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## Reforming the duty of utmost good faith/fair presentation in Hong Kong

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Reforming The Duty Of  
Utmost Good Faith/Fair Presentation  
In Hong Kong

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1682605

A Thesis submitted for the Doctor of Philosophy in Law

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## **Abstract**

This thesis aims to propose a reform on the current duty of utmost good faith in Hong Kong commercial insurance law. The duty has long been criticised on the basis that it is insurer-friendly and outdated. Although a call for reform was raised in Hong Kong in 1986, the attempt was in vain, and there has not been any major law reform in this area. In England and Wales, the Insurance Act 2015 came into force on 12<sup>th</sup> August 2016, and the duty of utmost good faith was replaced by the duty of fair presentation. In Hong Kong, English law was strictly adopted before the transfer of sovereignty in 1997. After 1997, Hong Kong became part of China's territory and is not obliged to follow any legal reform in England and Wales. Nevertheless, the author suggests that it is now the time to discuss the reform of the duty. The main theme of this thesis, therefore, is about how the duty should be reformed in Hong Kong.

Each chapter of this thesis will be divided into three parts. Firstly, the problems with the current duty in Hong Kong will be identified. There are two types of problems, namely the problems that are commonly shared between English law and Hong Kong law, and the problems that only Hong Kong experiences. Secondly, the chapter will discuss whether adopting the model of the Insurance Act 2015 can resolve the problems that have been identified. Lastly, reform suggestion for the Hong Kong commercial insurance law will be presented.

In the final chapter, all the reform suggestions in the previous chapters will be gathered and a concrete reform proposal will be put forward for the current legislation that is related to the duty of utmost good faith in Hong Kong.

# Introduction

## I. Background

In the context of English insurance law, the doctrine of utmost good faith has long been and remains complicated. Since an insurance contract is a contract of speculation, the doctrine aims to protect the insurer from the imbalance of information during the process of underwriting. One of the first cases that explained the doctrine was *Carter v Boehm*,<sup>1</sup> where Lord Mansfield underlined the principles of the doctrine as follows:

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 under-writer is deceived, and the policy is void; because the risque run is really different from the risque understood and intended to be run, at the time of the agreement.<sup>2</sup>

150 years after this landmark judgment, the Marine Insurance Act 1906 (MIA 1906) was enacted in the United Kingdom, and the duty was included in the Act. According to the legislation, the doctrine can be observed from two aspects. Firstly, an assured is obliged to disclose material facts to an insurer before an insurance contract is concluded. Secondly, an assured is obliged not to misrepresent material facts to an insurer at a pre-contractual stage. The operation of the doctrine has been criticised by judges and scholars.<sup>3</sup> The language of the legislation is ambiguous, and it has caused undue hardship for the assured to comply with the requirement.<sup>4</sup> Furthermore, it is suggested that the duty is a one-sided doctrine, which is strongly in favour of the insurer.<sup>5</sup> To resolve these problems, the Law Commission proposed two different reform solutions regarding consumer and commercial insurance cases. In relation to consumer insurance cases, the Consumer Insurance (Disclosure and Representation) Act 2012 was enacted, and the duty of disclosure and to avoid misrepresentation, as stipulated in

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<sup>1</sup> *Carter v Boehm* (1766) 3 Burr. 1905

<sup>2</sup> *ibid* 1909

<sup>3</sup> For example, see *Lambert v Co-operative Insurance Society Ltd* [1975] 2 Lloyd's Rep 485, 491 and F.D. Rose, "Informational asymmetry and the myth of good faith: back to basis" [2007] L.M.C.L.Q 181

<sup>4</sup> Law Commission, *Insurance Contract Law: Business Disclosure; Warranties; Insurers' Remedies for Fraudulent Claims; and Late Payment* (Law Com CP No 353, 2014) para 5.8

<sup>5</sup> *ibid* para 1.25

section 18, 19 and 20 of the MIA 1906, were abolished.<sup>6</sup> Later, the Insurance Act 2015 (IA 2015) was enacted to introduce reform in commercial insurance law, and the doctrine of utmost good faith was replaced by the duty of fair presentation of the risk.<sup>7</sup> It is suggested that the distinction between the reform solutions in consumer and commercial insurance cases lie in the complexity of the underwriting process.<sup>8</sup> Since the underwriting processes in commercial insurance cases are more complicated, the Law Commission has suggested that the duties of disclosure and not to misrepresent material knowledge should still be retained in commercial insurance cases.<sup>9</sup> It is noteworthy that as far as the new duty of fair presentation is concerned, there is only one Scottish case law, namely *Young v Royal and Sun Alliance Plc*,<sup>10</sup> that was considered under the IA 2015. This case will be examined in Chapter 2(I)(B)(i) of this thesis as a reference for the potential scope for the new duty of fair presentation under the IA 2015.

As a former British colony, Hong Kong remains a common law jurisdiction. Article 8 of the Basic Law of Hong Kong provides that:

The laws previously in force in Hong Kong, that is, the common law, rules of equity, ordinances, subordinate legislation and customary law shall be maintained, except for any that contravene this Law, and subject to any amendment by the legislature of the Hong Kong Special Administrative Region.

In addition, article 84 of the Basic Law also authorises the Hong Kong court to consider case law of other common law jurisdiction.<sup>11</sup> In other words, case law in England and Wales is directly applicable to the Hong Kong court before and after the transfer of sovereignty in 1997.

Hong Kong and London also share a similar market structure in relation to the placement of general insurance. According to the market statistics of the Hong Kong Insurance Authority in 2017, the four major classes of general insurance in Hong Kong were Accident and Health, Motor, Property and Liability insurances, which amounted to over 80% of the gross premiums of

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<sup>6</sup> The Consumer Insurance (Disclosure and Representations) Act 2012, S11. The assured now only needs to take reasonable care in order to avoid misrepresentation of risk. See The Consumer Insurance (Disclosure and Representations) Act 2012, S3

<sup>7</sup> The Insurance Act 2015, S3

<sup>8</sup> Law Commission (n4) para 6.28

<sup>9</sup> *ibid*

<sup>10</sup> *Young v Royal and Sun Alliance Plc* [2019] CSOH 32

<sup>11</sup> The Basic Law of the Hong Kong Special Administrative Region of the People's Republic of China, article 84

the Hong Kong general insurance market.<sup>12</sup> In London, the classes of general insurances are more diverse, but the above mentioned four types of insurance also amounted to over 50% of the gross premiums of the London market in 2017.<sup>13</sup>

In Hong Kong, there is no relevant regulation that applies to utmost good faith cases. The only reference, which is a self-regulatory initiative, is The Code of Conduct for Insurers. The Code was introduced by the Hong Kong Federation of Insurers (HKFI), but it does not have any binding effect. Paragraph 10 of the Code of Conduct requires the insurer to include a statement in the proposal form that explains the consequence of failure to comply with the duty of disclosure. It also requires the insurer to warn the assured to disclose every information that may be material to the risk, even when the assured is uncertain about whether such a piece of information is material or not. Paragraph 15 requires the insurer to remind the assured to comply with the duty of disclosure upon renewal. Paragraph 24 provides that the insurer should not reject the claim on the following grounds:-

- (a) on the grounds of non-disclosure of a material fact which the policyholder could not reasonably have been expected to disclose, or if the insurance was issued without the policyholder being requested to submit a proposal;
- (b) on the grounds of misrepresentation unless this is a deliberate or negligent misrepresentation of a material fact, provided that this does not apply to marine or aviation policies.<sup>14</sup>

Despite the existence of these provisions, utmost good faith cases are still in disputes frequently. According to the Insurance Complaints Bureau, non-disclosure was one the two major sources of complaints in the year of 2017/2018.<sup>15</sup> In this regard, the author suggests that the root of the problem may lie in the legislation. The relevant provisions can be found in the

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<sup>12</sup> Hong Kong Insurance Authority, Table G1 Underwriting Results of Direct & Reinsurance Inward Business for 2017, <[https://www.ia.org.hk/en/infocenter/statistics/files/T\\_G1\\_2017.pdf](https://www.ia.org.hk/en/infocenter/statistics/files/T_G1_2017.pdf)> accessed 14 March 2019

<sup>13</sup> International Underwriting Association of London, London company market statistics report, October 2018, <[https://www.iaa.co.uk/IUA\\_Member/Publications/London\\_Company\\_Market\\_Statistics\\_Report.aspx](https://www.iaa.co.uk/IUA_Member/Publications/London_Company_Market_Statistics_Report.aspx)> accessed 8 March 2019.

