honest, loyal and considerate behaviour, of acting with due regard for the interests of the other party, and it implies

and comprises the protection of reasonable reliance. Thus it is not legal rule with specific requirements that have to be checked but may be called an “open” form. Its content cannot be established in an abstract manner but takes shape only by the way in which it is applied. In some instances, Farnsworth (1994, pp.160) stated that the duty of good faith in the performance of contract may not only proscribe conduct or behaviour, but also may mandate affirmative action as well.

Beside that, under the perspective of the French jurists, the application of good faith in the performance of contract has two implied meanings for the duty of the contracting parties. First, a duty to act loyally; and second, a duty to cooperate. The first duty stipulates that one party must be free from bad faith, disloyalty and from manoeuvres which will make the performance of the contract impossible or more onerous for such party. A party is obliged to be judged to be in breach of loyalty duty if he imposes pecuniary hardship which is disproportionate or unfair to the usefulness of the object which the contract is purposed to achieve. Thus, the duty to cooperate contains the meaning of obligation to disclose the information or knowledge about certain facts in which one party has an interest to know in order to perform a contract, for example : in the sale of goods, the seller should disclose the information about its mode of use, manual to use and certain things should not be done, because it may create dangers. In addition, a duty to cooperate implies the necessity of the party to facilitate the performance of the contract by the other party.

Therefore, the concept of good faith in the performance of contract consists of two main types. These are the objective concept and the subjective concept. An objective concept of good faith performance refers to the behaviour or conduct of the honest businessman and under the perspective of subjective concept relates to the honest judgement of the party during the performance of a contract. Weitzenböck (2002) again provides the opinion of the Levanti in her legal writing about the relationship of good faith performance and the notion of abuse of rights, upon which the negative and positive duty of each party in a contract are recognised. Levanti said that the notion of negative duty of good faith performance means that a duty not to abuse of one's position so as not to unjustly

aggravate the situation of the other party. For the positive duty of good faith performance requires a contracting party to safeguard the usefulness of a contract for the other party insofar as this does not import an appreciable sacrifice of one's reason for contracting.

An example of the objective concept on the good faith performance can be seen from the US UCC section 1-203 which defined it as "honesty in fact in the conduct or transaction concerned". The word "conduct" fall under the category of objective concept.

II.1.3. Main Features of the Good Faith Principle

II.1.3.1. Duty of Disclosure

Any contract upon which the commercial transaction is established, always involves an exchange of information between the contracting parties. No transaction clothed in a contract will be concluded without involvement of proper information. This information has its function to give a clear picture about the nature of the transaction itself. Mostly, the information will articulate to the subject-matters or object of the contract. The result intended from this exchange information is to get a fair dealing of the transaction between the parties. Under the regime of good faith principle, an exchange of information about the object of the contract is under the scope of performing an honesty in fact. Then it should be delivered to the other party and negative duty as to not mislead for his own benefit. Having considered, the paramount importance of the information in a contract, the principle determines the necessity to impose a duty of disclosure. The general interpretation about this, it is a duty to disclose, inform or speak any information related to the execution of a contract. It applies commonly to the pre-conclusion of a contract as well as in the performance of contract. However, it focuses on largely in the negotiating process.

According to the Mussy(2000), generally, in relation to a contract, information may be considered in two ways : on the one hand, there is the information as the main object of the transaction and, on the other hand , which they are mainly common, it is obliged to give as a certain set of information is purely secondary. Therefore, the next question is how to determine the nature of information for the benefits of concluding a contract.

Fabre-Magnan (1994, pp. 102-103) explains the nature of information by three concepts : first, a party has only to disclose such information as is relevant having regard to the subject-matter of the contract and to the obligations undertaken by parties; second, such information should be essential, in which case the conclusion of the contract depends upon it, or such information is material in which case it will only influence the conditions under which the contract is concluded. Then a nullity of contract may be awarded as remedy for the breach of only disclosing essential information. The notion of essential or material information should be a question of fact determined by the judiciary settlement, and material facts are not opinion of the party. In addition, one may be deemed to conduct a non-disclosure act if remaining silent and failing to dispel a known misunderstanding of the other contracting party. In other words, the duty to disclose is an active duty, not a passive one. Thirdly, such information is likely to be useful for the basis of deciding a contract. If the information is not useful or even if it could cause damage, so that it does not have to be disclosed. For example, in the case of medical practice, a surgeon has no duty to disclose the exceedingly rare risks arising out of an operation, because such knowledge could cause such patient to refuse to undergo a very beneficial operation.

Furthermore, the duty to disclose is established based on several basis of circumstances. Those are : a) it arises as a result of unequal information; b) the actual knowledge of the contracting parties about the relevant information as well as the fact that such information is useful; c) no duty to disclose for the information already known; d) a contracting party may ignore the information provided by the other party. Under this circumstance, if such ignorance creates damage to such party, so no damages for that. In other words, the law does not relieve a person from the consequences of folly, imprudence and or lack of foresight (Birks & Yin, 1994, pp.79); e) the party is allowed to be unaware of information if : such information is impossible to know or one party relies on legitimately from the information guaranteed by the other party; f) in the context of the absence of knowledge or information, no party may use it as valid evidence to defence himself from the duty of disclosure if his absence of information is illegitimate. From this item, there is an implied

meaning that a party must have knowledge that ought to be known or is deemed to be known by him.

What it has been mentioned above, could be referred to the continental law system, mainly in the French or German contract law. Nevertheless, in the perspective of the common law system, the story of the duty to disclose has its different character, specially in the English contract law. English law has been hostile to the imposition of duty of disclosure (Fabre-Magnan, 1994, pp.106), although there was a doctrine of *caveat emptor* which requires the buyer to be aware and conduct a prudent action to examine the goods to be sold under the sale and purchase transaction. In order to avoid buying defective goods, there still remains one major principle applied to the English contract law. However, such hostility against the duty of disclosure does not occur in the context of insurance contract, which is categorized as contracts *uberrimae fidei*, which will be explained in detail in the following chapter. The reasons behind the hostility is opinion from common law jurists that the doctrine of duty of disclosure is very difficult to be circumscribed within the proper limits. In addition, such opinion was supported by the development of economic analysis of law, which was established by the prominent writers such as Anthony Kronman, Richard Posner, Bernard Rudden, etc.

The common conclusion taken from the study of those writers is no one who invest his resources to gathering information should be forced to disclose to the other party during the formation of contract (Fabre-Magnan, 1994, pp. 107). If he is permitted widely not to disclose information, it will encourage investment in the acquisition of information which finally brings benefits to the society at large. In other words, no obligation to disclose information derived from the basic thought that it is always a cost spent inherently by one party to gather information, so that without no reward to disclose such information, no obligation to disclose at all. However, there is possibility to disclose information in which such information has been casually acquired without any special investment, for example : in the sale of a house, the seller of the house should disclose information about the defects in the house, because such information is casually acquired by the seller by reason of his living in the house.

II.1.3.2. Representation and Warranty

According to Beatson (2002) representation means a statement or an assurance made by the contracting party served as to produce in mind of the other contracting party a belief that facts exist which render the proposed bargain advantageous to the interest of the other party. It also explained that a warranty is an agreement which refers to the subject matters of a contract as collateral to the main purpose of such contract, not as an essential part of the contract, either intrinsically or by agreement. The statement as mentioned above in the context of representation is about stating a fact, not intention, opinion or law (Treitel, 1989).

Theoretically, the legal concept of representation and warranty can be differed from the essential part of the contract which is called terms and conditions. Nevertheless, in practice, it is very difficult to determine such difference between representation and warranty and the terms and conditions. Having considered, the condition, which is the most essential part of a contract, might be in the form of a statement of fact, or a promise which is commonly felt under the category of notion of the representation and warranty. In addition, warranty has a similar function like representation to ensure that certain facts exist or not.

There are two types of warranty, and those are applied particularly in the marine insurance law. The first warranty called affirmatory warranty which has the meaning that a certain state of affairs exists at the time of making the warranty. Secondly, a promissory warranty binds its maker to a promise to do or to refrain from doing something during the performance of contract, or a certain of fact shall exist during the performance of contract (Hare, 2002). Both representation and warranty induce the contracting party to enter into a contract. However, their difference slightly may be pointed out by saying the notion of representation mainly has to induce in the period of negotiation to the contracting party to entering in a contract, and the notion of warranty which is largely decisive one by serving as to assure or guarantee the promise or statement which finally lead to the conclusion of the contract in the negotiation as well as in the performance of a contract. In the nature of

their remedies, both representation and warranty may cause the injured party to avoid the contract. Further, this sub-section will focus mainly on the discussion of representation, owing to the context of utmost good principle under English law, which separates the role of warranty law in the application of the utmost good faith principle

Specifically, in the context of representation, if one contracting party conducts a misleading statement in the formation of contract, such situation is defined as misrepresentation. It is simply a representation that is untrue (Furmston, 2001). The misleading statement, upon which the misrepresentation exists, may consist of three categories : first, it called “puff”, a commendatory expression which by its virtue of its vagueness or extravagance would not be expected to and does not ground any form of liability; second, the preliminary statement may be intended by neither party to have contractual effect, but may seriously affect the inclination of one party to enter into the contract; third, the preliminary statement may be a term of the contract or constitute a warranty collateral to the contract, if the making the statement undertakes or guarantees that it is true.

However, the first type is not sufficient to meet the nature of misrepresentation, owing to the nature of misrepresentation that should comply with several requirements upon which the liability may be imposed below.

1. There must be a false representation

A mere silence does not constitute a misrepresentation. However, there are three circumstances that may fall under the scope of misrepresentation. These are, firstly, where silence distorts positive representation; secondly, where the contract requires *uberrima fidei*; thirdly, where a fiduciary relation exists between contracting parties.

2. It could be partial non-disclosure and active concealment

3. Representation of opinion is normally insufficient

4. Expression of intention or prediction commonly is insufficient, unless for the person who has a special knowledge and skill. It may contain a representation of fact, that the maker of the statement have a duty to exercise reasonable care in making it.

5. Not a representation of law
6. The representation must be addressed to the party misled.
7. Representation must be unambiguous
8. Opportunities for inspection

When the representee does investigate and accordingly rely not so much upon such misrepresentation as upon the accuracy of the investigation, the cause of action for an operative misrepresentation will fail. In other words, no relief for being misled or having a weak or crippled judgment after investigation to the representation has been performed (Birks & Yin, 1994, pp.79).

9. Representation must induce the contract.

II.1.3.3. Nature of Inducement

Relating to the context of misleading statement and item j above regarding the inducement to enter into a contract through misrepresentation. The misrepresentation should still be treated as the misleading statement whether such statement of fact is included in a contract or not. Because the core notion of misrepresentation is the effect of pre-contractual statements to induce the other party to enter into contract. The notion of inducement is the most predominant factor to justify the existence of representation and unwanted/undesired contract made by the other party as a result of the misleading statement or misrepresentation. Based on such general overview, the further basic question may be arisen out what is really the meaning of inducement. Furmston (2001) explained that the meaning of inducement is as misrepresentation which have produced a misunderstanding in the other party's mind and that misunderstanding must have been one of the reasons which induced him to make a contract. It also was intended to cause and has in fact caused the other parties to enter into a contract. That is described precisely why a merely false statement, without the notion of actual inducement, shall not give rise to a cause of action or damages in the form of avoiding the contract.

Nevertheless, the notion of inducement and misrepresentation is legally acceptable or harmless if the party is misled under the circumstances below :

1. Never knew of its existence

A party misled must always be ready to prove that an alleged misrepresentation had an effect upon his mind. This duty should not be met definitely if he was never aware that it had been made. For example, if a buyer of stocks in a company claimed that he had been induced to purchase such stocks by a misrepresentation of publication of the false reports regarding the financial state of the company, he would fail in his cause of action for remedy if he is unable to prove that he had read one complete report of the company financial affairs or that anyone had told him of their contents.

2. Did not allow it to affect his judgement

There is no ground for remedy in the context of misrepresentation if the party misled does not allow or waive the representation to influence his judgement, even though it was designed to that end. As explained by the Furmston (2001) through the case of *Smith v. Chadwick* (1884) where party misled frankly admitted in cross-examination that he had been in no degree influenced by this fact. Therefore, no misrepresentation exists

Another situation may arise, if the other party after given a representation, do not rely on it, but he preferred to rely on his own judgement or business sense or upon an independent report which he specially obtained. As decided by the House of Lords in the *Attwood v Small* case (Furmston, 2001) that no remedy in the form of rescission under the regime of misrepresentation when the buyers had relied solely on the judgement of the independent agents about the accuracy of the statements than the vendor himself.,

3. He was aware of its untruth

A complete bar to obtain remedy for misrepresentation is when a representee has possessed actual and complete knowledge of the true facts or the knowledge of untruth of the misrepresentation, since the claimant could not claim that he has been misled by the statement of facts, even such misrepresentation was made fraudulently. Lord Dunedin added that no one is entitled to make a statement which on the face of it

conveys a false impression and then excuse himself on the ground that the person to whom he made it had available the means of corrections (Furmston,2001).

II.1.3.4. Types of Misrepresentation

Commonly, the misrepresentation is divided into three categories as follows :

1. Fraudulent Misrepresentation

Furmston (2001) defined that a fraudulent misrepresentation is a false statement which when made, the representor did not honestly believe to be true. Under common law system, the fraudulent misrepresentation not only renders the contract voidable at the suit of the party misled, but also gives rise to an action for damages in respect of the deceit (Beatson, 2002). Furthermore, he precisely added the definition of fraudulent misrepresentation through quoting the explanation of Lord Herschell in the case of *Derry v Peek* (1990) by saying that :

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 shown 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 the 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.

2. Negligent Misrepresentation

It defines by stating that an action in damages would lie for negligent misrepresentation if there was a fiduciary relationship between parties where the duty of care exists (Beatson, 2002 & Furmston, 2001). Therefore, in other circumstances a negligent misrepresentation made by one party to the other preparatory to entering into a contract may facilitate a legal basis to do an action for damages if the person making it has or professes to have special knowledge or skill in respect of the facts stated. Or if the representation in the context of the way of make it, is to be classified as neither casual nor unconsidered but to be relied on.

3. Innocent Misrepresentation.

An innocent misrepresentation means a misrepresentation is free from element of fraud or negligent statement.

