

INSURANCE AND REINSURANCE UPDATE

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CLAIMS SETTLEMENT: ENGLISH COMMERCIAL COURT CONSIDERS LEAD UNDERWRITER'S DUTIES TO FOLLOWING MARKET

In *San Evans Maritime Inc and others v Aigaion Insurance Co SA*¹, the English Commercial Court considered whether the following underwriter was obliged to follow the settlement of the lead underwriter on one policy, in circumstances where the second policy contained a follow settlements clause.

BACKGROUND

This decision concerned the Court's determination of three preliminary issues arising in a claim brought against the Greek insurance company Aigaion Insurance Co SA ("Aigaion") by the owner, manager and mortgagee of the vessel *St. Efrem*, which grounded in Brazil in July 2010 and suffered a generator breakdown (together, "the Assured").

Three Lloyd's syndicates, Catlin, Ark and Brit, insured 50% of the interest in the vessel under one policy ("the Lloyd's Policy"). Catlin was the slip leader. Aigaion insured 30% of the interest in the vessel under a separate policy ("the Aigaion Policy"). The remaining 20% interest was uninsured. The terms of the two policies differed. The Aigaion Policy contained a "Follow Clause" which provided, "Agreed to follow London's Catlin and Brit Syndicate in claims excluding ex-gratia payments".

A claim was made under both policies. The Lloyd's syndicates settled the claim against them, each being liable for its respective share of the settlement sum. Aigaion was not a party to the settlement agreement, the key clause of which (clause 7) provided, "*The settlement and release pursuant to the terms of this Agreement is made by each Underwriter for their respective participations in the Policy only and none of the Underwriters that are party to this Agreement participate in the capacity of a Leading Underwriter under the Policy and do not bind any other insurer providing hull and machinery cover in respect of the St. Efrem.*"

The Assured argued that Aigaion was obliged to follow that settlement, which Aigaion denied. Three preliminary issues fell to be determined by the Court:

- On a proper construction, did the Follow Clause (i) require Aigaion to follow any settlement made by Catlin and Brit under the Lloyd's Policy; or (ii) merely authorise Catlin and Brit to act on Aigaion's behalf in negotiating and/or agreeing the settlement of disputed claims with the Assured?
- If, on a proper construction of the Follow Clause, it required Aigaion to follow any settlement made by Catlin and Brit under the Lloyd's Policy, was the Follow Clause triggered by the settlement agreement?

¹ [2014] EWHC 163 (Comm)

- Did the Assured agree by clause 7 of the settlement agreement that the agreement would not be binding on Aigaion; and if so, was Aigaion entitled to rely on the Contracts (Rights of Third Parties) Act 1999 to enforce that term?

DECISION

Issue 1:

The Court held that the Follow Clause was a simple agreement between Aigaion and the Assured that Aigaion would follow the settlement of claims by Catlin and Brit. Applying a simple approach to the clause's construction was consistent with its commercial purpose to simplify the claims settlement process. The operation of the clause did not depend upon Catlin and Brit acting as agent for Aigaion so as to bind Aigaion to the settlement and it was not to be understood as authorising Catlin and Brit to act on behalf of Aigaion. The clause said nothing about authority. Aigaion simply agreed to follow Catlin and Brit in claims and therefore in settlements. There was no agreement between Aigaion and Catlin or Brit; the agreement was between Aigaion and the Assured. To suggest that the clause merely authorised Catlin and Brit to act on Aigaion's behalf when settling a claim ignored, and added to, the simple words of the clause. On the question of agency, the Court recognised that there is uncertain case law as to the basis upon which follow clauses operate. Introducing the concept of agency in this case, however, when there was no agreement between Aigaion and Catlin and Brit, would mean unnecessarily complicating the operation of the clause. Mr Justice Teare quoted the following passage in reaching his conclusion²:

"For better or worse following insurers trust and follow their leader....Following underwriters accept both the advantages and any risks of the leading underwriters' handling of settlements and of other matters affecting them."

Issue 2:

Aigaion contended that the Follow Clause did not apply to a settlement which was expressly agreed not to be binding on Aigaion. The Court disagreed and held that the Follow Clause was triggered by the settlement agreement. While case law suggests that a lead underwriter may owe a duty of care to the following underwriter (and he may therefore wish to clarify that in settling a claim he is doing so on his own behalf only and is not purporting or intending to bind the following

underwriter), it is not for the lead underwriter to go against the effect of a follow clause if it obliges the following underwriter to follow any settlement made by the lead. It therefore did not matter that Catlin and Brit purported to act only on their behalf when settling the claim, because Aigaion had agreed to follow any settlement by Catlin and Brit (excluding ex-gratia payments). The Court considered that the commercial purpose of the clause would be frustrated if it did not apply whenever an underwriter, fearing that he might be held to owe a fiduciary duty/duty of care to the following underwriter, made clear when settling a claim that he was doing so only on his own behalf.

Issue 3:

The Assured submitted that there was no need to construe clause 7 of the settlement agreement as though it applied to anyone other than the parties to the agreement. Aigaion submitted that the obvious commercial intention of the clause was that Aigaion would not be bound by the settlement agreement because it fell within the phrase *"any other insurer providing hull and machinery cover in respect of the St. Efrem"*. The Court agreed. In circumstances where the parties to the settlement agreement were aware that Aigaion insured 30% of the interest in the vessel on terms which included the Follow Clause, the reference in the clause to *"any other insurer"* was not a reference to underwriters subscribing to the Lloyd's Policy, but to other insurers such as Aigaion. Aigaion was not entitled to rely upon the Contracts (Rights of Third Parties) Act 1999 to enforce clause 7 because the parties' purpose in agreeing the clause was not to confer a benefit on Aigaion; it was to protect the syndicates from any possible liability in light of the fact that the Aigaion Policy contained the Follow Clause. Moreover, the Assured had not agreed to give up its right to rely upon the Follow Clause as against Aigaion.

CONCLUSION

The Court preferred to adopt a simple approach to the construction of the Follow Clause, in order to give effect to its commercial purpose of simplifying the claims settlement process. Lead and following underwriters should bear in mind, however, that this type of clause manifests itself in different forms. Interpreting the intended effect of such a clause therefore requires analysis of the terms of the particular clause in question, considered in the context of the surrounding circumstances.

² See *Roar Marine Ltd v Bimeh Iran Insurance Co*, [1998] 1 Lloyd's Reports 423

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