<sup>14</sup> Hong Kong Federation of Insurers, The Code of Conduct for Insurers <[https://www.hkfi.org.hk/pdf/en/download/e\\_abt.code.pdf](https://www.hkfi.org.hk/pdf/en/download/e_abt.code.pdf)> accessed 8 March 2019.

<sup>15</sup> The Insurance Complaints Bureau, annual report 2017/2018, page 27, <[http://www.icb.org.hk/files/ar\\_2017\\_18.pdf](http://www.icb.org.hk/files/ar_2017_18.pdf)> access on 8 March 2019. It is noteworthy that the Insurance Complaints Bureau only handles insurance complaints in relation to personal insurance. Nevertheless, it suggests that utmost good faith cases are problematic regardless of personal or commercial insurance, as the duty of utmost good faith applies to both types of insurance in Hong Kong.

Marine Insurance Ordinance (MIO), which is almost identical to the MIA 1906.<sup>16</sup> It is suggested that the duty of utmost good faith in Hong Kong also shares the same pitfalls with the duty in England and Wales. While the IA 2015 came into force on 12<sup>th</sup> August 2016 in England and Wales, Hong Kong commercial insurance law still follows the old English law principles in the MIA 1906. In other words, the duty of utmost good faith is still applicable to consumer and commercial insurance contracts in Hong Kong. The last attempt to reform the duty was made by the Law Reform Commission of Hong Kong in 1986, but no significant change was made after the issuance of the reform proposal.<sup>17</sup> In light of the enactment of the IA 2015 in England and Wales, it is now the appropriate moment for the legislator in Hong Kong to consider reforming the duty of utmost good faith.

## II. Aims and objectives

The main theme of this thesis is to propose reform solutions for the duty of utmost good faith in Hong Kong commercial insurance law.<sup>18</sup> The mainstream views are presented from the perspectives of practitioners, including judges, lawyers, brokers and insurers, but the fact is that the duty is imposed for the purpose of educating the assured to present the risk fairly. In other words, the duty is to be followed, observed and complied with by the assured, who is likely to be a layman with regard to insurance law and practice. However, the language of the legislation, in particular, the language of section 17, 18, 19 and 20 of the MIO, leads to ambiguity for the reader of the legislation. It may be suggested that the reader can understand the legal principles through reading cases and authoritative textbooks, which is too heavy a burden for the assured to take on.

In fact, it is not uncommon that in Hong Kong, even legal practitioners can be confused by the duty of utmost good faith. In *Wunsche Handelsgesellschaft International Mbh v General Accident Insurance Asia Limited*,<sup>19</sup> the lawyer for the plaintiff alleged that the insurer was in breach of the duty of disclosure, and thus the plaintiff was entitled to a remedy of rectification

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<sup>16</sup> See *Hua Tyan Development Ltd. v Zurich Insurance Co. Ltd. (The Ho Feng 7)* [2014] 2 Lloyd's Rep. 637, [2014] HKCFA 72 [14] – [15]

<sup>17</sup> Law Reform Commission of Hong Kong, *Reform on laws on insurance* (Topic 9, 1986)

<sup>18</sup> It is distinguished from the consumer insurance law.

<sup>19</sup> *Wunsche Handelsgesellschaft International Mbh v General Accident Insurance Asia Limited* HCCL 73/1994

with respect to the coverage terms of the insurance contract.<sup>20</sup> Although the current law is unclear as to the duty of disclosure that is owed by the insurer, it is evident that the remedy of avoidance is the only remedy available in the case of breaching the duty of utmost good faith.<sup>21</sup> It is submitted that, therefore, the lawyer for the plaintiff failed to observe the actual operation of the duty of utmost good faith and as a result, he sought an inappropriate remedy. The confusion, in this case, lies in the unique nature of the insurance contract. Insurance contract is based on a duty which is independent from general contract law, and therefore, remedies of general contract law are not applicable on the ground of breaching the duty of utmost good faith. In another case *Hua Tyan Development Ltd. v Zurich Insurance Co. Ltd. (The Ho Feng 7)*,<sup>22</sup> the counsel for the assured relied on Professor Bennett's passages in his authoritative textbook, *The Law of Marine Insurance*,<sup>23</sup> to support his allegation that the deadweight tonnage was concealed by the assured, and thus the assured breached the duty of disclosure. Nevertheless, it turned out that the reliance placed by the counsel on these passages was misplaced, as the issue in dispute was about the breach of warranty, and the allegation of breaching the duty of disclosure was irrelevant.<sup>24</sup>

Nevertheless, it is submitted that the confusion of the duty of utmost good faith is multi-faceted. It does not only merely arise in the practical operation of the doctrine about section 18, 19 and 20 of the MIO, but also appears to be misused in other contexts. For instance, in *HKSAR v Chan King Lam*,<sup>25</sup> Mr. Justice Line referred to the term "utmost good faith", in a criminal case which concerned a conspiracy to defraud, to describe the trust relationship between the insurer and the assured.<sup>26</sup> In another case *Chan Woon-Hung v Associated Bankers Insurance Co. Ltd.*,<sup>27</sup> which concerned a car accident claim, and the assured failed to comply with a clause in the insurance policy, which required him to forward every summons to the insurer. Yang, C.J., in his judgment, concluded that an insurance contract was a contract of utmost good faith, and therefore, it required the assured to "faithfully and strictly" comply with the contractual terms,

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<sup>20</sup> *ibid* [6]

<sup>21</sup> See *La Banque Financière De La Cite S.A. v Skandia (U.K) Insurance Co. Ltd.* [1990] 2 Lloyds Law Rep 377

<sup>22</sup> *The Ho Feng 7* (n16)

<sup>23</sup> Howard Bennett, *The Law of Marine Insurance*, (Oxford University Press Second Edition 2006)

<sup>24</sup> *The Ho Feng 7* (n16) [56]

<sup>25</sup> *HKSAR v Chan King Lam* HCMA482/2009

<sup>26</sup> *ibid* [6]

<sup>27</sup> *Chan Woon-Hung v Associated Bankers Insurance Co. Ltd.* CACV000036/1991

and failure to do so amounted to a breach of his contractual obligation.<sup>28</sup> The above two cases illustrates that the duty of utmost good faith in insurance law cases can be misinterpreted due to its lack of precisely defined scope in the legislation.

Besides, the current duty that applies in Hong Kong has put the insurer in a privileged position, and has failed to achieve a true fairness between the parties to an insurance contract. For instance, the legislation has not imposed any obligation of disclosure on the insurer; it is not even uncommon that the insurer may be in a better position to possess certain material knowledge which is related to the insured risk. For the duty of disclosure on the assured side, the insurer is not obligated to assist the assured through the process of the disclosure; even the insurer is in a better position to determine the materiality of the disclosable knowledge. The remedy of total avoidance of the contract, in the case where the breach of the duty is proved, also authorises the insurer to “underwrite” the risk again at a later stage of the contract. These are no doubt unfavourable in Hong Kong, where the economy heavily relies on the insurance market. The severity of the duty may reflect badly on the reputation of Hong Kong’s insurance market.