II.2. Principle of Good Faith under Tort Law

According to Jones (2002) the law of tort is primarily concerned with providing a remedy to persons who have been harmed by the others, owing to the conflicts of interest in any society are bound to lead to the infliction of loss. The two main functions of tort law are to allocate as well as to prevent the losses. In addition, Rogers (2002) through the Winfield's definition of tort which explained that tort as a tortious liability arises from the breach of a duty primarily fixed by law; this duty is towards persons generally and its breach is redressible by an action for unliquidated damages.

The existence of good faith principle under tort law relies on the legal conceptualization of the tort law itself which establishes a mechanism of remedy for breach of duty imposed by the statutory law. Misrepresentation as well as non-disclosure upon which the breach of good faith principle committed by the other contracting party may fall under the legal scope of the tort law. So that, the notion of good faith principle itself may exist in the scope of contractual basis as well as statutory basis or both of them exist. Mostly, in the context of forming a contract in the specific subject such as marine insurance, the good faith principle, which is derived from the implementation of the duty of disclosure as well as representation, will be applicable both in the contractual basis and statutory basis. In other words, the contractual and tortious duties may co-exist on the same facts (Rogers, 2002). For example, if there is a case about a claim for damages as a result of buying a defective product, it may involve the notion of contract law as well as tort law. The seller may be liable on the some facts in contract and the other facts in tort to the buyer.

Although, the enforcement of good faith principle may be undertaken under the regime of contract law and tort law, the legal differences between both regimes can still be described. These differences are : firstly, tortious duty exist by virtue of the law itself and do not depend upon the agreement or consent of the persons subjected to them;

secondly, in tort the content of the duties is fixed by the law whereas the content of contractual duties is fixed by the contract itself; thirdly, the “core” of a contract is the idea of enforcing promises, whereas the law of tort has its aims principally at the prevention or compensation of harms.

In the context of third difference, it can lead to the two major consequences : first consequence, that a mere failure to act will not usually be actionable in tort, for such act should be intended as legally binding and supported by consideration or the formality of a deed; second consequence, that damages can not be claimed in tort for a “loss of expectation”, or as it is sometimes expressed, damages in contract put the claimant in the position he would have been in had the contract been performed, whereas damages in tort put him in the position he would have been in had the tort not been committed.

II.2.1. Existence of Negligence in the Good Faith Duty

Specially, the role of tort law in the scope of good faith principle is derived from the legal conceptualization of negligence. The concept of negligence has an important position under tort law. It defined tort as a breach of a legal duty to take care which results in damage to the claimant (Rogers,2002). Breach of duty is concerned with the standard of care that ought to have been adopted in the circumstances and whether the defendant’s conducts fell below that standard. Hence, a legal conceptualization of a duty which exists and breach by the defendant is the core ingredient of the tort or negligence. In order to identify the existence of a duty to care, Jones (2002) said that one should determine first the availability of the several circumstances; namely, first, foreseeability of the damage; second, a sufficiently “proximate” relationship between the parties; third, although where (1) and (2) are satisfied, it must be “just and reasonable” to impose such duty.

Furthermore, if analysing the legal concept of negligence and the breach of duty to disclose as well as misrepresentation under the regime of good faith principle, one may see the legal similarity, upon which the representor may act negligently in performing his duty to disclose and to represent the facts truly and honestly. At the same time, it can also create a wider legal basis for the claimant to claim damage to the person who committed

negligent acts. However, this claim for damages under the tort law prohibits the claimant to insert the profitable expectation, which is always allowable in the case of breach of contractual duties.

II.2.2. Liability for Misstatement

Besides that, in the absence of statutory basis for imposing the notion of good faith principle, in the English Law, one may use the legal concept of liability for statement in order to claim for damages. The existence of liability for untrue statement has wider coverage. Among the features of liability for untrue statement, one major features is one is liable for untrue statement if such statement causes the other person to act in reliance on it and suffer loss as a result (Rogers,2002). This liability for misstatement is based on the broader concept of assumption of responsibility. It comes out as a response of the common rule in the tort law which stated that there could be no liability in tort law for a false statement honestly made. The clear example for this circumstance is the relationship between the professional advisers with their clients. In other words, the combination of the assumption of responsibility concept with the reliance theory creates the regime of liability for untrue statement.

According to Beatson (2002) and Rogers (2002) the legal theory of the assumption of responsibility for liability of misstatement was crystallized firstly in the case of *Hedley Byrne & Co.Ltd v. Hellers & Partners* (1964) by which the House of Lords decided that although there was no duty of care on facts, but nevertheless agreed that a duty of care in making statements was a legal possibility.

From the same case, it was held that a duty of care could exist where there was an assumption of liability such as to create a “special relationship”. In order to obtain a clear legal concept of a “special relationship” in the context of liability for statement, Rogers (2002) again quoted from the legal reasoning of the Lord Oliver in the case of *Caparo plc v. Dickman* which described the typical character of a special relationship, inter alia, as follows : first, it is known, either actually or inferentially, that the advice so

communicated is likely to be acted upon by the advisee for that purpose without independent inquiry; secondly, it is so acted upon by the advisee to his detriment.

Accordingly, the regime of liability for statement shall exist hand in hand with the application of the assumption of responsibility theory, reliance theory and the requirements of a special relationship.

CHAPTER III
THE APPLICATION OF THE UTMOST GOOD FAITH PRINCIPLE UNDER
ENGLISH MARINE INSURANCE LAW

III.1. An Overview of Marine Insurance Contract

Marine insurance is a contractual basis relationship between the assured and insurer with precise rights and obligations stipulated in the contract of marine insurance. In general, a marine insurance contract is similar to other contracts upon which law of contract, will apply. However, owing to the specific conditions of a maritime adventure, it has inherently different nature in the terms of the legal process of the contract formation and its legal form after the contract is concluded. And under the English marine insurance law, the Marine Insurance Act 1906 prevails. A legal definition of marine insurance contract has been provided in the section 1 which stated that a contract of marine insurance is a contract whereby the insurer undertakes to indemnify the assured, in manner and to the extent thereby agreed, against marine losses, that is to say, the losses incident to marine adventure.

Furthermore, such losses from the marine adventure must be caused by something called as the maritime perils. No loss shall be indemnified, unless it is caused by the maritime perils agreed in the contract of marine insurance. Each party has freedom to determine any other perils that shall be included in the marine insurance contract. Additionally, it may cover a mixed risk between land and sea voyage. A transit clause attached to the institute cargo clause constitutes a proof of that.

For the definition of maritime perils, it has meaning as the perils consequent on, or incidental to, the navigation of the sea such as fire, explosion, detainment, and war perils. Commonly, it is called to the peril of the sea. When the incident of maritime adventure occurs, the insurer will indemnify after conducting a survey to verify the incident and then determine the level of loss experienced by the assured. If the level of indemnification was already agreed by both parties, insurer shall refer to such agreed value of indemnification.

III.1.1. Effecting A Marine Insurance Contract

There are three main parties involved in the placing of marine insurance. They are the assured, broker and insurer. The assured is the one who want to buy a marine insurance cover, and the insurer is the one who want to sell the insurance cover. Then the role of marine insurance broker is to provide service to aid for effecting a marine insurance cover on behalf of the assured's interest. The use of broker is not compulsory. The assured may effect the marine insurance contract by himself. However, as a result of the common practice, most marine insurance contracts are effected through broker, particularly in the London market. The broker shall be very helpful to the assured in order to get his full cover as well as to aid him for claim settlement.

III.1.2. Slip

Slip is a written proposal of insurance made by the broker with the intention to offer to the insurer for acceptance, subject to negotiation. The existence of slip for placing the marine insurance contract expresses the unique practice conducted in the London market. If the insurer has agreed with the slip made by the broker, he will sign the slip as an evidence of acceptance about the certain percentage of total risk he will accept, and write his initials, reference and the date of signing. And the acceptance of insurer through his signing on the slip must be unconditional. This method of process is called as slip placing system (Thomas, 1996, pp.9). The acceptance of a certain percentage by the insurer explain the principle of spreading risk in the marine insurance business. It is very uncommon practice in marine insurance business to place insurance cover only by the single underwriter. Thus, when the slip is signed by the insurer, so that the contract of marine insurance is concluded legally.

III.1.3. Marine Policy

Besides the slip, another legal requirement needed to effect marine insurance cover is the marine policy. A marine policy is the instrument in which the contract of marine insurance is generally embodied. The essential design is that the policy terms and conditions are to reflect the contract of the parties concluded on the slip terms and

conditions. The insurer is obliged to issue a marine policy, after contract concluded. One should be aware of the issuance of the policy, since the marine insurance contract will be inadmissible unless it is embodied in a marine policy. The word “inadmissible” means that the marine insurance contract only be recognized by the court as a valid evidence for the insurance cover if marine policy has been produced for such cover.

If there is discrepancies between slip and policy, the slip wording will prevail the policy wording(Thomas,1996, pp. 16). A remedy for that discrepancies is to rectify the wording of a marine policy based on the exact wording of the slip.

III.2. Marine Insurance Contract is *Uberrimae Fidei*

A marine insurance contract under the regime of English Law is treated legally as a specific nature compared to other types of commercial contract. It was proven by the application of overreaching principle of the utmost good faith to the contract of marine insurance that is commonly contradictive to the general perception of the legal status of the good faith principle in the common law system including the English law system, by which, English law has declined to adopt a general principle of good faith (Beatson & Friedman, 1994). The different legal treatment of utmost good faith duty showed the use of court discretion and rule of law principle in the English marine insurance law, which suited the concept of modern contract law, upon which the demand to give greater weight to substantive fairness in the context of marine insurance contract (Eggers, 1999).

The special role of this principle to the marine insurance, can be seen from the expressed statutory law, section 17-20 of the Marine Insurance Act 1906, which categorized marine insurance contract as an *uberrimae fidei*, upon which the notion of the utmost good faith principle is a must. Robinson (1998) stated that *uberrimae fidei* is a phrase used to express the perfect good faith, concealing nothing, with which a contract must be made. The Marine Insurance Act 1906 was drafted by Sir Mackenzie Chalmers and was the last pieces of codifying legislation. The 1906 Act did not seek to change the law, but rather was a codification of some 200 years of judicial decisions (Merkin, 2000). One predominant court decision had been used to formulate that Act, particularly for the

principle of the utmost good faith in the English law system, was the decision of Lord Mansfield in the case of *Carter v. Boehm* in 1776 (Thomas, 1996, pp.32-33). He stated the strong nature legally of utmost good faith duty under the insurance contract by saying that :

First, *insurance is a contract upon speculation. The special facts, upon which contingent chance is to be computed, lie most commonly in the knowledge of the insured only : the underwriter trusts to his representation, and proceeds upon confidence that he does not keep back any circumstance in his knowledge, to mislead the underwriter into a belief that the circumstance does not exist, and to induce him to estimate the risqué, as if it did not exist.* The keeping back such circumstance is a fraud, and therefore the *policy is void*. Although the suppression should happen through *mistake, without any fraudulent intention* : yet still the underwriter is deceived, *and the policy is void*; because the risqué run is really different from the risqué understood and intended to be run, at the time of the agreement.

From the legal observance of the Lord Mansfield above, several legal key points can be analysed. These were recognized as the major legal basis to establish the systematic legal concept of the utmost good faith principle in the English marine insurance law. First of all, the nature of marine insurance transaction which is named as the speculation one, and to manage this transaction is far from speculated action; the facts from the assured is a must to be informed to the insurer as a main basis for the judgement of the risks. Therefore, from this legal statement, the notion of duty of disclosure was evolved. And at the same time, all the facts disclosed must be represented by the assured while the insurer will trust on the honesty and truthfulness of the facts disclosed as well as representation made by the assured. The existence of misleading or inducement from facts stated by the assured plays important legal roles to determine the possibility to give remedy for the insurer. A remedy for the insurer as a result of non-disclosure as well as misrepresentation which made the insurer to be misled and or induced to place the marine cover for the assured is to avoid the contract, a draconian remedy. The critical point is the remedy to avoid the contract being awarded on the basis of mistake made by the assured. In other words, regardless of the gravity of fault when one breaches the utmost good faith (fraudulent, innocent, or negligent) the insurer will be given the right to avoid the

contract. In addition, the decision of the Lord Mansfield was directed apparently to focus more on the burden of the assured for the observance of the utmost good faith principle.

III.3. Legal Nature of the Utmost Good Faith Principle under MIA 1906

The section 17 determines the nature of that principle to the insurance contract as “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. There is neither precise definition about the utmost good faith principle in the MIA 1906, nor the legal guidance on what fields of operation this principle may be applied, particularly in the context of deciding the remedy of avoidance. Rather, this principle will be defined as to the legal concept of the *uberrimae fidei* and the complex combination legal concept derived from the section 17,18, 19 and 20.

In the beginning, unlike the legal conceptualization which formulated by the Lord Mansfield was expressly stressed on the duties of the assured to observe the utmost good faith principle, section 17 of MIA 1906 as mentioned above maintains the balance of obligation to comply with the utmost good principle for both the insurer and the assured. At least from the legal expression in the section 17, the assured has the right to demand the insurer to observe the utmost good faith principle. Nevertheless, this notion of the balance of duty for both the assured and the insurer, particularly the obligation of the insurer in the context of this principle, has changed when it applies to. It can be seen the settlement of the case of *Banque Financiere de la Cite SA v. Westgate Insurance Co. Ltd* (1990) upon which the Slade SJ, in the Court of Appeal, made different legal formulation as decided by the House of Lords by saying that :

In our judgement, the duty falling upon the insurer must at least extend to disclosing all facts known to him which are material either to the nature of the risk sought to be covered or the recoverability of a claim under the policy which a prudent insured would take into account in deciding whether or not to place the risk for which he seeks cover with that insurer.

However, the judgement has been rejected when it was settled in the English highest court, the House of Lords. The House of Lords had agreed the general observation of the obligation to comply with the good faith by the insurer, but it seemed that the Lords in

this same case as quoted by Thomas (1996, pp.31), having decided a contrary view by deciding that the primary insurer was not under duty to disclose the discovered fraud on the part of the assured's broker to the assured. In other words, in its application to this legal case, the nature of a balance obligation between the insurer and the assured in the observance of the utmost good faith principle was not justified legally, it tends to be more in favour to the side of the insurer.

III.4. Sanctioning System : Single Remedy ?

Referring to this section, the failure to observe the utmost good faith principle creates a single remedy without no more alternative. Such remedy is an avoidance of the contract by either party. The legal meaning of “..the contract may be avoided by the other party...” is the contract is rescinded by such party, and a contract is rescinded if the injured party makes it clear that he refuses to be bound by any provisions on the contract. The effect is that contract is terminated *ab initio* as if it had never existed (Furmston, 2001). Accordingly, this section affirms only a remedy by avoidance of contract retrospectively in nature as a single legal choice from the breach. One also should bear in mind that the nature of the remedy under the section 17 is precisely similar to the legal nature established by the Lord Mansfield in the case of *Carter v. Boehm*, upon which the contract may be avoided when duty of utmost good faith is breached regardless such breach was as result of the fraudulent, negligent or innocent conducts.

Therefore, the other remedies such as damages in the context of the breach of the utmost good faith principle, but rescission, are rejected. As it has been decided in the *Banque* case upon which the House of Lords dismissed the legal argument that breach of the utmost good faith duties could sound in damages (Thomas,1996). The legal position under the MIA 1906 about the single remedy for breach the utmost good faith principle is affirmed definitely through the decision of the Aiken J, in the case *HIH Casualty and General Insurance Ltd and Others v. Chase Manhattan Bank and Others* (2001) which stipulated that the insurers had no right to claim damages against the assured (Chase) for breach of the duty of utmost good faith; that issue arose only in relation to the contracts of insurance. And at the same time, the insurers also would not have the right to claim

damages for the negligent misstatements of brokers (Heaths) in relation to the contracts of insurance.

Although, it has been provided a single remedy, in the context of complex legal settlement to the case of breach of utmost good faith principle, the insurer may claim, in lieu of rescission, for damages based on the grounds of deceit made by the assured's broker. As mentioned in the *HIH* case, the Aiken J states the insurer would on the proper construction of the contracts of and for insurance have a right to claim damages for deceit based on the intention or reckless misrepresentation of fact by the Heaths, insurance broker whether in relation to the contracts of insurance or the contracts for insurance. Furthermore, the judges of Court of Appeal when examined such case as result of the appeal from the Chase, again affirmed the possibility to claim for damages against Chase by the HIH only on the basis of a good claim in deceit. The insurers would have the right to claim for damages either if such claim submit under section 2 (1) of the Misrepresentation Act 1967.

A good claim in deceit means that the claimant should prove the five legal natures that must be met in the context of such case : (1) there must be a representation of fact made by words or conduct; (2) the representation must be made with knowledge that it is or may be false. It must be wilfully false, or at least made in the absence of any genuine belief that it is true;(3) the representation must be made with the intention that it should be acted upon by the claimant, in the manner which resulted in damage to him;(4) it must be proved that the claimant has acted upon the false statement;(5) it must be proved that the claimant suffered damage by so doing (Rogers, 2002)

III.5. Utmost Good Faith : Its Scope of Application

III.5.1. Pre-Contractual Stage

A duration of the application of the utmost good faith principle applies mainly to the pre-contractual stage. The meaning of the application of utmost good faith in the pre-contractual stage reaches the duration of before or at the time of formation a contract. Owing to the nature of the insurance transaction, the reasons behind this pre-contractual good faith issue are to give earlier and strong legal protection for the insurer from the dishonesty or unfair insurance transaction, and to ensure the insurer in the same position as the assured and gives the insurer the same means and opportunity of judging the risk. This application is widely accepted as predominant legal practice when one deals with the utmost good faith principle in the contract. In addition, most of the time, claim for breach of the utmost good faith principle by the injured party on the ground of the breach of utmost good faith occurs before the contract is concluded. Its recognition of that pre-contractual stage as a major application of the utmost good faith principle can be seen from section 18 item 1 and the several cases below :

18 (1)- Subject to the provisions of this section, the assured must disclose to the insurer, *before the contract is concluded.....*”.

The importance of pre-contractual stage as a major concern in its application, has a reasonable ground from the breach of the good faith duty in the negotiation process which mislead the judgement of the either party (often:insurer) in respect of placing insurance coverage. It also become a common legal basis for the insurer while deciding to rescind the contract retrospectively on the ground of the breach of the utmost good faith principle, the stressing of failure to observe this principle in the pre-contractual stage usually is dominant. The nature of pre-contractual breach has been applied to the case of non-marine insurance, *St. Paul Fire & Insurance Co.Ltd(UK) v. McConnell Dowell Constructors Ltd. And Others* (1993). In that case, the Potter, J stated that :

(1) Having been presented with the risk described and having accepted it on particular terms and /or at particular premium rates without exclusion or

qualification, the plaintiffs were entitled to be told and /or defendants were obliged to disclose, prior to the contract, the change in the proposal represented by the decision to use spread foundations, whether that decision was made before or after the proposal was presented and quoted for; the failure to do so clearly amounted to a material no-disclosure; (2)...then the plaintiffs succeeded to avoid the contract on the grounds of non-disclosure.

Additionally, when this case was held in the Court of Appeal, all judges decided that the true state of affairs not disclosed to the underwriters before the contract was made was that the projects involved and the contractors intended to design and build shallow spread foundations rather than piled or other deep foundation, and subsequently the appeal by the assureds were dismissed and the decision taken by Judge Potter J to allow the insurer avoiding the contract was upheld.

The focus on the pre-contractual breach of utmost good faith was again affirmed by the other case of *Lambert V. Cooperative Insurance Society, Ltd* (1975) in the Court of Appeal when the insurers repudiated the claim on the ground that before the contract of insurance was concluded the assured had failed to disclose her husband's first conviction and on the further or alternative ground that she had failed before the renewal in March, 1972, to disclose the second conviction.

The focus on the pre-contractual duty, namely to observe the duty of utmost good faith in the course of negotiation has gained its support legally from the judgement of the case of *HIH Casualty and General Insurance Ltd and Others v. Chase Manhattan Bank and Others* (2001).

The predominant focus on the pre-contractual stage in the context of utmost good faith duty is to ensure the pre-contractual standard of behaviour between the contracting parties, insurer as well assured. It seems similar to the legal formulation of the doctrine of *culpa contrahenda*, that applied in the civil law states, upon which the remedy should be recoverable against the party whose blameworthy conducts during the negotiation for a contract brought about its validity or prevented from its perfection (Kessler & Fine, 1964).

III.5.2. Post-Contractual Stage

According to Soyer (2003) the existence of post-contractual effect in the application of utmost good faith principle, particularly in the contract of insurance is relatively new one in the English marine insurance law. It was firstly acknowledged at the beginning of the last century and the meaning and its legal nature was not judicially analysed until the beginning of the 1980s. This kind of post-contractual effect is derived from the broad meaning of section 17, which does not explicitly restrict the nature of the utmost good faith duty applied only in the negotiation period.

III.5.2.1. Fraudulent Claim in the Post-Contract Duty

In its legal application, key legal words should be ensured to exist in the case of post-contractual effect of utmost good faith duty which is the presence of any fraudulent conducts during the currency of marine insurance policy upon which the utmost good faith post-contractual effect may be established accordingly.

In the context of the insurance contract, the fraudulent claim could take three forms : either the assured intends to deceive the insurer in order to obtain money or some benefits from himself or some other person to which, it is known, there is no right; or the assured submits a claim in a situation where he has no honest belief in the truth of the claim; or the assured submits a claim recklessly, not caring whether it is true or false, and the claim is in fact false (Soyer,2003). Furthermore, he stated that the first type of fraudulent claim is a “pure fraud”. The pure fraud is classified into three categories namely: first, the assured may assert that he suffered a loss, which has not taken place; secondly, the assured might make a claim under his insurance policy after deliberately bringing about the loss; thirdly, the assured taking advantage of a loss might attempt to obtain an unlawful benefit from the insurer by submitting an inflated or exaggerated claim.

The next question about the third category of pure frauds is how to determine the nature of exaggeration claim upon which the fraudulent claim could be created. Lord Woolf, M.R. the judge of the Court of Appeal in the case of *Galloway v. Guardian Royal*

Exchange (UK) (1999) has established the method to measure the nature of exaggeration claim which is under the category of the fraudulent claim by comparing the percentage of claim that is deemed as a fraudulent claim with the total amount of the claim. In addition, the Millet, L.J., has a different approach in the case of determining whether the limit of exaggeration claim is fraudulent or not by considering the fraudulent claim as if it were the only claim and then considering whether, taken on its own, the fraudulent claim was sufficiently serious. Therefore, if there is a case of total claim is USD 100,000 with the exaggerated claim USD 2000, the Millet's approach would say that such claim is a fraudulent one, but Lord Woolf would reject it as fraudulent claim. It is strongly suggested that both methods be used to measure the legal scope of fraudulent contents in the exaggerated claim (Soyer,2003).

III.5.2.2. Fraud or Culpability is The Legal Basis of the Post-Contractual Duty ?

Back to the main issue in this sub-section, the nature of fraudulent conducts or claim which successfully triggered the application of post-contractual effect in the duty of utmost good faith was recognized firstly in the context of judicial settlement from the court decision in the case of *Black King Shipping Corporation and Wayang (Panama) S.A. v. Mark Ranald Massie* which was well-known to the *Litsion Pride* case (1985). In that case which states below.

The facts :

The plaintiffs were the owner of the vessel *Litsion Pride* which was insured against war risks with the defendant underwriters, syndicates 868 and 505 in the proportion of 75% and 25 % respectively at a value of USD 4,750,000 for 12 months from 5 pm on July 25, 1982. The clause of war risk trading warranty was included by A.P. for sailing on the excluded area and the requirement to inform such excluded area voyage to the insures as soon as practicable.

On May 25, 1982, *Litsion Pride* was chartered to make a voyage from Europe to a port in the Persian Gulf, later nominated as Bandar Khomeini. It was common ground that Bandar Khomeini at the time by far the most dangerous port in the Gulf attracting additional premium (A.P) at a very substantial rate. She crossed latitude 24 degree north in the straits of Hormuz on August 2, 1982.

By letter dated or purportedly dated August 2, 1982, the plaintiffs' management company Macedonia Shipping Co. Ltd (Macedonia) wrote to the brokers to proceeding with war insurance and advise the underwriters accordingly. The

brokers did not receive the letter until August 11, 1982. And then on August 9, 1982, while the vessel was passing in convoy through the Khormusa Channel at the head of the Persian Gulf, she was attacked by an Iraqi helicopter and struck by missile. Her cargo of sugar immediately caught on fire and fire spread to the engine room and adjoining compartments so that soon afterwards the whole of the after part of the vessel was ablaze, and water entered the hull. The captain and the crew were forced to abandon the ship. The vessel drifted aground on to a sand bank where she broke her back and sank. The incident was notified by Macedonia by telex to the brokers dated August 11, 1982.

The plaintiff claimed under the policy but the defendants denied liability contending that there was an implied term that the notification requirements contained in the warranty, on its proper construction, was a condition precedent to underwriters' liability for loss in A.P. area. The underwriters further argued that the owners and /or brokers were fraudulent or at least in breach of a duty of utmost good faith to the underwriters and that consequently were debarred from recovering under the policy.

Held by the Hirst, J :

1. The letter of August 2, 1982 was concocted and the false information invented in order to deceive the underwriters in the hope that they would accept the failure to give notice was innocent oversight.
2. Such letter was a fraud and connected directly with the claim and deemed as material one in respect of the presentation of the claim.
3. So that ,the plaintiffs were guilty of material fraud and material breaches of utmost good faith duty.
4. The remedy for that fraudulent conducts in the post-contract of marine insurance is section 17 which gives the right to the insurer to avoid the contract *ab initio*. However, because of the notion of avoidance the contract is not that it must be avoided, so then in the case of post contract breach it was open to the underwriters to defend claim without avoiding the contract. At the same time, owing to the duty not to make fraudulent claim and not to make claims in breach of the utmost good faith duty was an implied term of the policy, the underwriters entitled to maintain the defence of the fraudulent claim.
5. In his legal reasoning for the decision of this case, Hirst J also explained that the section 17 of MIA 1906 requires the continuing duty in the post-contract by imposing the assured to disclose material facts and not merely to refrain from dishonest, deliberate or culpable concealment.

Although the decision from the case above recognized legally to the nature of post-contractual dimension of utmost good faith principle which is restricted to the fraudulent conducts including claim, there are still several critical legal points causing much debate and or disagreements regarding their fairness and or its logic legally. The first critical issue of such case is legal assumption/interpretation regarding remedy under section 17

which provides not only to avoid a contract *ab initio* but also may reject the claim with no avoidance remedy at all in the context of post-contract dimension. Soyer (2003) criticised that no contract law principle as well as no case law explain why a fraudulent claim should be de-coupled from the policy entitling the insurer to reject the claim only without affecting the validity of the policy. Secondly, it seems very complicated to understand the decision to avoid a contract by the underwriters based on the reason of breaching an implied term of the contract upon which a duty not to make a fraudulent claim existed. Because when assumed the duty of utmost good faith as an implied term of a contract, the nature of remedy is totally different. Breach of the duty as an implied term would give the remedy for terminate the contract prospectively, while the section 17 imposes the remedy of avoidance contract *ab initio* with retrospective in its nature.

Third critical point is the legal assumption used in that case which stated that section 17 allows to use culpable breach of utmost good faith in the context of post-contract issue as legal basis to give draconian remedy of the avoidance of the contract. In other words, fraud is not solely a requirement to impose post-contract duty, negligent acts are also highly possible as a legal basis for claim of avoiding the contract. Subsequently, from this circumstance, there is similarity between the nature of breach of the utmost good faith in the pre-contractual stage as well as in the post-contract dimension. Both require the same standard of conduct and the same nature of remedy. Additionally, Hirst, J also demanded the assured to give time to time information during the currency of policy which may lead to the unnecessary or “endless” duty to inform that should be complied by the assured.

The decision of Hirst J in the case above was followed precisely by the Evans, J when decided in the case of *The Captain Panagos DP* (1982). In this case, the vessel which was the subject-matter of the insurance contract was grounded and then destroyed by the fire. Such incident was strongly alleged as a result of deliberate action conducted by the assured, shipowners. Under the nature of deliberate grounding, not the fire, fraudulent claim was submitted by the assured. Therefore, based on the legal basis formulated in the

case of *Litsion Pride* about the continuing duty of utmost good faith principle, the insurer is able to avoid the contract *ab initio*.