Therefore, to resolve the problems, this thesis will introduce a reform proposal to the duty, so that even a layman is able to understand and follow it. In order to achieve this aim, this thesis will examine the possibility of reform from three perspectives. Firstly, the current problems with the existing duty will be identified, and then this thesis will consider whether the IA 2015 in England and Wales is a good precedent for Hong Kong to follow. It is suggested that the IA 2015 may not be the best solution for reforming the duty of utmost good faith in Hong Kong. One of the reasons is that the IA 2015 is imposed as a “default regime” for the insurance market rather than mandatory.<sup>29</sup> In other words, as far as the new duty of fair presentation is concerned, the parties to an commercial insurance contract are free to contract out of the IA 2015, with the conditions that the terms imposed cannot put the assured in a worse position than the one in IA 2015,<sup>30</sup> and the insurer also needs to satisfy the transparency requirement in

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<sup>28</sup> *ibid*

<sup>29</sup> Explanatory notes to Insurance Bill 2015, para 19

<sup>30</sup> The Insurance Act 2015, section 16(2)

section 17 of the IA 2015.<sup>31</sup> With respect, it is submitted that the contracting out clauses will only give rise to uncertainties over the obligation of the assured. Worse still, the ambiguous definition of “the disadvantageous term”<sup>32</sup> and also “the transparency requirement” may lead to an increase in litigation which concerns the requirement of contracting out of IA 2015.

Another reason why the IA 2015 may not be a good precedent for Hong Kong law reform is that the insurance market in England and Wales does not entirely welcome the enactment of the IA 2015. For example, the Shipowners’ Limited has issued a notice and suggested that the group will not follow the remedies as introduced in the IA 2015 regarding the duty of fair presentation.<sup>33</sup> This thesis will also further explore other possible solutions to reform the existing duty of utmost good faith in Hong Kong, apart from adopting the IA 2015. These can be achieved by modifying the current duty of utmost good faith with reference to the general contract law, alternatively by amending the language of MIO and IA 2015.

### **III. Structure**

There are two types of problems about the duty of utmost good faith in Hong Kong. The first type of problems relates to issues that are commonly shared between English law and Hong Kong law. As the MIO is almost identical to the MIA 1906, it is suggested that Hong Kong law also shares the same problems with English law. To resolve the problems, this thesis will focus on the situation in England and Wales, as most of the research materials on the law reform are published by the practitioners and the scholars in England and Wales. The related research materials include case reports, textbooks, journal articles and also consultation papers and reports that are published by the Law Commission in England and Wales.<sup>34</sup> For example, the Law Commission has published lengthy papers and reports on the legal developments and the comments from the practitioners on the reform of the duty, which are considered as one of the most important sources of this thesis. It is suggested that these research materials are all directly applicable to the situation in Hong Kong.

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<sup>31</sup> The Insurance Act 2015, section 17

<sup>32</sup> The Insurance Act 2015, section 16(2) and section 17(1)

<sup>33</sup> The Shipowners’ Limited, ‘Notice to Members Concerning the International Group’s Position on The Insurance Act 2015’ <<https://www.shipownersclub.com/media/2015/11/Notice-to-Members-concerning-the-International-Groups-position-on-the-insurance-act-2015.pdf>> accessed 29 August 2018

<sup>34</sup> It is noteworthy that since the duty of utmost good faith in Hong Kong is not reformed in both consumer and commercial insurance law, therefore, the consumer insurance case law in relation to the duty of utmost good faith in England and Wales, the disputes of which happened before the enactment of The Consumer Insurance (Disclosure and Representations) Act 2012, are all applicable in Hong Kong.



The second type of problems relates to the specific issues in the context of Hong Kong law, which are unique to the situation in Hong Kong only. It is suggested that the root cause of these problems lies in the inevitable loss in translation in applying the MIO and the MIA 1906. Nevertheless, as opposed to research materials that cover the situation in England and Wales, one can rarely locate research materials that are solely based on the Hong Kong situation. Therefore, the major source of research will be based on the case reports in Hong Kong. As the primary source of law in Hong Kong, these case reports can accurately identify the problems in Hong Kong, in comparison with the situation in England and Wales.

This thesis consists of six chapters. Chapter 1 of this thesis considers the knowledge requirement of the duty of disclosure. In commercial insurance cases, the assured is always a company which encompasses a group of people. The problematic part of the knowledge requirement is that it is difficult for the assured to identify the exact person to be subject to the duty of disclosure in a company. The legislation and case law suggest that the whole company is treated as a legal entity, and thus subject to the duty of disclosure. However, it is contradictory to the “actual underwriter” approach under section 18(3)(b) of the MIA 1906/MIO. Section 18(3)(b) only concerns the knowledge of a single person, that is, the underwriter who is responsible for underwriting the risk. The scope of the duty may also be too wide to be dealt with by the assured. To solve this problem, a reform which involves adopting the “actual assured” approach to fulfil the knowledge requirement of the assured is proposed in this thesis. This ensures that in an assured company, the duty of disclosure only requires a single person, who is responsible for the arrangement of the insurance, to submit material information to the insurer. Chapter 1 also identifies the problem that the definition of the term “deemed knowledge” under the MIA 1906/MIO is too vague and wide for the assured to comply. Therefore, under the reform proposal of this thesis, the scope of the “deemed knowledge” should be limited by a new duty of reasonable search, which ensures that the assured is only deemed to know the knowledge that is reasonably reachable by the actual assured. The duty of reasonable search also prevents the actual assured to turn a blind eye to the knowledge that is in fact reachable by him or her but for the reduction of premium, he or she chooses to ignore that piece of information. It is noteworthy that the said new duty of reasonable search is different from the same duty under the IA 2015. The most significant difference is that the new duty of reasonable

search, under the reform proposal, is also imposed on the insurer to ensure fairness between the parties to an insurance contract.

Chapter 2 examines the materiality and inducement tests of the duty of disclosure. While the materiality test requires the assured to put himself or herself into the shoes of the fictional “prudent insurer” to deduce what is disclosable to the insurer, the test does not require the insurer to act prudently during the underwriting process. This is regarded as a double standard that is unfavourable to the assured. Furthermore, the performance of practitioners in the cases suggest that the materiality test is unreasonably difficult for the assured to understand and thus to comply with it. To solve these problems, a new materiality test is imposed under the reform proposal of this thesis. The new test is a hybrid of the reasonable insured test and prudent insurer test. It ensures that the assured will be able to understand what to disclose, and the insurer will be able to obtain enough information to carry out a risk assessment.

This chapter also examines the problem of the inducement test. The inducement test is a subjective test which relies on the insurer to prove his or her own case. Since the test is subjective, the insurer may be able to exaggerate the degree of inducement without any consequences. Furthermore, the use of the presumption of inducement may provide a short-cut for the insurer to escape from the liability of proving inducement. To fix these problems, the reform proposal of this thesis proposes new provisions to govern the proof of inducement by the insurer. The reform encourages the insurer to prove inducement in a more systematic and objective manner. In addition, the new provisions also restrict the use of the presumption of inducement to cases with justifiable reasons only.

Chapter 3 considers the problem of the law of misrepresentation in relation to the duty of utmost good faith. The MIA 1906 and MIO are unclear as to whether the duty of disclosure shares the same inducement test with the duty not to misrepresent. The cause of this problem is identified in chapter 2 of the thesis, which is the absence of inducement test from the legislation. The reform proposal of this thesis imposes new provisions to clarify that the two duties share the same inducement test. As a result, the inducement test should not lead to different judgments on the same issue in relation to non-disclosure and misrepresentation. The other problem of the law of misrepresentation is that the insurer habitually pleaded misrepresentation under the

Misrepresentation Act 1967 as an alternative allegation of breaching the duty of utmost good faith under the MIA 1906. This practice was not the intention of the draftsmen of the Misrepresentation Act 1967, and the insurer may have been able to benefit from the unjust privilege of trialling the same issue twice. Furthermore, a case trend analysis also suggests that the Misrepresentation Act 1967 is not applicable to utmost good faith cases. The reform proposal of this thesis, therefore, fixes this problem by imposing a new provision in section 17 that forbids the use of Misrepresentation Ordinance in utmost good faith cases.