The judgement of the *Litsion Pride* had been criticised as creating an unfair and disproportionate circumstance through imposing similarity of its remedy to avoid the contract in the post-contract utmost good faith duty.

III.5.2.3. Legal Scope of Fraudulent Claim in the Post-Contract Duty

The case of *Manifest Shipping Co.Ltd v. Uni-Polaris Insurance Co.Ltd and La Reunion Europeene (The Star Sea)* (2001) shows an effort to relieve that unfair and disproportionate legal formulation adopted by the Hirst J in the case of *Litsion Pride*, by establishing the legal scope of the avoidance of the contract on the ground of the fraudulent claims. The facts that the *Star Sea* is owned by the single-ship management company, and Kappa Maritime which is beneficially owned by the Kollakis family. She was built in 1974. On May 27, 1990, *the Star Sea* sailed from Corinto in Nicaragua bound for Zeebrugge with a full cargo of bananas, mangoes, and coffee. On May 29, 1990, as a ship approached Panama Canal a fire started in her engine-room. It spreads to other parts of the ship and was not finally put out for several days by which time the ship had become a constructive total loss. The plaintiff claimed under the insurance policy but the underwriters denied the liability based on the ground of unseaworthiness of the ship. As to the emergency pump was useless, ineffective sealing of the engine-room, the master was incompetent in that he was unaware of the need to use CO₂ system as soon as he realized that the fire could not be fought in any other way and that for the system to be effective in the engine-room, all the CO₂ had to be discharged at once.

After trial was started, the underwriter also contended that the assured was in breach of duty of utmost good faith when presented the claim of the *Star Sea*. The legal basis for this accusation was the assured and their solicitors had misrepresented in witness statements and expert reports the facts concerning the assured's state of knowledge about the causes of the fire onboard the "Kastora", which they had obtained as a result of the reports of Dr. Atherton. It was also asserted that the assured had been guilty of non-

disclosure of the two reports of Dr. Atherton on the Kastora fire. It was alleged that various people, who were said to be “alter ego” of the assured, had been guilty of fraudulent or reckless misrepresentation in their witness statements (Soyer, 2001).

In respect of this case, Tucker J held that in the absence of fraud or recklessness about the presentation of the claim, section 17 of MIA 1906 would not be applicable as defence for the insurer. He also added that when the underwriters rejected the claim or the trial was started officially, there was no more the post-contractual duty of utmost good faith principle. Furthermore, when the case was settled in the Court of Appeal, the decision was upheld precisely with its different notion about the end of duty only based on the basis of the commencement of the trial proceeding, not when the claim was rejected.

In that same case, the House of Lords upheld the decision taken by the two courts above, and in specific stipulated that only fraud, not culpability, could be a legal basis to obtain a defence with the remedy of the avoidance of contract ab initio under section 17 of the MIA.

Although, the legal certainty has been obtained from the decision of such case above about the fraud is the only legal basis for the post-contractual duty of utmost good faith, it was still not precisely clear what kind of fraudulent claims/conducts during the currency of the policy determined by section 17. How is the role of materiality as well as inducement theory in this context. Those legal questions will be covered by the explanation from the case of the *K/S Merc-Scandia XXXXII v. Certain Lloyd's Underwriters Subscribing to Lloyd's Policy No.25 T 105487 and Ocean Marine Insurance Co.Ltd and Others (The “Mercandian Continent) (2001)*. In that case, it was explained that Trinidadian ship repairers were the assured under a liability insurance policy. They became liable to shipowners (the claimants) under the ship repair contract. The policy contained the following provisions which are relevant about notice of claims :

In the event of any occurrence which may result in a claim....the assured shall give prompt written notice....and shall keep underwriters fully advised.

In addition, there were general conditions for claims control by stipulating that “Underwriters shall be entitled ...to control or take over the conduct of investigation defence and settlement of any claim”. As a result of using the J form policy insurance, agreed that “If the assured shall make any claim knowing the same to be false and fraudulent, as regards amount or otherwise, the policy shall become void and all claims hereunder shall be forfeited”.

As a matter of the vessel, her engine was exploded and severe damage was done to the vessel. Such incident was accepted due to the negligent repair works done by the assured. The claimant claimed against the assured for negligent repair and consequential loss. Notice of a potential claim was given to the insurers and the insurers agreed to take over the defence of the claim.

Proceedings were started in the English Court by the claimants against the assured and permission to serve the proceedings out of the English jurisdiction was obtained. The assured then to the solicitors appointed by the insurer a forged documents (letter of July 1) which the assured thought would assist the solicitors on the issue of the English jurisdiction. The forgery was discovered and the insurers avoided the liability for breach of the duty of utmost good faith and breach of contract by the assured.

It was held by the Aikens, J *inter alia* that :

1. The assured’s fulfilment of the express and implied contractual obligations has nothing to do with the claim on the policy. They only concerned the provision of information in relation to a collateral matter, whether the English or Trinidad Court had jurisdiction could not make any difference to the liability of the insurers, so the insurers were not going to be prejudiced in respect of either “risqué” or “speculation” or in relation to his ultimate liability on the claim. Although, the assured had forged the July 1 letter, it would not have influenced the outcome on the issue of the assured’s liability to the claimants.

2. The deliberate and culpable misrepresentation such as forged July 1 letter was immaterial. It had no legal relevance to the assured's claim, and either the duty of utmost good faith did not attach to the acts of the assured in producing it or the act was not a breach of the duty of utmost good faith that gave the insurers the right to avoid contract.
3. There was no evidence to suggest that the defendant insurers were induced to do anything in relation to the claim under the policy as a result of production of the July 1 letter; if the "narrow" definition of "materiality" was correct, then the inducement of the insurers could only be in relation to a fact that was material; if facts that did not concern the legal liability of the insurers on the claims were immaterial, then there could be no relevant inducement of the insurers by an immaterial fact; and the insurers were not entitled to avoid.

When that case was brought to the Court of Appeal, the judges had precisely upheld the judgement of the Aikens, J based on the similar legal reason that underwriters had suffered no prejudice as a result of the assured's fraudulent acts. So that no remedy of the avoidance of contract will be awarded to the insurer.

Furthermore, the critical legal issues raised by the Longmore, LJ about his judgement in the Court of Appeal for the same case that variations to the risk, renewals and held covered clauses, would not be treated legally under post-contractual duty of utmost good faith.

The nature of materiality and inducement which were required to judge the fraudulent claim under the regime of the post-contractual duty, again was judged from the judgement of Toulson J in the case of *Agapitos v. Agnew and Others (The "Aegeon")* (2002) where he decided that the defence of the underwriters to avoid the contract under the scope of the section 17 for breach of continuing duty of utmost good faith based on the reason of , during the proceedings, the assured had been the party to putting forward a knowingly false case about when the hot works began, was rejected. It was caused by the legal reasoning which was formulated in the *Star Sea* case, by which the subsequent lies

told by the assured, mainly in the proceedings would not amount to concealment of facts and also would not have had any effect to the ultimate liability of the insurers.

Accordingly, the position of the English marine insurance law in that issues is, in the absence of the materiality and prejudiced impacts to the ultimate liability of the insurers regarding the fraudulent acts committed by the assured during the currency of contract, the post-contractual duty of utmost good faith which gives the remedy of the avoidance of contract *ab initio* would not exist.

III.6. Duty of Disclosure and Knowledge of the Assured

Although, in the contract of insurance, particularly marine insurance, the nature of information is definitely very important. It is caused by the nature of marine insurance contract in which the unequal of information between the insurer and the assured exists. At the same time, it is common in the insurance contract transaction where an insurer relies on the information provided by the assured. It was explained by Wilhelmsen (2000) the legal reason behind that duty is a question of fairness, in which to evaluate the risk with less information related to the risk that particularly possessed by the person effecting insurance would create inequality between the contracting parties. Further, an economic reason for that duty is to minimise cost to both the insurer and assured. One would realize that the cost of insurance will be much higher if the insurer should investigate the risk by himself without support from the obligation of disclosure the material information with regard to the risk insured. That circumstances had triggered the application of the duty of disclosure, particularly during negotiation, in the scope of utmost good faith principle. This duty of disclosure plays a very significant role in order to apply the utmost good faith principle in the marine insurance contract. Under the English marine insurance law, such duty is strongly supported to be precisely complied with by the assured. If failing to comply, the draconian remedy of avoidance the contract would be given to the insurer. The strong nature of duty to disclose in the context of marine insurance under the English law can be seen from section 18 of MIA 1906. As stated by the Justice Lloyd J in the case of *Container Transport International Inc. (CTI) and Reliance Group Inc. v. Oceanus*

Mutual Underwriting Association (Bermuda) Ltd (1982), section 18 is an extremely powerful weapon placed by law in the hands of the insurer.

18 (1) Subject to the provisions of this section, the assured must disclose to the insurer, before the contract is concluded, every material circumstance which is known to the assured, and the assured is deemed to know every circumstance which, in the ordinary course of business, ought to be known by him. If the assured fails to make such disclosure, the insurer may avoid the contract.

18(2) Every circumstance is material which would influence the judgement of a prudent insurer in fixing the premium, or determining whether he will take the risk.

18(3) In the absence of inquiry the following circumstance need not be disclosed, namely:

- a. any circumstance which diminish the risk
- b. any circumstance which is known or presumed to be known to the insurer. The insurer is presumed to know matters of common notoriety or knowledge, and matters which an insurer in the ordinary course of business, as such, ought to know.
- c. Any circumstance as to which information is waived by the insurer.
- d. Any circumstance which it is superfluous to disclose by reason of any express or implied warranty.

18(4) Whether any particular circumstance, which is not disclosed, be material or not is, in each case, a question of fact.

18(5) the term “circumstance” includes any communication made to, or information received by, the assured.

The duty of disclosure should be performed by the assured before the contract is concluded. What to be disclosed is about the material information upon which the insurer would be influence in order to fix premium or take decision whether to accept or refuse the risks. The information that must be disclosed not only the actual information that is known by the assured but also the constructive information. It means that the ignorance of the assured about the information not in his hand or having it partially is unacceptable if such information is deemed under the notion of ordinary business condition, ought to be known by the assured. This duty was widely accepted as an active one. How is the scope of this duty applied in the context of the English marine insurance law and practice, will be explained below.

The nature of duty to disclose as mentioned in the section 18 is largely stronger when it is applied in the case of insurance contract. The case of *Schoolman v. Hall* (1951) in the Court of Appeal has formulated the strong nature of duty of disclosure in the burden of the assured.

The facts

The assured, Mr. Schoolman, a jewellery trader took an insurance cover from the underwriter, Mr. Hall who was one of the subscribers to a jewellers' block policy issued to the assured. The policy was issued after the assured completed the proposal form provided by the insurer, by which the assured should answer a number of questions. It was agreed that this form shall be the basis of the contract of insurance.

In December 1948, the assured's shop was burgled and the jewellery, valued at 19,976,9 poundsterlings stolen. He then claimed to the insurer under the policy, but the insurer contended that the policy was void because the assured had not disclosed his criminal record which occurred 15 years ago to the insurer.

Held by the Court of Appeal that, based on the support of the jury who stipulated that the non-disclosure of such criminal record was material, so that the insurer may avoid the contract with the legal reason; although in the proposal form, the assured was only required to answer certain questions, those questions related to business matters and did not relieve the assured of his general common law obligation to disclose any further material facts which might affect the insurer's mind in accepting the risk. At the same time, the completion of form has no meaning that the insurer has waived the material information further in the context of concluding the contract.

That decision had the basis from the case of *Glicksman v. Lancashire and General Assurance Company, Ltd*, (1927) by which the Cohen has referred to the legal reason of the judgement of the Lord Dunedin who said that a contract of insurance is denominated a contract *uberrimae fidei*. It is possible for the person to stipulate that answers to certain questions shall be the basis of the insurance, and if that is done then there is no question as to materiality left, because the persons have contracted that there should be materiality in those questions; but quite apart from that, and alongside of that, there is duty of no

concealment of any consideration which would affect the mind of the ordinary prudent man in accepting the risk.

Therefore, applying those observations here, while the insurers have stipulated that the answer to the fifteen questions “shall be the basis of the contract”, that only has the effect of preventing any argument as to the materiality of those questions should dispute arise. And the as mentioned above, it does not relieve the assured of his general common law obligation to disclose any further material facts which might affect the insurer’s mind as to whether or not he should issue a policy. At the same time, Cohen stated that it is quite impossible to spell out of the form of the proposal that any agreement by the insurers exist in order to waive their rights to the general information which the nature of the contract required.

The decision of Schoolman’s case in the context of duty to disclose above was followed clearly by the Justice McNair in the case of *Roselodge.Ltd.(Formerly “Rose” Diamond Products, Ltd) v. Castle* (1966) . In that case, when the plaintiff (the assured), a diamond merchants insured their diamonds against all risks with the defendant (the insurer) and after completing the proposal form in which no question was asked as to previous convictions of employees. Plaintiff claimed under the policy as a result of R, his principal director, had been robbed of diamonds worth 304,590,3 poundsterlings on Jan 31, 1965, by which the claim to the defendants only to pay amount to 73 poundsterlings of the total amounts insured.

The insurers repudiated the liability based on the ground of the plaintiff’s failure to disclose that (1) R, the principal director, had been convicted of bribing a police officer in 1946 and was fined 75 poundsterlings; (2) M, plaintiff’s sales manager, had been convicted of smuggling diamonds to the US in 1956, and had been engaged with plaintiff a year after his release from prison. The plaintiff contended that the facts were not material and his obligation to disclose was released by the completion of form’s question provided by the insurer.

Held by the Justice McNair, *inter alia*, that (1) that the issue of disclosure was to be determined by the view of reasonable man; (2) that R's offence and conviction were not material facts and need not have been disclosed; (3) that M's offence and conviction were material facts which should have been disclosed ; (4) that there was no waiver as between plaintiff and insurer could be inferred and accordingly, the plaintiff claim failed.

III.6.1. Should Material Rumours be Disclosed ?

Under the regime of English marine insurance law, the notion of material information that must be disclosed by the assured as well the broker reaches the legal concept of the material rumours. The recognition of material rumours had been justified based on the judgement of *Elena* case (2001) which stipulated that the assured must disclose every material fact to the risk to be insured including any rumours or reports of which the insured is aware, so long as the rumours or reports are not "mere speculations, vague rumours or unreasoned fears". Before the judgment of *Elena* case, the legal regime of material rumours had been used to settle the case of *Inversiones Manria S.A. v. Sphere Drake Insurance Co.Plc., Malvern Insurance Co.Ltd., and Niagara Fire Insurance Co.Inc.*, (1989). In that case, the assured committed to non-disclosure act by ignoring the allegations that the smuggling conducts had been made against members of the crew of the insured vessel. And then such allegations were proved in fact well-founded, but remarked. The legal reasons of the Phillips, J's judgement in the case was the judgement of an underwriter to placing the risk, not only influenced by the mere facts that can be shown actually to have affected the risk, but also with the facts that raise doubts as to risk. In other words, from both cases, the assured must be much aware of the sense of any material rumours or reports within his knowledge, actual or constructive. Accordingly, the burden of the assured is much higher with uncertain legal guidance to protect from the legal concept of material rumours disclosure. So any mistake made in respect of that issue would give the assured the risk without cover, owing to the draconian remedy of avoiding the contract by the insurer.

Therefore, the life of an assured would be more complicated in the context of duty to disclose the material rumours if the legal formulation made by the Lord Mansfield, C.J in

his judgement from the case of *Lynch and Jones v. Hamilton* (1810) might be applied in any material rumours case. By which he stated that the non-disclosure of report as to the insured vessel as having been seen “leaky and deeply laden”, ought to have been disclosed, although as it turned out, it had been false. It means that it will make no difference whether the rumours or report is true, accurate or false, as long as such rumours will raise doubts as to the risk insured, This will be enough to stipulate the obligation of disclosing such rumours to the insurer.

However, the “endless” burden of the assured in the context of duty to disclose was relieved from the judgement of Colman, J in the quite recent case of the *Gracia Express* (2002). This case had brought back the balance condition of mutual duty to disclose between the insurer and the assured, in which it seemingly had existed unbalance or unfair in the scope of material rumours disclosure.

In that case, the assured took war risk insurance from the insurer for his ship. When the assured claimed for his disappeared ship, the insurer claimed back to avoid the policy based on the ground that the assured had failed to disclose the facts about some years ago a yacht owned by him had disappeared suspiciously upon which the allegation of it might have been cast away existed. The insurer argued that the previous disappeared ship owned by the assured was material to be disclosed, as the allegation of dishonesty contained within them was relevant to moral hazard.

It was held by Colman, J that since the assured had proved that the allegation of dishonesty contained within the facts of previous disappearance to the assured’s ship was untrue, so that the insurer was precluded from the remedy of avoidance the contract based on the basis of non-disclosure (rumours).

The legal reasoning of the Colman, J’s judgement in that case as follows :

Utilizing loss of the opportunity of forming an unfounded suspicion of non-existent facts in order to avoid paying a loss under policy which, had the truth been made known to them when they wrote the risk, they would not have hesitated to

underwrite. To persist in such a course in the face of evidence before the Court that the suggested facts never existed would, in my judgement, be quite contrary to their duty of the utmost good faith. Such a course would be so starkly unjust that I would hold that in such a case it would be unconscionable for the Court to permit the insurers to avoid the policy on the ground of non-disclosure.

Although the decision of this case was contrary to the precedent and created a great deal of criticism on it, Colman, J's judgement is legitimate and reasonable legal basis by stating that it is truly true, a prudent insurer would not take account of a matter which could not possibly be true when forming his judgment upon the acceptance of insurance contract.

III.6.2. Duty of Disclosure Test

According to the Justice MacKenna from his judgement in the case of *Lambert v. Co-operative Insurance Society, Ltd.* (1975) described the formulation of the four test of duty to disclosure : first, the duty is to disclose such facts only as the particular assured believes to be material; secondly, it is to disclose such facts as a reasonable man would believe to be material; thirdly, it is to disclose such facts as the particular insurer would regard as material; fourthly, it is to disclose such facts as a reasonable or prudent insurer might have treated as material.

The first test of duty to disclose had been rejected by the decision of the Lord Blackburn in the case of *Brownlie v. Campbell* (1820) by stipulating that there is an obligation there to disclose what you know, and the concealment of a material circumstance known to you whether you thought it material or not, avoids the policy.

III.6.3. Reasonable Man or Reasonable Insurer Test ?

The legal concept of the reasonable man, the second test, mentioned in the decision as mentioned by the Justice McNair in the Roselodge's case was formulated based on the judgment of the Lord Justice Fletcher Moulton in the case of *Joel v. Law Union and Crown Insurance Company* (1908) who stated that if reasonable person would know that underwriters would naturally be influenced, in deciding whether to accept the risk and what premiums to charge, by those circumstance, the fact that they were kept in

ignorance of them and indeed, were misled, is fatal to the assured's claim. Later, he added that the obligation to disclose, therefore, necessarily depends on the knowledge you possess. Your opinion of the materiality of that knowledge is of no moment. If a reasonable man would have recognized that it was material to disclose the knowledge in question, it is no excuse that you did not recognize it to be so.

However if the fact, though material, is one which he did not and could not have been expected to know in the particular circumstances, or if its materiality would not have been apparent to a reasonable man, his failure to disclose it is not a breach of duty. For example, if the ordinary man would not infer a serious malady from a headache, knowledge of malady can not be proved.

In other words, he agreed that it was not enough for the applicant to tell the insured what he thought was material. There is further duty that he should do it to the extent that a reasonable man would have done it. The disclosure must be of all you ought to have realized to be material, not of that only which you did in fact realize to be so.

In the case of *Becker v. Marshall* (1922), the regime of second test in the duty of disclosure was affirmed definitely by the Justice Salter who said that a policy against burglary was avoided, because of the assured's failure to disclose three matters : previous burglary, his foreign origin, and a change of his name, which under the perspective of average reasonable man would have disclosed and would have known that it was necessary to disclose. When this case appealed in the Court of Appeal, Lord Sterndale confirmed that he will accept for the purposes of the judgement that material should be interpreted in the view of a reasonable man.

Nevertheless, the test of reasonable man was not purely used under the Moulton's test in the Joel's case, if examining carefully his judgement, the notion of fourth test existed. It can be seen from the statement of him who stated that :

“...if an ordinary person taking reasonable care and using reasonable judgement, would not know all the facts, if for example, he would not know that a particular

symptom indicated the presence of a serious malady, he is under no duty to state that he had the symptom, because all the material facts would not be within his knowledge. But they were within his knowledge, or if they would be within the knowledge of an ordinary reasonable person, then...he must disclose them if they would naturally influence a reasonable underwriter”.

The words of “...he must disclose them if they would naturally influence a reasonable underwriter” fall under the fourth test of duty to disclose. This test has been developed by the Justice Blackburn, in the case of *Ionides and Another v. Pender* (1872) said that all should be disclosed which would affect the judgement of a rational underwriter governing himself by the principles and calculations on which underwriters do in practice act.

The concept of reasonable insurer test has also played very significant role in the case of *Mutual Life Insurance Co. of New York v. Ontario Metal Products Co. Ltd* (1925), a Canadian case, in which the Privy Council stipulated that it is a question of fact in each case whether if the matters concealed or misrepresented had been truly disclosed they would, on a fair consideration of the evidence, have influenced a reasonable insurer to decline the risk or to have stipulated for a higher premium.

In addition, the judgement of the Justice Megaw in the case of *Anglo-African Merchants Ltd. and Another v. Bayley and Others* (1969) clarifies the existence of both second and fourth test which were applied in the English marine insurance law relating to the case of duty of disclosure. In that case, the Justice Megaw stated that :

If, however, the assured knew of facts, and if as a reasonable man he should have realised that knowledge of those facts might be, regarded as material by a normal prudent underwriter, then if those facts are not disclosed and if they would have been material, the defence of non-disclosure prevails.

Nevertheless, the application of the fourth test of duty to disclose, which is similar to section 18 (2) of MIA 1906, later has gained largely strong supports when it comes to the concept of materiality test and inducement.

III.6.4. Test of Materiality and Inducement

The notion of duty to disclose the material information falls under the basis of judgement both the test of reasonable man and the reasonable or prudent insurer as mentioned clearly above. However, in the subsequent condition, the test of prudent insurer was chosen mainly to be applied, particularly when we discuss about the limit of materiality of any information informed in the making of insurance contract. The prudent insurer test, in the context of marine insurance specifically, has been derived from section 18 (2) of the MIA 1906 which stipulated that information is material if it would influence the judgement of a prudent insurer in fixing the premium, or determining whether he will take the risk.

Thomas (1996) stated that, under the context of English marine insurance law, the test of materiality is an objective one. It means that the basis of judgement for materiality test is the reaction of the hypothetical prudent insurer, not that of the actual insurer which is of relevance. Accordingly, the assured is protected from the potential subjective capriciousness and idiosyncrasies of the actual underwriter, whose professional ways may be uncertain, variable, and impossible to predict. The reaction of a prudent insurer should be measured on a case by case basis by the expert evidence provided by expert witness in the relevant insurance market. The negative meaning of those proposition is the first test of duty to disclose as mentioned above, is inapplicable.

The supporting case for the materiality test from the prudent insurer perspective can be seen from the case of *Container Transport International Inc. (CTI) and Reliance Group Inc. v. Oceanus Mutual Underwriting Association (Bermuda) Ltd.* (1982). In that case, the plaintiff, CTI, placed the insurance cover for container damage with C.E. Heath and Co represented by the Mr. Fleetwood and other syndicates at Lloyd's underwriters commencing on June 1, 1975. Before placing insurance cover with those underwriters, CTI had placed its insurance with the Crum & Foster; it was over as matters of disagreement about the terms upon which the CTI found unacceptable.

With some reasons, the underwriters at Lloyd's would not renew beyond Dec 1, 1976 and in due course the insurance was placed with the defendants Oceanus. It was common ground that Oceanus were shown the Lloyd's experience for the year June, 1975 to May, 1976, plus the month of June 1976 prepared by the plaintiff's broker including a telex dated September 10, 1976 described the Lloyd's experience from years to June 1, 1976, together with the losses which would have incurred. On December 1, 1976, the Oceanus came on risk.

On December 2, 1977 Oceanus declined to pay any further claims by the assured and pending investigation. The plaintiff CTI demanded payments of their claims for August to October 1977 and issued their writ on March 1, 1978. Fifteen days after, Oceanus wrote avoiding the policy of the assured based on the ground of misrepresentation and non-disclosure contending that : (1) CTI had put forward an inaccurate or incomplete and misleading claims record; (2) that they had failed to disclose a refusal by underwriters to renew. Then by further amendment it was alleged that the assured had failed to make full disclosure when obtaining insurance at Lloyd's for the period of June 1975 to November 1976 and the Lloyd's policy was avoidable.

It was held by the Justice Lloyd, inter alia, that :

1. For the issue (2) about the refusal to renew, said that the submission by Oceanus that the non-disclosure of the Crum & Forster figures for the previous years was a material factor would be rejected in that the evidence was insufficient to support an allegation of non-disclosure; even if it had been material, on the facts, Oceanus had waived information as to that experience by making clear to Mr. Fleetwood their decision to work on the telex of September 10, 1976.
2. For the issue (1), the submission of incomplete figure was rejected since Oceanus could have seen the claims figures for the months June, 1975 to May 1976 from the documents they had in their possession when the risk was placed. Premium figures that Oceanus did not have were not a matter in the perspective of the court.
3. The submission that CTI ought to have disclose to Oceanus that they had failed to make full disclosure to Lloyd's would also be rejected based on the facts that neither

CTI nor Mr. Fleetwood were guilty of any non-disclosure at any stage and the Lloyd's insurance was never voidable on that or any other ground.

In other words, from the other statement made by the Justice Lloyd in the same case, who states the insurer would not be succeed to proceed a defence of non-disclosure if the insurer could not satisfy the court by evidence or otherwise that a prudent insurer if he had known the facts in question would have declined the risk altogether or charged higher premium.

From the Lloyd's statements above, there is clear meaning that the nature of materiality test in the context of non-disclosure has recognized the existence of inducement. Or it can be said that any material non-disclosure should be proved to induce the prudent insurer in his judgement to place the risk in order to make the insurer gaining the benefit of avoidance remedy under section 18 of MIA 1906. However, the test of inducement shown by the "influence" of section 18, is formulated as a non-decisive one. It does not have a meaning that the inducement makes as to his final state of mind of the judgement of the prudent underwriter as so expressed in the decision of placing the risk.

It seems fair for the assured as a shield of protection from the strong weapon of defence owned by the insurer in the section 18, that the word "influence" was "non-decisive influence". The legal formulation of the non-decisive influence test and the causal connection between non-disclosure and the making of the contract of marine insurance has gained very strong support from the decision of further case of *Pan Atlantic Insurance Co. Ltd. and Another v. Pine Top Insurance Co. Ltd.*(1993). This case was quite special based on the reason of this a kind of reinsurance contract dispute, and its nature of case was much similar to the case of CTI above. In his judgement in the Court of Appeal for that case, Steyn, L.J., in no doubt adopted the legal formulation made in the case of CTI by establishing the judgement based on the ground that the avoidance for non-disclosure is the remedy provided by law because the risk presented is different from the true risk. In the words of Lord Mansfield in the case of *Carter v. Boehm* (1766) 3

Burr. 1905 described the effect of non-disclosure as to induce him to estimate the risk as if it did not exist.

The basis of reason chosen by the Steyn, L.J. differed from the legal concept which explained that a fact is material if a prudent insurer would have wished to be aware of it in reaching his decision. The previous test which is similar to the Lord Mansfield's formula would make the insurer more difficult to prove the existence of increased risk in the presence of material non-disclosure. Such test also would protect the assured as well as the broker from disclosing the endless material information about the assured's past.

The Court of Appeal's judgement in the case of Pan Atlantic was upheld by the House of Lords through the concise judgement of Lord Mustill that "if the... non-disclosure of a material fact did not in fact induce the making of the contract (in the sense in which the expression is used in the general law of misrepresentation), the underwriter is not entitled to rely on it as a ground for avoiding the contract".(Thomas, 1996).

In addition, in the issue of non-decisive influence, the Lord Mustill also stated that it has the meaning of the "right to know" test. The notion of fairness in this formulation is it would make the less burden of the assured to perform the duty of disclosure and at the same time, it restricts the right of the insurer to avoid the contract under the section 18 of MIA 1906.