Chapter 4 examines the problems in relation to the remedies of the breach of the duty of utmost good faith/fair presentation. It is evident that the duty of utmost good faith is a bilateral duty, but the reality is that the assured is not able to sue against the insurer, as there is no appropriate remedy available under the MIA 1906/MIO. The reform proposal of this thesis introduces a remedy of damages in the new section 17 of the MIO as a starting point of the future development of the insurer's duty of utmost good faith. The reform also separates section 17 from section 18, 19 and 20 of the MIO. The new section 17 would regulate issues that are not covered by the new duty of fair presentation introduced under section 18, 19 and 20. (i.e. the post-contractual duty of utmost good faith).

The other problem of the remedies is that the single remedy approach is too harsh for the assured. In some cases, the seriousness of a breach of the duty may not justify the use of such a draconian remedy. The IA 2015 has tried to solve the problem by introducing the proportionate remedies. One of the new remedies allows the insurer to reduce claim payments in proportion to the premium that would have been charged if the risk was fairly presented. This approach is certainly fairer than the single remedy approach under the MIA 1906/MIO, but again, this approach is still in favour of the insurer and penalises the assured without any justifiable reason. Therefore, to solve this problem, the reform proposal of this thesis introduces new proportionate remedies for the new duty of fair presentation. The first remedy is the remedy of avoidance, which allows the insurer to avoid the contract if the breach is serious enough for the insurer. The second remedy is the remedy of charging an additional premium, which allows the insurer to recover the loss of the premium due to a minor breach of the duty. These remedies are proposed in the hope that the duty can be operated in a way that is more

proportionate to the loss and that a balancing act can be done between the two contracting parties.

Chapter 5 examines the agent's duty of disclosure. Due to the complication of commercial risk assessment, the use of an agent is a common practice for commercial insurance. It is for this reason that the MIA 1906/MIO imposes an independent provision for the duty of disclosure of the agent. Nevertheless, the so-called independent duty of agent causes the confusion that the insurer is entitled to claim against the agent for an independent remedy, which is a mere misunderstanding of the law. In practice, the agent's duty of disclosure has rarely been litigated in both English and Hong Kong courts. Considering the confusion that has been caused by the agent's duty of disclosure, the reform proposal of this thesis suggests that section 19 of the MIO should be eliminated, and the agent's duty of disclosure should be governed by the new section 18 under the reform proposal.

Chapter 6 formulates the detailed reform proposal and the result of the online survey for the duty of utmost good faith/fair presentation in Hong Kong. In the author's view, the duty of utmost good faith/fair presentation is the essence of commercial insurance contracts for without the said duty, it is highly unlikely that a risk assessment can be fairly conducted by the insurer at the pre-contractual stage. For example, under a cargo risk policy, in the absence of the duty of disclosure, the assured is not obliged to disclose accurate information about the cargo (i.e. the type of cargo and condition of the cargo). However, these information is crucial to the assessment of risk, and it is highly unlikely that the insurer would be able to find out this kind of information without the assured volunteering it. Therefore, it is submitted that the "contracting out" provisions should not be introduced in the reform proposal of this thesis, because it is necessary to regulate the exchange of information between the two contracting parties at the pre-contractual stage. However, the said regulations should be amended as time goes by. In the author's view, there is no better time than now for Hong Kong to reform its duty of utmost good faith.

#### **IV. Methodology**

This section will be divided into two parts. The first part sets out the criteria for evaluation in relation to the proposed law reform in Hong Kong. The second part considers the methodology

of the anonymous online survey (the Hong Kong survey), the result of which is examined in chapter 6 of this thesis.

### **A. Criteria for the law reform proposal**

In relation to the criteria for evaluation of the law reform in Hong Kong, it should be noted that there are no universal criteria for law reform, and the said criteria can only be established in accordance with the surrounding circumstances of each area of law. In summary, there are two general criteria that can be observed in this thesis.

The first criterion is that the reform aims to ensure fairness to both parties to an insurance contract. It should be noted that there is no definite answer as to what amounts to fairness. As Lord Bingham put it, fairness means “fairness to both sides, not just one”<sup>35</sup> and “fairness is a constantly evolving concept, not frozen at any moment of time”.<sup>36</sup> As far as the duty of utmost good faith is concerned, the concept of fairness is rarely defined by practitioners and judges. For instance, the word fairness was mentioned in the Law Commission reports but it was not referred to in the context of utmost good faith.<sup>37</sup> In “*Arnould: Law of Marine Insurance and Average*”, the word fairness was mostly referred to as “fairness of presentation”, which is also irrelevant to the discussion of the concept of fairness in law reform.<sup>38</sup> In “*MacGillivray on Insurance Law*”, the test of fairness was mentioned in the context of consumer insurance only, which is inapplicable to this thesis as it examines the reform of commercial insurance.<sup>39</sup> In *WISE Ltd. v. Grupo Nacional Provincial S.A.*,<sup>40</sup> Lord Justice Rix mentioned that the duty of utmost good faith applied to both the assured and the insurer based on “the notion of fairness”, but there was no further discussion about how the notion could be assessed.<sup>41</sup> The only relevant discussion about fairness can be found in *Colinvaux & Merkin's Insurance Contract Law*, where the word fairness was referred to as follows:-

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<sup>35</sup> Tom Bingham, *The Rule of Law*, Penguin Books (2011), page 90

<sup>36</sup> *ibid* page 91

<sup>37</sup> See, for example, Law Commission, *Insurance Contract Law: The Business Insured's Duty of Disclosure and the Law* (Law Com CP No 204), para 11.12

<sup>38</sup> Jonathan Gilman, Mark Templeman, Claire Blanchard, Philippa Hopkins and Neil Hart (eds), *Arnould: Law of Marine Insurance and Average* (19th edn, Sweet & Maxwell 2018) para 16-127

<sup>39</sup> John Birds, Simon Milnes; Ben Lynch, *MacGillivray on Insurance Law* (14th ed Sweet & Maxwell 2018) Para 18-050

<sup>40</sup> *WISE Ltd. v. Grupo Nacional Provincial S.A.* [2004] Lloyd's Rep IR 764 [64]

<sup>41</sup> *ibid*

A number of early cases referred to the duty requiring each party to adhere to comply with fairness, reasonableness and community standards of decency and fair dealing, so that honesty was not the limit of the duty but rather that utmost good faith imposed a market standard of fairness based on what was customary and acceptable conduct in the insurance market.<sup>42</sup>

In this passage, the concept of fairness was defined based on the insurance market standard, but again, there was no further discussion on how the market standard was established. Since there is no framed concept of fairness in the context of utmost good faith, the author suggests that in this thesis, the concept of fairness, for the purpose of reforming insurance law in Hong Kong, is simply a concept that is not contrary to common sense and the observations of Lord Bingham. One of the literal meanings of fairness is that “Impartial and just treatment or behaviour without favouritism or discrimination”.<sup>43</sup>

It is noteworthy that this thesis is focusing on fairness in the specific context, and it is not seeking to develop a jurisprudential account of fairness. As far as the reform in Hong Kong is concerned, the concept of fairness will be assessed by three questions. The first question is about whether both parties to an insurance contract are subject to the same standard of requirement under the law. In a case where the answer to the first question is negative, then the next question to be asked is whether there is any justifiable reason for such an asymmetric treatment. If the answer to the second question is also negative, then such a legal requirement is regarded as unfair and thus, a solution should be imposed to ensure fairness. The final question to be asked is whether the remedies imposed under the duty of utmost good faith/fair presentation are proportionate to the loss of the suffered party. A detailed discussion of the concept of proportionality is included in chapter 4(II) of this thesis where the meaning adopted for proportionality is that the remedy has not over- or under-compensated the loss suffered by the innocent party.