III.7. Misrepresentation

Unlike the law of misrepresentation in the context of general contract law, which gives the injured party the range of remedies based on the nature of the misrepresentation itself, the law of misrepresentation under the regime of English marine insurance law, particularly section 20 of MIA 1906, gives only draconian remedy if the assured as well the broker breach any material representation to the insurer before the contract is concluded or during the period of negotiation. It makes no difference whether such breach of material representation is innocent, negligent or fraudulent, the remedy to avoid

the contract *ab initio* will prevail. The legal basis for the claim to avoid contract is the proof of representation made by the assured or broker was untrue.

Practically, the notion of misrepresentation is precisely difficult to differentiate with the non-disclosure. Both relatively resembles. Conceptually speaking, the fundamental distinction between them is for a duty to disclose is an obligation to merely disclose material information, and representation means that an obligation to ensure that any information volunteered is truthful and accurate. Therefore, it is not surprise when recognizing the legal concept under the English law if the fact of one conducts a partial non-disclosure might be categorized as a misrepresentation.

Accordingly, the issue of materiality in the sense of representation will be treated similar to the duty of disclosure, upon which the representation is material if it would influence the judgement of a prudent insurer in fixing the premium, or determining whether he will take the risk. It has legal impact similarly to the treatment in the duty to disclose, by which the test of materiality has to be measured under the basis of a prudent insurer by questioning the existence of the material misrepresentation whether having induced the insurer to place the risk or not. This test is an objective approach as mentioned in the sub section of duty of disclosure above.

The case of *Pan Atlantic*, again, had become very good example for the legal formulation above, through the decision made by the House of Lords which stated that no remedy of avoidance of a contract for the insurer unless he could prove that such material misrepresentation induced the prudent insurer in respect of the making of the contract.

However, the inducement theory will not be practicable legally to pinpoint the remedy of avoidance if the insurer waive the inducement as mentioned in the general concept of contract law. So, in order to make it practicable legally in the context of misrepresentation, one should show that the representee relies on the misrepresentation made by the representor. In other words, if there is no reliance on the fact of a material misrepresentation, the insurer could not avoid the contract. That circumstance has its

legal basis on the judgement of Lord Mustill in the same case, Pan Atlantic, by saying that to enable an underwriter to escape liability when he has suffered no harm, would be positively unjust and contrary to the spirit of mutual good faith recognised by section 17 of MIA 1906. Whether a particular representation be material or not is in each case, a question of fact.

In addition, under the English marine insurance law, a representation is either a representation as to matter of fact, or as to a matter of expectation or belief. Therefore, a representation as to a matter of fact is true, if it be substantially correct, that is to say, if the difference between what is represented and what is actually correct would not be considered material by a prudent insurer.

For the issue of representation of expectation or belief, those are true if it is made in good faith. However, from the author's point of view, the statement above need to be clarified as to whether the mere good faith duty will prevail in the scope of representation of the expectation or belief, or in the notion of duty of care under the regime of general tort law. In tort law, a representation of expectation or belief shall be measured based upon the ground of negligent acts by which such negligent acts was conducted by the person who has a skill and or special knowledge in respect of making a representation of expectation or belief.

Unlike the nature of non-disclosure, a misrepresentation may be withdrawn or corrected before the contract is concluded.

III.8. Broker's Role

In the context of marine insurance transaction, the insurance broker plays a very significant role. It is very rare to place marine insurance risk without the role of the marine insurance broker. Considering that nature, section 19 of the Marine Insurance Act 1906 stipulated that, subject to other section stipulated in the large section of utmost good faith duty in the marine insurance law, where an insurance is effected for the assured by an agent, the agent must disclose to the insurer :

1. 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;
2. every material circumstance which the assured is bound to disclose, unless it come to his knowledge too late to communicate it to the agent.

The word “agent” as mentioned above implies a different meaning with the term “broker”. It seems difficult to differentiate, but broker is a kind of agent in the context of agency law. The word “broker” has the specific meaning to show an agent is employed primarily to negotiate contract between two parties (Beatson, 2002). In addition, it is simply defined as to show the general term of fiduciary relationship between the principal and agent upon which the agent should acts on behalf of the name and the interest of a principal. Relating to the difference, Parks (1988) states that when talking about marine insurance, brokers mean a person is commonly employed by the assured who seeking insurance.

Nevertheless, the term “agent” also resembles the meaning of Parks’ definition in the context of the opinion of the Lord Harlsbury in the case of *Blackburn v. Vigors* (1887) by saying that “some agents, so far represent the principal the principal that in all respects their acts and intentions and their knowledge may truly be said to be the acts and intentions and knowledge of the principal”.

Section 19 stipulates clearly the meaning of agent in it as a person who is employed by the assured in order seek an insurance cover. In the words of Merkin (1996) who said that an insurance broker is an independent intermediary who owes parallel duties of care in contract and tort to his client, the assured, and that broker’s duty is owed to the assured and not to the insurer or any third party. However, in the practice of marine insurance business, the pure meaning of an agent is to serve the interests of the assured only, did not exist any longer. As affirmed by the Ratnayeke (1992) that due to the present commercial requirements the broker seems to be acting as agent of the insurer as well as the assured with regard to the different of the agreement in a marine insurance contract.

Therefore, up to what extent the broker's responsibility to both assured and insurer is a question fact.

In addition, there are other three common types of condition in an agency relationship in the context of marine insurance, explained by the Merkin (1996) as follows : (1) the underwriting agent, an independent company appointed by one or more insurers to receive proposal from the brokers and to take underwriting decisions on behalf of the insurers; (2) the Lloyd's line slip, by means of this device, an underwriter may be given authority by other underwriters to accept the risk on their behalves as well as on his behalf. So that a broker who procures the signature of the leading underwriter will automatically obtain a substantial proportion of the total subscription required; (3) the broker acting under a binding authority or "binder". A binder means a contract between an insurer and a broker delegating certain underwriting power through conferring a right to accept risks of a given description and under given financial limit.

III.8.1. Broker's Role and Utmost Good Faith Duty

One significant role of an insurance broker is to negotiate the proposed cover with the insurer in the pre-contractual stage. In this context, the insurance broker should disclose actual knowledge as well his constructive knowledge which is known by the broker, and also any material information that the assured is bound to disclose. The notion of duty to disclose and representation owed by the broker is precisely similar to the assured. No prohibition is imposed to the insurer for claiming to avoid the contract as a result of the broker breach of the duty of utmost good faith. Furthermore, the insurance broker may be liable to damages to the insurer if the broker failed to disclose every material circumstance as mentioned in section 19 of MIA 1906. It was clarified from the case of *Wolcott v. Excess Insurance* (1978) in which it was held that the broker was liable to indemnify the defendant insurer with regard to the money that had to be given to the plaintiff assured as a result of failing to convey information to the insurer, who was his principal.

Accordingly, in the pure sense when broker is an agent of the assured only or to the insurer, situation seems simpler to determine to whom broker is responsible. The situation becomes more complicated when a broker is responsible in different nature for both the assured and the insurer. As described in the context of binder circumstances when the broker is the agent of the insurer in operating the binder but he is also the agent of the assured whose risks he declared to the binder. This nature of binder will be divided into two categories : first, obligatory binder when a broker, on accepting a risk, makes an appropriate declaration to the insurer, confirming that the risk has been allocated to the binder; secondly, non-obligatory binder when a broker does not confer on the final power to accept risks but merely to receive them and to seek confirmation of acceptance by the insurer.

Therefore, for the question of the first category, whether the broker owes duty of care to the insurer in making declaration under the obligatory binder was answered by the judgement of Kennedy, J in the case of *Empress Assurance Corporation Ltd v. Bowring & Co.Ltd* (1905). In that case the broker had in good faith made reinsurance declarations which contained false information regarding the premium paid to the reassured. The insurer then claimed for breach of good faith duty. It was held by him that there was no duty of care to the reinsurer, although the broker had administered the binder on behalf of the reinsurer. The broker remained the agent of the reassured. It was also held that by appointing as his agent a broker who owes the primary duties to the assured, the insurer must be taken to have waived any cause of action against the broker for furthering the interest of the assured. The notion of waiver taken by the insurer in this circumstance also would apply to the situation when the assured made full disclosure to broker, but broker did not communicate to the insurer. Kennedy believed that in the absence of fraudulent acts, the response of insurer as to that situation is either waived disclosure or was deemed to receive the information, The legal formulation established by the *Empress* case, has been followed in the judgement of the *White v. Jones* case (1995), which permitted the intermediary agent, such as the insurance broker, to undertake contractual responsibilities to A and tortious responsibilities to B, with a condition that no conflict of interest existed.

However, under non-obligatory binder, the case of *Berger and Light Diffusers Pty. Ltd v. Pollock* (1973) stipulated that in respect of making a declaration, if the assured has failed to disclose all material facts to the broker, the insurer clearly has the right to avoid that particular declaration.

The situation of the assured-broker relationship seems to be unfortunate to the assured's interest when it comes to the context of the broker's liability to the assured. It was derived from the non-recognition of the English court to justify the liability on the broker for breach of his contractual duty by not to observe the utmost good faith to the insurer. The court rejected to the liability on the broker when he failed to inform the assured of the latter's duty of disclosure. The legal reason for that was if it was accepted, it would amount to requiring brokers to advise their client's on the law, unless the factual situation demands that a broker informs his client as to the broad requirements of insurance (Ratnayeke, 1992).

III.8.2. Knowledge of the Broker

It was identified by Ratnayeke (1992) that in the context of an agency relating to non-disclosure, most problems arise where the agent's knowledge is imputed to the principal. This issue of imputation of the agent's knowledge to the principal is mainly related to the application of section 18 (1) upon which the assured is bound to disclose any material facts which is ought to be known by him in the ordinary course of business.

The necessity of that issue of the imputation has gained the justification from the courts through the several key rules below :

1. Where a loss must fall on one of two innocent parties through the fraud or negligence of a third party it must be borne by the party who employed and trusted the third person.
2. The ability of the principal to misuse the knowledge of the agent to his advantage.

3. The assumption of the insurer when entering into the agreement that all material facts connected with the property insured, known to the agent employed for that purpose, have been by him communicated to his principal.

The rules of imputation above has the objective to maintain the application of utmost good faith which is not reduced by the implementation of the agency law to the marine insurance law.

Relating to the issue of imputation as mentioned in section 19, the judgement of the Lord Macnagthen in the case of *Blackburn v. Vigors* (1886) which stated that the agent did not carry out the transaction and the facts that he had previously been employed did not impute the knowledge to the principal for all purposes. In other words, as long as the agent is not a person to whom the assured needs to effect the insurance policy, the knowledge of the agent is not imputed to the principal (the assured). This judgement had been affirmed by the settlement of the case of *PCW Syndicates v. PCW Reinsurers* (1996) upon which the Waller J decided that the claim of the reinsurers to repudiate the contract was rejected because the knowledge of PCW Syndicates as to their dishonesty was not held in their capacity as agent (effecting insurance) for the insurers, PCW was an underwriting agents/intermediary agents, and therefore there was no obligation to disclose such dishonest conduct.

Nevertheless, Waller J added that the insurance contract would be vitiated by concealment on the part of the agent just as it would be by concealment on the part of the principal. But that is not because the knowledge of the agent is to be imputed to principal, but because the agent of the assured is bound as principal is bound to communicate to the underwriters, all material facts within his knowledge.

Therefore, the situation in respect of imputation issue and concealment which lead to the dishonesty of the agent seems more challenging when questioning whether the obligation to disclose on an agent instructed to effect insurance, would have applied to the facts that revealed a fraud by the agent on his principal. The answer is no liability would be

attached to the assured. That answer was supported by the judgement of the Devlin J in the case of *Kwei Tek Chao v. British Traders and Shippers Ltd.* (1954). In that case, in which his agent did fraudulent misrepresentation, he stated that :

A principal is thus liable for a false misrepresentation made fraudulently if the agent is acting within the scope of his authority actual or apparent, but if the chain is innocent principal, dishonesty agent, innocent agent and if dishonesty is directed at principal, then since knowledge can not attributed to the principal, the principal is not liable for fraudulent misstatement.

The next critical issue of knowledge of the assured in the English marine insurance law is about the non-disclosure of the employee working in the broker firm. In the beginning, the legal formulation for that issue was quite restricted through the judgement in the case of *Stewart v. Dunlop* (Ratnayeke, 1992) which stated as follows :

It is certainly the duty of a clerk to disclose to his employer whatever information he receives in regard to the latter's business and it is submitted that the employer is responsible for not disclosing a fact which was within the knowledge of his clerk.

It seems that no matter what the particular relationship and its nature take place, the broker should be liable for such non-disclosure. This judgement would cause some difficulties for the big insurance broker who has a complicated structure of organisation with many lines of duty and authority. However, in the twentieth century, the legal formulation was revised by the judgement of *Mahli v. Abbey Life Assurance Co.Ltd* (Merkin, 1996). In that case, there was material facts in respect of the assured possessed by the underwriting department of the defendant insurer following its rejection of a proposal. Such facts failed to be submitted to the general administration of the insurer. Accordingly, the insurer keeps collecting premiums on earlier policy which could precisely be deemed to have been procured by misrepresentation and non-disclosure. It was held by the Court of Appeal that the facts known to the underwriting department could not be imputed to the rest of the company. Therefore, the premium collections by the insurer did not mean to the waiver of the assured's breach of duty. In other words, an

imputed interchange information between the various department of the broking organisation is not recognised legally.

In addition, the law of insurance under English jurisdiction seems quite fair not to impose very strict to the context of non-disclosure related to the involvement of agent when effecting insurance, as stipulated in the case of *Roberts V. Plaisted* (1989). In that case, the circumstances existed when the broker had visited the subject matter of insurance cover and after making a judgement on it he filled out the proposal form by himself. In which then, the assured had to responsible for non-disclosure of a circumstance which was alleged to be material by the insurer. The court rejected that claim and found the judgement in favour of the assured.