The second criterion of the law reform, which is proposed in this thesis, aims to ensure that the law is accessible. Again, as far as utmost good faith is concerned, the concept of accessibility

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<sup>42</sup> Robert Merkin, Colinvaux & Merkin's Insurance Contract Law (Sweet & Maxwell, 2019) para A-0654

<sup>43</sup> Oxford dictionaries, <<https://en.oxforddictionaries.com/definition/fairness>> accessed on 30 March 2019

is rarely discussed in the context of law reform. Nevertheless, under the Insurance Act 2015, the duty of fair presentation requires the assured to present the risk to the insurer in a reasonably clear and accessible manner. According to the Law Commission, there are two ways to ensure that the disclosed materials are clear and accessible. First, the information must be organised appropriately and the important part of the information should be highlighted. Second, there should be an overview and a summary for the information.<sup>44</sup> It is suggested that the same logic applies to the question of whether the law in relation to utmost good faith is accessible. The law is only accessible when the reader is able to understand and observe the relevant legal requirements easily.

In this thesis, two main reasons have been identified for an argument that, as currently stands, the law explaining the principles of the duty of utmost good faith is not easily accessible. Firstly, the scope and meaning of the duty itself are difficult for a reasonable man to read and understand and secondly, the duty itself has some grey areas that are in need of clarifications. An example of the former problem is section 18(1) of the MIA 1906/MIO, where it requires the assured to disclose material circumstances that would affect the mind of a prudent insurer in the risk assessment. By reading the provisions as well as case law, it is unlikely that the reader, who has no knowledge of insurance law, will be able to understand and comply with the “prudent insurer test”.<sup>45</sup> An example of the grey area of the duty of utmost good faith is the inducement test of the duty of disclosure. The said test was not mentioned in the legislation since 1906, but it was implied by the case law *Pan Atlantic Insurance Co. Ltd v Pine Top Insurance Co. Ltd*<sup>46</sup> in 1995. While the material test is expressly stated in the legislation, the inducement test is still absent from the MIA 1906/MIO and thus, a clarification is needed for the purpose of consistency with regards to the sources of the materiality and inducement tests.

To sum up, the reform that is proposed by this thesis aims to ensure that the law in Hong Kong is fair and accessible. The concept of accessibility and fairness are two sides of the same coin. They can be viewed independently, but they are also interrelated. If the law is inaccessible to the assured, it can also be unfair to the assured, because due to the inaccessibility, the assured

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<sup>44</sup> Law Commission (n4) para 7.44

<sup>45</sup> The detail of the prudent insurer test will be examined in chapter 2 of this thesis.

<sup>46</sup> *Pan Atlantic Insurance Co. Ltd v Pine Top Insurance Co. Ltd* [1994] 3 Lloyd's Rep IR 101

is deprived of the right to understand and to comply with the law. Therefore, it is suggested that both fairness and accessibility should carry the same weight in evaluating law reform in Hong Kong. As highlighted by Lord Bingham in his book *The Rule of Law*:

It is that the successful conduct of trade, investment and business generally is promoted by a body of accessible legal rules governing commercial right and obligations. No one would choose to do business, perhaps involving large sums of money, in a country where the parties rights and obligations were vague and undecided.<sup>47</sup>

Lord Bingham then cited Lord Mansfield's judgment in *Hamilton v Mendes*<sup>48</sup> to support his view that the commercial rules should always be "easily learned and retained".<sup>49</sup> This is, however, not the case for the duty of utmost good faith in Hong Kong. The current duty of utmost good faith is insurer-friendly, and the duty cannot be easily understood by people who have no knowledge about insurance law. These are potential factors that may discourage assured from all over the world to purchase commercial insurance in Hong Kong. By reforming the duty of utmost good faith in Hong Kong, it is suggested that the duty will be more customer friendly and accessible, which may be positive factors to attract foreign businesses to invest in Hong Kong.

## **B. Methodology of the anonymous online survey**

In relation to the Hong Kong survey result that is discussed in chapter 6 of this thesis, there were total 19 participants who gave their valuable responses to the reform of the duty of utmost good faith in Hong Kong. The survey was conducted from a distance through using online facilities. The participants were chosen from academia, insurance lawyers and practitioners from insurance broking firms and insurance companies. The selection was random in the sense that it was a non-statistically random selection of respondents rather than the mathematically random selection of participants in social research methodology.<sup>50</sup> Due to the limitation of cost and time, this survey does not aim to achieve "statistical generalisation", and thus the frame of the survey is not based on a representative sample but on a probability sample, which aims to

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<sup>47</sup> Bingham (n35) page 38

<sup>48</sup> (1761) 2 Burr 1198

<sup>49</sup> *ibid* 1214

<sup>50</sup> For the details of social survey random sampling method, see T May, *Social Research: Issues, Methods and Process*, Open University Press (2011), page 99



achieve “analytic and logical generality”.<sup>51</sup> The advantage of this survey method is that it saves the time and cost of both the author and the respondents in comparison to other types of survey.

The shortcoming of this survey is that, due to the limitation of time and cost, the sample size is small and the survey sample is random. It may be questioned why all respondents were asked the same set of questions. It is also arguable that academics are not practitioners and thus, they should not be included in the survey. The reasons why academics are chosen in this survey is that, first, it is not uncommon that legal academics will have practical experiences. Even if some of them have no experiences in practice, their views are still valuable as they may conduct research on the subject matter. Every participant’s contribution therefore is equally valuable to reflect their understanding of how the principles of the duty of utmost good faith operate. Additionally, the survey included interviewing a number of lawyers whose area of expertise is not only insurance but generally commercial law.

The questionnaire has also included an answer of “Other (please specify)” for practice related questions, where the respondents can specify their reasons in the answer when the questions are not applicable to their own situation. It is noteworthy that the intended effect of this survey is to serve as a reference to crosscheck the reform suggestion that is made in this thesis. The survey itself is not intended to carry any weight and the survey result is by no means representative.

## **V. Outcomes**

It follows that this thesis identifies the following problems:

- The problems of the MIO in Hong Kong regarding the duty of utmost good faith
- The problems of the IA 2015 in England and Wales regarding the duty of fair presentation
- Whether the model of the IA 2015 in England and Wales should be adopted in Hong Kong, with a particular emphasis on the duty of fair presentation

The key recommendations for reform to address these problems are:

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<sup>51</sup>ibid page 223

- In relation to section 18(1) of the MIO, the author suggests that the current approach for knowledge requirement of the assured should be replaced by the new “actual assured” approach
- The author also suggests that a new duty of reasonable search should be imposed on both the insurer and the assured
- In relation to section 18(2) of the MIO, the author suggests that the materiality test should be reformed from the prudent insurer test to the new “third-way” test
- The author also suggests that clear guidance should be provided for the test of actual inducement and presumption of inducement
- In relation to section 20 of the MIO, the author suggests that clear guidance should be provided for the application of the materiality and inducement tests in the case of misrepresentation
- The author suggests that the Misrepresentation Ordinance should not be applicable to utmost good faith cases
- The author suggests that the jurisdiction of section 17 of the MIO should be separated from section 18, 19 and 20 of the MIO
- In relation to the remedy of section 17, the author suggests that a new remedy of damages should be introduced as an alternative remedy to the remedy of avoidance
- In relation to the remedy of breaching the duty of fair presentation at the pre-contractual stage, the author suggests that new proportionate remedies should be introduced in Hong Kong
- The author suggests that section 19 should be eliminated and the agent’s duty of disclosure should be governed by section 18 of the MIO
- The draft bill of the new Marine Insurance Ordinance for the reform of the duty of utmost good faith/fair presentation in Hong Kong will be attached in Annex 5 of this thesis

# Chapter 1 The Knowledge Requirement Of The Duty Of Disclosure

In this chapter, the scope of knowledge that is required to be disclosed by the assured under the duty of disclosure (the knowledge requirement) will be analysed as the said requirement indicates the scope of the duty of disclosure.<sup>52</sup> The definition of the term “knowledge” is stated in section 18(1) of the MIO, which provides that:

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.<sup>53</sup>

The assured is bound by this section to disclose the actual or deemed knowledge to the insurer at the pre-contractual stage. It is submitted that the definition of the term “knowledge” indicates the ambit of the duty, with the exception that the assured is not required to disclose anything that the insurer already knows or is presumed to know, as stated in section 18(3)(b) of the MIO:

(3) In the absence of inquiry the following circumstances need not be disclosed, namely-

(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 his business, as such, ought to know.