III.9. Utmost Good Faith Duty to the Third Party

In the context of the duty of insurer to observe the utmost good faith towards the third party's interest of insurance cover under the assignment scheme, the English court took a position not to recognize it. This position had been derived from the judgement of *the Bank of Nova Scotia v. Hellenic Mutual War Risks Association (Bermuda) Ltd (The Good Luck)* case in 1989. In that case, a plaintiff bank was a mortgagee of the ship owned by the shipowner as the mortgagor. The mortgagee's interest had been insured by the owner, and the assigned it to the plaintiff bank. When the ship was struck by missile while in the prohibited area, upon which the special arrangement had to be made, but the defendants (insurer) refused to compensate the loss with the reason that conditions of the agreement had been violated by the owner, assignor of the cover. As a result of that refusal, plaintiff bank claimed compensation to the defendants. Plaintiff had reasoned that based on the assignment of the beneficial interest, the defendant owed of the utmost good faith duty to the plaintiff, that they were in breach of it. The breach of utmost good faith duty arguments was rejected by the Justice Hobhouse by stating that the assignee of the benefits of such an insurance contract does not owe any duty of the utmost good faith to the insurer nor on the basis of mutuality is there. The insurer's duty of the utmost good faith was only to the shipowner.

Therefore, for the mortgagee, that judgement would make him to be very careful in near future when deals with the cover of the mortgagee's interest. A safeguard clause specifically has to be included to protect his interests properly.

CHAPTER IV LEGAL CRITICISM ON THE UTMOST GOOD FAITH PRINCIPLE

IV.1. Uncertainty of the Prudent Insurer Test

Knowledge of the assured as well the broker is the basis to activate the duty to disclose upon which the breach of it can be claimed as non-disclosure of material information. The English marine insurance law imposes high standard to the issue of the knowledge by stipulating that knowledge covers actual and constructive knowledge. In other words, there will be a presumption of knowledge which must be known by the assured under the limit of ordinary course of his business. When it relates to the test of materiality, by which the prudent insurer approach will prevail, also known as the objective approach, its legal formulation in fact would result in greater difficulty in assessing the standard of constructive knowledge by which to judge the information which ought to be disclosed to the insurer and would result in a greater degree of uncertainty.

Such difficult and uncertain circumstance caused by the benchmark of a “prudent insurer” is relatively easy to fix as compared with the complexities arising out of the “prudent assured” approach who could vary as widely as possible from the small exporter or importer to the giant ship owning company and shippers. That makes the marine insurance industry continuing to be troubled by the concept of the “prudent insurer”.(Derrington, 1998).

Therefore, in the context of effecting insurance cover by the person who does not have special knowledge relating to the subject-matters, such as occurred in the case of *HIH Casualty and General Insurance Ltd and Others v. Chase Manhattan Bank and Others* (2001) where the assured, banking firms, have less special knowledge to the subject-matters of financing the film productions. The regime of a prudent insurer to be disclosed actual knowledge as well as constructive knowledge tends to create a weaker legal protection in the hand of the assured. It is more complicated if relating this issue with the application of active duty of disclosure to the English marine insurance law, upon which the duty to assess what information is material for the insurer rests with the person

effecting the insurance, as mentioned in the Lambert and Schoolman cases. In other words, the burden to disclose does not stop when all material questions in the proposed form have been answered correctly by the person effecting insurance.

In addition, it is very unclear how to precisely interpret the legal concept of the “prudent insurer”. Diamond (1996) stated that if we go to the Lloyd’s Office and asking some questions relating to the placing the risks, one would find in not so difficult way that there are only few prudent insurers, even if it is possible for us to show that some insurers are not prudent ones at all. From the business point of view, it is not uncommon when some underwriters have an occasion to write “loss leaders” knowing that the business will be unprofitable and in the hope of getting an entree into a particular line of business in the future.

A prudent insurer test also faces difficulty to define the scope of information that need not to be disclosed to an underwriter, owing to the variety of expertise among the underwriters themselves. For example, fertilizers which have tendency to “cake” on exposure and moisture, a relevant factor in the level of risk involved in its carriage of goods. Such fact could be understood firmly by the insurer who is a specialist in those matters, but perhaps not to the other underwriters which has not.

The prudent test in the context of utmost good faith had been revised by another common law system, Australia marine insurance law. It was stipulated by the Insurance Contract Act 1984 with formulating legal rule with regard to the duty of disclosure as follows :

Section 21 (1) Subject to this Act, an insured has a duty to disclose to the insurer, before the relevant contract of insurance is entered into, every matter that is known to the insured, being a matter that : (a) the insured knows to be a matter relevant to the decision of the insurer whether to accept the risk and, if so, on what terms; or (b) a reasonable person in the circumstances could be expected to know to be a matter so relevant.

Section 26 (2) A statement that was made by a person in connection with a proposed contract of insurance shall not be taken to be a misrepresentation unless the person who made the statement knew, or a reasonable person in the

circumstances could be expected to have known, that the statement would have been relevant to the decision of the insurer whether to accept the risk and, if so, on what terms.

As stated in the rules above, the Australian marine insurance law has taken an approach of the reasonable assured by stipulating that the test of materiality would be measured based on the reasonable person test, instead of the prudent insurer. In addition, section 21 (3) of the Insurance Contract Act also states that where a person has failed to answer or given an obviously incomplete or irrelevant answer to a question included in a proposal form, the insurer is deemed to have waived compliance with the duty of disclosure in relation to the matter.

Furthermore, section 21 (3) was felt too generous for the insurer's benefit, upon which it placed too onerous burden on an assured to assess what matters are relevant to decision of the insurer when accepting the risks. Therefore, through *Insurance Laws Amendment Act 1998* which came into effect on 1 September 1999, section 21 (3) has been replaced by a new section 21 A, which demands an insurer to pose specific questions to an assured that are relevant to the risk and to request expressly that the insured disclose each "exceptional circumstances", which is known to the insured, and which the insured knows. Where the insured properly answers these questions the insured is deemed to have complied with the duty of disclosure.

IV.2. Legal Problems of the Actual Inducement

The notion of presumption of the inducement in the scope of non-disclosure that should be showed by the judgement of the Pan Atlantic is not free from the legal problems which are necessary to be clarified. As to the problem of doubt regarding which party bears the burden of proof in regard to the inducement. For the assured, it is very difficult to produce evidence in order to prove that the insurer was not actually induced into making the contract. In the issue of evidentiary problem, as stated by the Justice Byrne from the Australian marine insurance case, *Akedian* (1997) by which he referred to the difficulty of the court evaluating the evidence of insurers that they were induced.

Whether one calls it a presumption of fact or a matter of inference, there is a very short step between conclusion that the mind of a prudent underwriter would be affected by a matter and the further conclusion that this underwriter before the was so induced. This more difficult in the case of non-disclosure because the question can not be that these insurers were induced to issue the policy in question by something they were ignorant; it must be that they would not have issued the policy if they had been aware of the non-disclosed fact.

The legal formulation made by the Justice Byrne above, seems to be similar to the statement of the Lord Mustill in the case of *Pan Atlantic* who said that referring to a presumption of inducement, which would go against the general law of inducement upon which ruled that no inducement existed when the induced party was waived that inducement with regard of the subject-matters insured.

Furthermore, the practice of marine insurance is mostly conducted under the principle of spreading risk. That principle will be realized in the form of signing a slip provided by the assured or his broker. Meaning that in one insurance cover held by the assured, the insurer who agreed to indemnify the risk is more than 2 insurers, not uncommon if that insurers reach more than ten insurers. So then the issue of inducement in the context of non-disclosure particularly, has no effect if not, less effect of inducement to the non-leading underwriters as a result of non-leading underwriters will merely refer to the judgement of risk made by the leading underwriter. Accordingly, the nature of fairness will not be maintained if non-leading underwriters are given the right to avoid the contract based on the ground of actual inducement not made to them.

IV.3. Unfairness of A Single Remedy ?

The uncertainty of a prudent insurer test, difficulty in applying the actual inducement, true is not necessary in material disclosure, and broad meaning of active duty of disclosure have been colouring negatively the character of the English marine insurance law. In addition, the nature of no gravity of fault has added the problems to the assured to get fair treatment legally and a shield of protection from bad faith and bad-underwriting made by the insurer with regard of the marine insurance policy. The fact that an underwriter may have a bad faith to escape from his liability, clearly could

happen. The case of *Alfred McAlpine v. BAI (Run-off)* (2000) justifies such condition. In the light of that case, Yeo (2002) states that “there was clear indication of bad faith on the part of the insurer – sloppiness in contract drafting, evasiveness in claim handling and general lack of cooperation. Yet BAI, the insurer, was the one to cry foul, turns the tables round and allege that the insured was the one in breach of utmost good faith. The insurer has unapologetically drawn a very tenuous line between over-reliance on and abuse of the good faith defence”.

Another critical legal formulation for those who effecting insurance in the English jurisdiction is the most extreme remedy of avoidance of the contract for breach of the utmost good faith principle. This remedy applies to the pre-contractual stage as well as post-contract time. A fairness of remedy in the context of utmost good faith breach based on the case by case judgment has not been perceived by the English law and practice. As stated by Eggers (2001) this remedy does not allow for the justice of the case. He added also that the court discretion to make it more flexible has not got the basis from referring to no reported cases of allowing court discretion to make another fair remedy in the context of the breach of the utmost good faith duty. Actually, the nature of more flexible remedy has been raised personally by the Lord Hobhouse in the case of *The Star Sea*, particularly when discussing about the post-contract stage of utmost good faith duty.

An evitable consequence in the post-contract situation is that remedy of avoidance of the contract is impractical terms wholly one-sided. It is a remedy of a value to the insurer and, if the defendants’ argument is accepted, of disproportionate benefit to him; it enables him to escape retrospectively the liability to indemnify which he has previously and validly undertaken. Save possibly for some types of reinsurance treaty, it is hard to think of circumstances where an assured will stand to benefit from the avoidance of the policy for something that has occurred after the contract has been entered into.

Unfortunately, the legal formulation taken by Lord Hobhouse was not a majority voice of legal judgement in the context of utmost good faith duty in the English marine insurance law. Most of them, still believe that the remedy of avoidance has been chosen rigidly as a “proper” remedy to give the “injured” party a right to avoid contract.

IV.4. Practice in the Other Jurisdictions

Having said that the regime of sanction in the English marine insurance law with regard to breaching the utmost good faith duty, it has become the strictest and draconian one in the terms of not allowing other remedies than rescission. While it is compared to other European countries. As cited in the Norway, under the Norwegian Marine Insurance Plan 1996 Chapter 3. The primary legal basis has been formulated in this plan is the remedy of avoidance and other remedies will be given based on the gravity of fault. It also stipulates that only fraudulent acts as well as non-disclosure that assumed the insurer would not have accepted the risk if had been disclosed can give the right to the insurer claiming to avoid contract. Or he may cancel the other insurance contracts he has with the person effecting insurance by giving fourteen days notice. In addition, if it must be assumed that the insurer would have accepted but on other condition, he shall only be liable to the extent that it is proved that the loss is not attributable to such circumstances as the person effecting insurance should have disclose. For the post-contract duty, the plan stated that the liability is limited in the same manner if the person effecting insurance has been in breach of the duty of disclosure after the contract was concluded, unless it has been proved that the loss occurred before the person effecting insurance was able to correct the information supplied by him.

Furthermore, Wilhemsen (2000) explains that such legal formulations affirmed the alternative sanction in the context of the Norwegian Plan in which the insurer has freedom of liability for incurred casualties. Or, in the context of both circumstances, the insurer may cancel the contract prospectively, not to avoid the contract retrospectively. She also added that the other alternative of remedy is recognised in the Norwegian cargo clause in the form of reduction in indemnity according to the evaluation based on the influence of the undisclosed information on the insurance contract and the casualty, the degree of fault or other circumstances.

In specific, when it comes to the rule the innocent breach of utmost good faith duty, it was held that if the person effecting insurance has given the incorrect or incomplete

information without any blame attached to him, the insurer is liable as if the correct information has been given to him, or the insurer may cancel the contract by giving fourteen days' notice. In other words, breach of duty in good faith will make the insurer fully liable for the incurred casualties.

One more difference between the English marine insurance law and the Norwegian Marine Insurance Plan is the explicit prohibition in the plan for the insurer to claim for avoiding or cancel the contract if he failed to notify the assured the incorrect or incomplete information has been given to him in respect of effecting insurance. This rule will solve the problem of balance of duty between the assured and the insurer, by which in the English insurance case such as *Banque Financiere* case, proved the unbalance of duty in the application of section 17-20 of MIA 1906.

In another European country, Wilhemsen (2000) again said that French marine insurance law has similar nature in the context of obligation to disclose to the English marine insurance law. Both apply the actual and constructive knowledge. However, French legal formulation on that issue is basically different by stating that if the assured does not possess the knowledge of the factual information, he can not know that this information is material for the insurer. It applies particularly in the French hull and cargo conditions. From here, there is no surprise if the nature of sanction in the French marine insurance law is more flexible and varied than in the English marine insurance case. For example, French Insurance Contract Act article L 172-2 seems to be most favourable with the full protection for the assured who has no knowledge about the information, even if he ought to have known. Accordingly, the insurer is entitled to reduce indemnity proportionally to the premium paid if as a result of non-disclosure that he ought to know, the insurer would have accepted the insurance, but on other conditions and terms. Also, it has been used if the assured knew about the information, but thought it was insignificant (good faith). That legal formulation was totally contrary to the English marine insurance system which allows the insurer to claim avoiding the contract, even if the assured did not possess the information.

In Italy and Slovenia, the avoidance of a contract insurance is only given under the ground of gross-negligence and reduction in liability or additional premium in ordinary negligence. Sweden, Denmark, Germany, Japan and apparently Croatia, the insurer will fully be liable for incurred casualties if there is breach of the duty of disclosure in good faith (innocent breach) (Wilhemsen, 2000).

In the context of common law state, Australia, has stipulated the regime of flexibility in the issue of utmost good faith duty application with section 13 of Insurance Contract Act which provides that there is an implied term in a contract of general insurance requiring each party to act towards the other party with utmost good faith. The legal consequence of making the duty of good faith an implied term of the contract is said to be make a broad range of contractual remedies available both insurer and insured for a breach of the duty of utmost good faith (Derrington, 1996).

Therefore, an effort to make a flexible regime in the context of the application of utmost good faith duty by Australia goes to the basic change of its legal formulation by proposing the new legal concept of utmost good faith duty in the its marine insurance law. This legal proposal of changing the utmost good faith regime in Australia had been recommended by the Australian Law Reform Commission (ALRC) from its report on the Review of the Marine Insurance Act 1909. The ALRC proposed several new legal concept of the application of utmost good faith principle, inter alia, as follows :

1. MIA 1909 must be amended to provide that there is implied term in a contract of marine insurance a provisions requiring each party to act towards the other party with utmost good faith in the terms of ICA section 13 and 14.
2. MIA section 24 (1) and 26 (1) should be amended to provide that an insured must disclose accurately all circumstances that it knows, or a reasonable person in its position would know, to be material.
3. MIA 1909 should be amended to insert new provisions which provide that if the insured has breached its duties relating to non-disclosure and misrepresentation :
 - (1) if the breach is fraudulent, the insurer is entitled to avoid the policy from its outset with no return of premium;
 - (2) if the breach is not fraudulent :

- (a) where the insurer would not have entered into the contract if it had known of the undisclosed circumstance or the truth of the misrepresented circumstance, the insurer is entitled to avoid the policy from its outset but with a return of premium.
- (b) Where the insurer would have entered into the contract but on other conditions, the insurer is not entitled to avoid the policy but : (i) is not liable to indemnify the insured from a loss proximately caused by the undisclosed or misrepresented circumstance; (ii) is entitled to vary its liability to the insured to reflect the amount of any variation in premium, deductible or excess that would have been imposed if it had known of the undisclosed circumstance or the truth of the misrepresented circumstance; and (iii) is entitled to cancel the policy in accordance with the other provisions of the Marine Insurance Act on cancellation which are subject of recommendation 18.

IV.5. The Promising Change of the Utmost Good Faith Duty

From the perspective of the insurer, the remedy of damages has been opened to be used by the insurer in the case of a negligent misrepresentation to the insurer by the assured in a marine insurance contract, as mentioned in section 2(1) of the Misrepresentation Act 1967. However, in the author's view, to use this alternative remedy independently has gained less attention. So that it is more reasonable if this damages will be claim in lieu of the avoidance of a contract.

Nevertheless, the promising change of the harshness and disproportionate regime in the context of utmost good faith duty under the English marine insurance law could be seen from the decision of the House of Lords in the case of *HIH Casualty and General Insurance Ltd and Others v. Chase Manhattan Bank and Others* (2003). In that case, (which was analysed from different perspective in the previous chapter) describes the assured who had no relevant knowledge of the subject-matters insured, financing the film production, placed the risk through his brokers to the insurer. As a matter of having no relevant knowledge and experience in the context of effecting marine insurance, the assured through the broker, asserted the truth of statement into the contract of insurance in order to regulate the duty of utmost good faith owed by the assured and his agents, insurance broker, by the virtue of section 17 – 20 of the Marine Insurance Act 1906. The main purposes of that truth of statement clause is to protect the assured from the extreme

rules applied in the context of utmost good faith principle under the English insurance regime. The clause of a statement truth had regulated, inter alia, as follows :

- (6) the insured will not have any duty or obligation to make any representation, warranty or disclosure of any nature, express or implied (such duty and obligation being expressly waived by the insurers), and;
- (7) shall have no liability of any nature to the insurers for any information provided by any other parties;
- (8) any such information provided by or non-disclosure by other parties.....shall not be a ground or grounds for avoidance of the insurer's obligations under the insurance policy or cancellation thereof.

The assured made claims under the policy amounting to USD 16,5 million, in which the insurers contended by claiming back to avoid the insurance policy based on the grounds of fraudulent as well as negligent misrepresentation and non-disclosure made by his broker. In addition, the insurers also claimed damages to the assured as well as the broker. In his response, the assured denied to the insurer that he could activate the remedy of avoidance or damages based on the application of the truth statement in the insurance policy agreed by both contracting parties, even if the allegation made by the insurer was true.

It was held by the House of Lords that : (1) the clause (6) concerned about the exclusion of the assured's obligations to observe the pre-contractual utmost good faith duty. Therefore, the assured does need to make representation as well as duty to disclose regarding the risks insured, such duties being expressly waived by the insurer. However, the claim that this clause was capable of relieving the broker's duty to disclose was rejected; (2) the clause (7) precludes the right of the insurer to avoid the contract based on the ground of innocent as well as negligent misrepresentation made by the broker. It also precludes the liability of the assured to be claimed in damages under section of 2(1) of the Misrepresentation Act 1967 for any negligent misrepresentation of the broker; (3) clause (8) operates similar to clause (7) above as long as the non-disclosure concerned.

This clause precludes the insurer's right to avoid contract based on the innocent and negligent non-disclosure made by the broker; (4) However, even the truth statement clause was capable to exclude the consequences of any misrepresentation as well as non-disclosure, regardless of their types, the Lords believed that the wording of the truth statement clause was not sufficient enough to exclude the possibility of avoiding the policy by the insurer due to the fraudulent misrepresentation and non-disclosure. Nevertheless, there was dissenting judgment from Scott LJ by stating that the wording of the truth statement clause is capable enough to cover the fraudulent misrepresentation and non-disclosure made by the broker.

According to the legal comments in the Journal of International Maritime Law (2003) the judgement of the House of Lords in the case of *HIH Casualty and General Insurance Ltd and Others v. Chase Manhattan Bank and Others* has given the legal basis that the English court would adopt in interpreting clauses which attempt to limit or exclude the duty of utmost good faith in insurance contracts. The facts that the assured had less relevant knowledge with regard of subject-matters insured, film production business, and the existence of a genuine need to protect his interest against niceties of insurance law. From the legal perspective of the House of Lords, the clause agreed amicably by the contracting parties to exclude the application utmost good faith duty when concluding insurance contract should not be prevented or prohibited under the reasons of public policy or rule of law. Even if there is no reason for public policy this is why he should not be able to exclude his contractual liability for fraudulent non-disclosure or misrepresentation by his agent, unless such agent or broker of the assured knew of, or was otherwise complicit in, the fraud or when the agent was the alter ego of the principal.

Accordingly, the judgement above is good news for the assured who was struggling to find a solution to protect himself from the unfair legal regime under the English law in the context of utmost good faith principle. The contractual approach should include similar the truth statement clause as cited from such case constitutes, at present, the best practical solution legally that the assured may obtain in order to get proper legal protection of his interest in the marine insurance cover. That case also could be a legal

guidance to formulate better wording in the term of exclusion clauses covering the issue of duty of disclosure and misrepresentation, regardless of their types. The adoption of exclusion clause to preclude the utmost good faith duty by the House of Lords has become the recent position of the English marine insurance law in the context of utmost good faith principle.

CHAPTER V CONCLUSION AND RECOMMENDATION

The existence of the utmost good faith principle under the English marine insurance law has been crystallizing the unique position of this principle in its application to the marine insurance business globally. The uniqueness of this principle was derived from the specific application and its different legal approach that it had been taken by the English jurisdiction when dealing with the legal disputes of marine insurance contract under utmost good faith issues. The legal approach uniquely taken by the English jurisdiction has been formulated through the interpretation of section 17-20 of MIA 1906 and applied it to the several prominent legal cases upon which the established legal formula, in the context of utmost good faith principle, upheld precisely. This uniqueness tends largely to be more focused on the protection of the insurer's interests, than making the duty balance between the assured and the insurer.

V.1. English Legal Position of Utmost Good Faith Principle

The acknowledgement of a unbalance obligations in the utmost good faith duty has been proved firstly by the legal issue of balanced duty of utmost good faith in the marine insurance contract. It was not recognized under the English marine insurance law by the judgement of *Banque Financiere de la Cite SA v. Westgate Insurance Co. Ltd. (1990)* which concluded that no duty of disclosure for the insurer to inform the discovered fraud conducted by the assured's broker.

The draconian remedy of avoidance has become the only legal choice that the English can provide, which is proved by the *Litsion Pride*(1985). There was no right to claim damages as stipulated in the case of *HIH Casualty and General Insurance Ltd and Others v. Chase Manhattan Bank and Others. (2001)*. This very extreme remedy was definitely connected with the regime of no gravity of fault in the context of utmost good faith breach. In other words, there is no difference the breach was committed fraudulently, negligently or innocently, all breaches would give the right of the insurer to claim an avoidance of contract.

Truth was not a necessary concept in the context of duty to disclose; the material information is not true such as the material rumours upon which its nature of truth not to be known yet may give the insurer to avoid contract. The case of *Elena* (2001) and *Inversiones Manria S.A. v. Sphere Drake Insurance Co.Plc., Malvern Insurance Co.Ltd., and Niagara Fire Insurance Co.Inc.*, (1989) have proven the legal formulation of the truth of any material information that must be disclosed under the English marine insurance law. However, under the legal basis of truth of the material information, if the assured can prove that such material rumours is not true, he may use it as the legal protection to reject the claim of the insurer to avoid the contract on the ground of material rumours non-disclosure as decided firmly in the case of *Gracia Express* (2002). In addition, the new regime of truth in the material rumours disclosure might not guarantee the assured to be judged under the legal formulation of *Elena* and *Inversiones* cases, owing to the doctrine of precedent law in the common law system which described that the court should not have to follow precisely the court decision which had been decided previously. So then the possibility of the assured being judged for the case of material rumours non-disclosure is still relatively open.

Knowledge of the assured as well as the broker exists under the basis of the actual and constructive knowledge. It means that the presumption of knowledge which could be seen from the words “ought to be known in the course of ordinary business”, may impose the breach of duty if it is failed to disclose. Therefore, when it is connected to the regime of materiality and inducement, the question of non-disclosure, for actual and constructive knowledge, will be measured from the prudent insurer approach. Thus, such non-disclosure, as applied to the law of misrepresentation, has to be proven as to whether having induced the insurer or not. A test of inducement shall be determined as a non-decisive one. This explained that the inducement approach also to be operative in the duty of disclosure. The cases of *CTI* and *Pan Atlantic* have supported such legal formulation applicable in the English marine insurance law.

Another thing that is very interesting is the application of utmost good faith in the pre-contractual stage as well as post-contractual period. The post-contract issue would give the opportunity to the insurer to avoid liability on the grounds which do not connect to the occurrence of the loss. The fraudulent conducts is the only legal basis that may activate the breach of post-contract duty of the utmost good faith. As it can be proved from the cases of the *Litsion Pride*, *Star Sea*, *Mercandian Continent* and *Aegeon*. However, the insurer must show that the fraudulent conducts must be material and induce prejudicially to the ultimate liability of the insurer.

The brief description with regard to the existing law and practice to the application of utmost good faith duty in the context of the English marine insurance regime shows the legal situation which has been disproportionate and unfair from the point of view of the mutual obligation to the insurer and the assured to observe the good faith issues. Particularly, when it compares to the other legal regimes established by several leading marine insurance markets in the European states and Australia.

V.2. Different Approaches

Several European countries, mainly from the civil law system, had adopted a different approach as taken by the English jurisdiction. Countries like Norway, Italy, Germany, France, Slovenia, and Croatia much prefer to establish a balance duty of utmost good faith by stipulating the flexibility in terms of remedy to the breach of such duty based on the gravity of fault. And they provide a fair legal formulation in the issue of materiality test as well as the limit of knowledge that should be disclose to the insurer. That fair regime of the application of utmost good faith duty also has been followed by one common law state, Australia, by applying broad choices of remedies in the context of the application of utmost good faith in a insurance contract under the ICA. Then it revises its marine insurance law turning to the position much in favour of the protection of the assured's interests. The force to take a harmonised marine policy among the states, has been accelerating through the commitment made in the European Community. In addition, an international action taken by the Comite Maritime International to persuade the harmonisation of certain issues of the marine insurance among jurisdictions, can be a

good step to persuade the English marine insurance community in order to reconsider of change the section 17.20 of the MIA 1906.

V.3. A New Legal Position

In the absence of any change to the section 17-20 of the MIA, the assured may achieve the benefits of the recent legal position taken by the English court. By which, it allows to limit or exclude the duty of utmost good faith by applying an specific clause in the insurance policy. At least, for those, the assureds, who want to effect the insurance cover under the English law, may obtain a better legal protection of harshness and disproportionate of the application of utmost good faith duty including its draconian remedy of avoidance the contract under the basis of contractual approach by inserting a similar clause of the truth statement. It would become a high relief to create a balance position and legal solution for the assured to have certainty in his insurance cover.

V.4. Legal Recommendations

1. It is highly desirable to revise the legal conceptualisation of the section 17-20 of Marine Insurance Act 1906. The subject-matters are recommended to be revised namely; the notion of no gravity of faults in its application, the extreme remedy of avoidance of the contract, the prudent insurer test, conceptualisation of the assured's knowledge, and actual inducement of non-disclosure.

2. If the assured has an intention to effect an insurance cover, particularly marine insurance policy, and does not want to be involved with the intrigues of the English marine insurance law, upon which his cover may be abolished drastically as a result of breach of the utmost good faith duty, he may choose other kind of policy under the jurisdiction of different states in other insurance markets such as :
 - a. Norway
 - b. France.
 - c. Germany.
 - d. Australia.

The legal reason for that choices of using other types of jurisdiction when one effecting insurance cover is caused by the legal regime applied to those types of jurisdiction above simply is generally fairer and proportionate in terms of imposing the duty of utmost good faith in the insurance policy and provides a broad range of remedies based on the gravity of the fault. Hence an assured, which is afraid of losing the insurance cover as a result of breach, innocently or mere negligently, of the utmost good faith duty, will get better legal treatment which much more tends to protect the assured's interests and keep a balance to observe the obligation of utmost good faith between the assured and the insurer.

3. If one wants to effect the insurance cover under the context of the English marine insurance law, that person should be legally aware or careful of the legal effects of the utmost good faith duty imposed on the shoulder of an assured or his broker. It is because the effect of such duty, when breaching it regardless the gravity of fault, leaves the assured without his insurance cover. So in order to solve this legal problem, under the regime of the freedom of contract, one should assert the specific clauses in an insurance contract which generally regulates the exclusion of utmost good faith duty stipulated in the section 17-20 of Marine Insurance Act 1906. In specific, such exclusion clauses would cover the legal issues of :
 - a. An exclusion of the obligations to perform the duty of utmost good faith, particularly when the assured has no relevant knowledge to the subject-matters insured;
 - b. Limit the scope of the insurer's right to avoid the contract only based on the grounds of fraudulent breach of utmost good faith duty.
 - c. An exclusion not to observe the utmost good faith duty is applicable to the assured as well as the broker.
 - d. It should be ensured that the wording of the exclusion clauses regulate firmly the legal formulation stipulated I item a, b, and c in order to give the strong evidence to the court regarding the exclusion of utmost good faith precisely as mentioned in the MIA 1906 (when it is necessary).

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