It is submitted that there are two major problems for the above-mentioned knowledge requirements for the duty of disclosure. The first problem regards the identification of the person who is subject to the knowledge requirement under section 18(1) of the MIO. This problem is unique in commercial insurance law, when a group of people in a company is at stake rather than an individual person. This problem does not arise in consumer insurance cases, as the

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<sup>52</sup> It is noteworthy that the problem of knowledge requirement may also exist in other areas of the law, nevertheless, this chapter will only focus on the said requirement with respect to the doctrine of utmost good faith in insurance law.

<sup>53</sup> According to section 19(a) of the MIO, an agent of insurance contract is also subject to the knowledge requirement and the implication of it will be considered in chapter 5 of this thesis.

assured is the person who is referred to as the assured in the insurance contract, and the state of mind of that particular person will be subject to the knowledge requirement. In the context of commercial insurance cases, the knowledge requirement of the insurer is also clear. It is the actual underwriter, who is responsible for the risk assessment, that is subject to the knowledge requirement under section 18(3)(b) of the MIO. In relation to section 18(1) of the MIO, it is submitted that the knowledge requirement of the assured is problematic. The immediate question that arises is whose state of mind in an assured company should be examined under the law? The legislation and case law have not provided a clear answer to this question. As such, it is almost impossible for an assured company to comply with the duty of disclosure, as the knowledge requirement is too wide to start with.

The second problem of the knowledge requirement regards the definition of the term “deemed knowledge”. At present, the transition of knowledge is more complicated than the time when such a requirement was imposed. Information can now be acquired through computers and the internet without boundaries, but the knowledge requirement of the assured has not embraced the change of the modern technologies. In this regard, there is a necessity to clarify and redefine the meaning of “deemed knowledge”.

This chapter will be divided into two sections to examine the above-mentioned problems. The first section considers the identification of who is subject to the duty of disclosure under section 18(1) of the MIO. An analogy will be made between the knowledge requirement of the assured and the insurer to identify the problem of the assured’s duty of disclosure. The characteristics of a hypothetical person in an assured company, who is subject to the assured’s duty of disclosure, will be identified to demonstrate that the scope of the duty of disclosure is too broad to be complied with; and that the knowledge requirement of the assured is inconsistent with the prevailing business practices in the insurance industry. At the end of this section, a reform suggestion will be made, namely the “actual assured” approach should be adopted for the knowledge requirement of the assured under section 18(1) of the MIO.

The second section considers the problem of the definition of the “deemed knowledge” under section 18(1) of the MIO. Case law in England and Hong Kong suggest that there is no clear definition as to what amounts to the knowledge that is deemed to be known by the assured and

the insurer. The IA 2015 has imposed additional duties on the assured, but the new duties does not clarify the meaning of the “deemed knowledge”. In particular, the new requirement on the assured's part to present the risk in a “clear and accessible” manner remains vague. For the new duty of reasonable search introduced under the IA 2015, it is arguably too wide in scope, rendering it difficult, if not impossible for the assured to comply with it. At the end of the second section, a reform suggestion is made to redefine the meaning of the “deemed knowledge”. It is suggested that a new duty of reasonable search should be introduced to reframe the scope of the “deemed knowledge” requirement.

**I. The first problem of the knowledge requirement - the identification of the person who is subject to the knowledge requirement**

Contrary to the knowledge requirement of the assured, it is suggested that the knowledge requirement of the insurer, which is governed by section 18(3) of the MIO, is not problematic. In most of the cases, it is evident that the actual underwriter, who has taken part in the process of risk assessment, is subject to the knowledge requirement. In *Synergy Health (UK) Ltd v CGU Insurance Plc and Others*,<sup>54</sup> this case concerned a fire risk, and the insurance contract contained a risk improvement clause. One of the issues was whether the insurer was deemed to know, under section 18(3)(b) of the MIA 1906, that the fire alarms had not been installed in the assured premises. The assured alleged that since the specifications of the fire alarms were not disclosed to the insurer, the insurer should have noticed that the fire alarms were not installed in the premises. The court examined the evidence submitted by the actual underwriter, in this case Mr. Smith, and held that the insurer did not know or was not deemed to know that the fire alarms were not installed, as it was not a normal practice for the assured to comply with the risk improvement clause and submit the fire alarms specifications to the insurer for approval.<sup>55</sup>

Although the language of section 18(3)(b) of the MIO does not explicitly provide for whose knowledge is subject to the requirement, the above-mentioned case law suggests that it is the underwriter of the insurance company who is subject to the knowledge requirement. The author refers this approach as the “actual underwriter” approach, and it is certain that this approach is

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<sup>54</sup> *Synergy Health (UK) Ltd v CGU Insurance Plc and Others* [2011] 1 Lloyd's Rep. IR 500

<sup>55</sup> *ibid* [181]-[182]

easy to observe and follow by the insurance company. However, the only problem with the current knowledge requirement of the insurer is that the language of the legislation does not explicitly identify the exact person who is subject to the requirement under section 18(3)(b) of the MIO, it is suggested that the impact of such a problem is minimal.

Nevertheless, the situation is more complicated when one needs to determine whose knowledge is subject to the requirement in an assured company in relation to section 18(1) of the MIO, as it is almost impossible for the assured to identify the particular person who is responsible for disclosing both actual and deemed knowledge to the insurer. In this context, actual knowledge means the fact or information that is attributed to the assured company.<sup>56</sup> In *Group Josi Re v Walbrook Insurance Co. Ltd. and Others*,<sup>57</sup> Saville L.J. explained the actual knowledge of a corporation as follows:

A corporation is a legal abstraction to which the law attributes acts, omissions and states of mind of natural persons. Thus if the law attributes the knowledge of a natural person to a corporation, then in law the corporation has that knowledge, and not merely deemed or constructive knowledge.

In general, the actual knowledge of a company is attributed by the employee of the company. In *Brit UW Ltd v F & B Trenchless Solutions Ltd*,<sup>58</sup> this case concerned the non-disclosure of a void under the insured construction site. The existing of the void was known by the commercial director and managing director of the company and thus, it was the actual knowledge of the assured company.<sup>59</sup> In *A C Ward v Catlin (Five)*,<sup>60</sup> this case concerned the non-disclosure of fact that the security system of the insured warehouse was not functioning. The court examined the witness statement of the managing director of the warehouse and concluded that the assured company had no actual knowledge of the malfunction of the security system.<sup>61</sup>

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<sup>56</sup> Peter MacDonald Eggers, Simon Picken and Patrick Foss, *Good Faith and Insurance Contract* (3rd edn. Informa 2010) paras 7.93 - 7.96

<sup>57</sup> *Group Josi Re v Walbrook Insurance Co. Ltd. and Others* [1996] 5 Lloyd's Rep IR 91

<sup>58</sup> *Brit UW Ltd v F & B Trenchless Solutions Ltd* [2016] Lloyd's Rep. IR 69

<sup>59</sup> *ibid* [143] – [145]

<sup>60</sup> [2010] Lloyd's Rep IR 695

<sup>61</sup> *ibid* [188]. However, the claim was still rejected by the insurer on the ground of failure to comply with the Endorsement 6.

On the contrary, deemed knowledge means the knowledge that may not be known by the assured, but the assured is presumed and deemed to know the fact or information in the ordinary course of business.<sup>62</sup> In *Sea Glory Maritime Co, Swedish Management Co SA v AL Sagar National Insurance Co (The M/V Nancy)*,<sup>63</sup> it was held by the court that the shipowner and manager were not deemed to know the “U-turn” transaction policy in the United States. The relevant rules were frequently changed and the assured would not have deemed knowledge about the changes in the ordinary course of business.<sup>64</sup>

Similarly, in *ERC Frankona Reinsurance v American National*,<sup>65</sup> this case concerned a non-disclosure of the conviction record of the placing broker. The court held that the responsible person of the reinsured risk should have known that the underwriting agent’s previous conviction record or even he did not know that, he was deemed to know of it as in the ordinary course of business, he would have obtained the concealed information from the underwriting agent and would have aware of the conviction record.<sup>66</sup>

It is suggested that section 18(1) is problematic because companies may have different practices in obtaining insurance covers. For companies that obtain employee compensation insurance only, the process of the disclosure may be handled by the human resources department. For large international companies, the insurance arrangement may be handled by their own insurance department. Therefore, it may be unfavourable to identify the actual assured who should be responsible to satisfy the knowledge requirement under the legislation, as the application of the said requirement depends on the individual circumstances in each case.<sup>67</sup>

Nevertheless, the root cause of the above-mentioned problem can be found in *Group Josi Re v Walbrook Insurance Co. Ltd. and Others*,<sup>68</sup>

where Saville L.J. explained the knowledge requirement of a co-operated assured as follows:

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<sup>62</sup> Eggers, Picken and Foss, (n56) paras 7.93 - 7.96 and 7.118

<sup>63</sup> *Sea Glory Maritime Co, Swedish Management Co SA vs AL Sagar National Insurance Co (The M/V Nancy)* [2014] 1 Lloyd’s Rep 14

<sup>64</sup> *ibid* [309]

<sup>65</sup> *ERC Frankona Reinsurance v American National Insurance* [2006] 1 Lloyd’s Rep IR 157

<sup>66</sup> *ibid* [120]

<sup>67</sup> Gilman, Templeman, Blanchard, Hopkins and Hart (n38) para16-06

<sup>68</sup> *Group Josi* (n57)

In the case of a corporation the test is again whether there are natural persons who ought in the ordinary course of business to know the material circumstances and whether the deemed (i.e. constructive) knowledge of those persons is to be attributed to the corporation.<sup>69</sup>

Thus, a company assured is treated as a “legal person” under the law, and thus the whole company is required to disclose both actual and deemed knowledge to the insurer. The literal meaning is that all the people in the company can be potentially subject to the knowledge requirement, and hence, it may be a vain attempt to identify a single person who is subject to the requirement. Nevertheless, the identification of the characteristics of such a hypothetical actual assured is still necessary, as such characteristics are significant in ascertaining the scope of the knowledge requirement of the assured.

#### **A. The actual person who is subject to the duty of disclosure in an assured company**

To examine the problem of whose knowledge is subject to the requirement in an assured company, the author would like to make a presumption that there is always a hypothetical person, namely the actual assured, who is responsible for the arrangement of insurance for his or her own company. This concept is derived from the “actual underwriter” approach, which has been identified in the previous sub-section.

The first characteristic of this actual assured can be found in an English case *PCW Syndicates v PCW Reinsurer*,<sup>70</sup> where Lord Justice Staughton discussed the knowledge requirement as follows:

By s.18 the person seeking insurance must first disclose what is known to him. If he is a natural person, that means known to him personally; if a company, known to a director or any employee at an appropriate level. Secondly, the person must disclose everything which in the ordinary course of business ought to be known to him.<sup>71</sup>

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<sup>69</sup> *ibid*

<sup>70</sup> *PCW Syndicates v PCW Reinsurers* [1995] 4 Lloyd's Rep IR 373

<sup>71</sup> *ibid* 378



The first characteristic, as suggested by Lord Justice Staughton, is that the actual assured should possess both the actual and deemed knowledge of a director or any personnel at an appropriate level, and the responsible person is obligated to disclose any knowledge that is ought to be known to him or her in the ordinary course of business. Although Lord Justice Staughton did not give a definite meaning of “any employee at an appropriate level”, he suggested that the responsible person may not be “the directing mind and will” of the company.<sup>72</sup> In other words, the actual assured needs to possess the material knowledge of all personnel at different levels, no matter high or low, to comply with the knowledge requirement.

Lord Justice Staughton also suggested that the actual assured need not be restricted to any particular staff in the company.<sup>73</sup> His Lordship referred to an English case *Tesco Stores Ltd v Brent London Borough Council*<sup>74</sup> for determining the scope of knowledge of a company. In this case, the cashier of a supermarket had sold a video to a customer who was at the age of fourteen. However, the video was not allowed to be sold to any customer who was below eighteen years old. The supermarket was convicted of an offence under section 11(1) of the Video Recordings Act 1984. The defendant raised a defence that the fraud was committed by the cashier, the knowledge of which was not imputed to the “directing mind” of the supermarket. The court rejected the argument of the defendant and held that the supermarket was liable for the offence, even though the senior management did not aware of the fraud.<sup>75</sup>

The above-mentioned case has illustrated the rationale behind the judgment of Lord Justice Staughton that the relevant state of mind, that is examined under the duty of disclosure, may not be the state of mind of senior management in an assured company. In some cases, however, the state of mind of senior management can also be examined under the duty of disclosure. For example, in *Group Josi*,<sup>76</sup> it was the knowledge of the three company directors which was subject to the knowledge requirement.<sup>77</sup> Therefore, to identify the actual person who is subject to the knowledge requirement, one must examine the actual circumstances of each case carefully.

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<sup>72</sup> *ibid*

<sup>73</sup> *ibid* 377-378

<sup>74</sup> *Tesco Stores Ltd v Brent London Borough Council* [1993] 1 W.L.R. 1037

<sup>75</sup> *ibid* 1044 - 1045

<sup>76</sup> *Group Josi* (n57)

<sup>77</sup> *ibid* 100-101

The above analysis shows that there is no definite answer as to who, in an assured company, is subject to the knowledge requirement. Nevertheless, it is suggested that the hypothetical actual assured is more likely to be a member of senior management rather than a staff in junior level, as the knowledge of a director is always relevant to the requirement, and he or she is more likely to have the access to all levels of information in a company. In this regard, it is suggested that the hypothetical actual assured is more likely to be a senior member of staff, in particular a company director.

The second characteristic of the actual assured, however, is likely to be contradictory to the first characteristic of the actual assured. The said characteristic provides that the actual assured does not need to possess any knowledge which concerns the fraud of its own agent or officer. This characteristic is based on the Hampshire Land principle. This principle is derived from an English case *Re Hampshire Land Company*,<sup>78</sup> and the general definition of the principle in the context of insurance law is provided as follows:

English law has long recognised that even if the relationship between the principal and agent is such that the agent's knowledge is that of the principal, there is no attribution of knowledge that the agent has defrauded the assured, as it cannot be expected that the agent will inform the assured of his wrongdoing and accordingly the assured is not aware of such fraud in the ordinary course of business.<sup>79</sup>

Nevertheless, this principle also applies to cases where the fraud is committed by an employee of the assured company. In *Re Hampshire Land Company*,<sup>80</sup> the company directors incurred a debt on behalf of their company without obtaining ratification from the shareholders. The issue, in this case, was whether the company would be deemed to know the fraud of the directors when the company was itself the victim of the fraud. The court held that the knowledge of the director was not imputed to the company as the principle was applicable to the common agent. The rationale behind this exception was that ".....because common sense at once leads one to the conclusion that it would be impossible to infer that the duty, either of giving or receiving

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<sup>78</sup> *Re Hampshire Land Company* [1896] 2 Ch. 743

<sup>79</sup> Merkin (n42) para A-0739

<sup>80</sup> *Re Hampshire Land Company* (n79)

notice, will be fulfilled where the common agent is himself guilty of fraud.”<sup>81</sup> Therefore, the second characteristic suggests that the actual assured is unlikely to be a company director or a member of senior management, because in that situation where a director is responsible for the arrangement of insurance cover, he or she is no doubt liable to disclose all material knowledge to the insurer, including his or her own fault which is related to the insured risk, in order to comply with the duty of disclosure. In this regard, it is suggested that the actual assured can only be a person other than the company director, for example, an agent to insure of the assured company.

To sum up, the first and second characteristics of the actual assured have exposed the problems of the knowledge requirement of the assured. In theory, it is impossible for any person of a company to possess information of all levels of staff unless it is a one-man company. It is also impractical to apply the Hampshire Land principle on top of the first requirement, as one would not expect the law to allow a person, who can possess all levels of knowledge of a company, to conceal the fraud which is relevant to the insured risk. The exception to the Hampshire Land principle, as the author can think of, is also that the assured company is a one-man company. The current legislation, in this regard, is inconsistent with the modern business environment. The scale and structure of companies nowadays are more complicated than the old times when the MIA 1906 was drafted and enacted. The knowledge requirement operates efficiently if the assured company is a one-man company, or a small-scale company. However, the requirement falls short when the company is a large-scale international company, as it is impossible for a single staff to gather all employees’ knowledge.

Furthermore, the knowledge requirement may also underestimate the complication of how knowledge is transferred within a company. For instance, if the staff, who is responsible for the arrangement of insurance, is not a director, he or she may not be able to possess the material knowledge of the director. It can be argued, and relevant points were also raised in the House of Lords discussion, that the staff can request the director to provide the relevant information that is requested by the insurer,<sup>82</sup> however, in that situation, the staff may not have sufficient knowledge to judge the accuracy of the disclosed knowledge from the director. In this regard, it

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<sup>81</sup> *ibid* page 749

<sup>82</sup> See, for example, House of Lords, Special Public Bill Committee, *Insurance Bill (HL)*, HL paper 81, page 61-62, Q37

is submitted that the lawmaker has underestimated the difficulty of collecting relevant information within a company, and the knowledge requirement places the assured at a disadvantaged position to comply with the duty of disclosure.<sup>83</sup> In addition, the accessibility of this area of law may also be a problem. As a layman of insurance law, it is highly unlikely that the assured will be able to correctly observe and understand the complicated knowledge requirement, and it thereby causes undue hardship to the assured in complying with the requirement. In this regard, it is submitted that the knowledge requirement of the assured is in need of reform, and the question to be considered then is how the reform should be introduced.

**B. The IA 2015 has not identified the actual person who is subject to the duty of disclosure in an assured company**

It is submitted that one of the possible ways of reforming the knowledge requirement is to adopt the model of the IA 2015. The question is whether the IA 2015 has successfully solved the above-mentioned problem. Under the MIA 1906, there were basically three parties who were subject to the knowledge requirement, namely, the insurer, the assured and the agent of the assured. Under the IA 2015, the agent of the assured no longer owes any independent duty under the new duty of fair presentation.<sup>84</sup> Instead, such a duty is now imposed on the assured to disclose any material information, which is possessed by the agent regarding the risk, to the insurer.<sup>85</sup> It is noteworthy that the scope of the knowledge requirement of the assured's agent, under the IA 2015, is almost identical to the old duty under the MIA 1906, except that the IA 2015 excludes the assured from disclosing any information obtained by the agent from a party that is irrelevant to the insurance contract.<sup>86</sup> In other words, there are now only two parties who are subject to the knowledge requirement under the IA 2015, namely the insurer and the assured.

With regard to the problem of whose knowledge is subject to the requirement in an insurance company, section 5(1) of the IA 2015 states that:

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<sup>83</sup> Similar point of view can be found in Law Commission (n37) para 6.68

<sup>84</sup> Explanatory Notes to Insurance Bill 2015 (n29) para 60

<sup>85</sup> The Insurance Act 2015, section 4(3)(b)

<sup>86</sup> The Insurance Act 2015, section 4(4)(b) provides that "the information was acquired by the insured's agent (or by an employee of that agent) through a business relationship with a person who is not connected with the contract of insurance."

For the purposes of section 3(5)(b), an insurer knows something only if it is known to one or more of the individuals who participate on behalf of the insurer in the decision whether to take the risk, and if so on what terms (whether the individual does so as the insurer's employee or agent, as an employee of the insurer's agent or in any other capacity).

Comparing this section with section 18(3)(b) of the MIA 1906, it is certain that section 5(1) of the IA 2015 has adopted the "actual underwriter" approach. The new section has explicitly provided that it is the actual underwriter who is subject to the requirement, which has solved the problem that has been identified in the previous sub-sections.

The problem of whose knowledge is subject to the requirement in an assured company still remains complicated in the IA 2015. Section 4 of the IA 2015 has defined the scope of the knowledge requirement for both individual and non-individual.<sup>87</sup> Section 4(2) provides for the scope of knowledge for the individual:

An insured who is an individual knows only—

- (a) what is known to the individual, and
- (b) what is known to one or more of the individuals who are responsible for the insured's insurance.

Section 4(2)(a) reflects the legal position of an individual assured before the enactment of the IA 2015,<sup>88</sup> but section 4(2)(b) has expanded the scope of the knowledge requirement to include those who are also responsible for the arrangement of the insurance. Similarly, section 4(3) provides the scope of the knowledge requirement for the non-individuals that:

An insured who is not an individual knows only what is known to one or more of the individuals who are—

- (a) part of the insured's senior management, or
- (b) responsible for the insured's insurance.

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<sup>87</sup> In section 4 of the IA 2015, non-individual means company assured in commercial insurance case.

<sup>88</sup> The literal meaning of this section is in line with the judgment of *PCW Syndicates* (n71)

The meaning of the term “senior management”, which is stated in section 4(3)(a), can be found in section 4(8)(c)<sup>89</sup> and also the Explanatory Notes to the Insurance Bill 2015.<sup>90</sup> Nevertheless, the definition of the “senior management” in section 4(8)(c) has not clarified the knowledge requirement, but it has not created any adverse impact on the knowledge requirement either.

The problematic part of the IA 2015 lies in section 4(3)(b). Section 4(3)(b) requires the assured to possess the material knowledge of who are responsible for the insurance contract. Section 4(8) further elaborates the requirement in section 4(3)(b) as follows:

(b)an individual is responsible for the insured’s insurance if the individual participates on behalf of the insured in the process of procuring the insured’s insurance (whether the individual does so as the insured’s employee or agent, as an employee of the insured’s agent or in any other capacity).

The Explanatory Notes to the Insurance Bill 2015 has explained the rationale behind section 4(8) as follows:

Clause 4(8)(b) defines a person “responsible for the insured’s insurance”. It is expected to catch, for example, the insured’s risk manager if they have one, and any employee who assists in the collection of data or negotiates the terms of the insurance. It may also include an individual acting as the insured’s broker.<sup>91</sup>

It is argued that section 4(8) has imposed a wider scope for the knowledge requirement of the duty of disclosure in comparison to the same duty under the MIA 1906. This approach, however, defeats the purpose of reforming the knowledge requirement in Hong Kong. With the advancement of modern technologies, nowadays it is no longer necessary to impose a strict requirement on the assured to disclose information, as some of the information, which is required for risk assessment, may be found on the internet.<sup>92</sup> The insurer is no longer in an absolute unprivileged position of obtaining information which is related to the risk. Therefore, it

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<sup>89</sup> The Insurance Act 2015, section 4(8)(c) provides that “senior management” means those individuals who play significant roles in the making of decisions about how the insured’s activities are to be managed or organised.”

<sup>90</sup> Explanatory Notes to Insurance Bill 2015 (n29) para 53

<sup>91</sup> *ibid* para 54

<sup>92</sup> For example, see Merkin (n42), para A-0824 “In modern conditions.....information is almost certainly going to be available somewhere, generally online, and the question is whether the insurers themselves had ready access to the information.” It is noteworthy that both the MIA 1906 and the IA 2015 do not assume possession of knowledge through internet unless the database is subscribed by the parties to an insurance contract.

is submitted that the duty at the present moment should be more lenient on the assured than it was in the past.

Nevertheless, the IA 2015 has failed to rectify the knowledge requirement. It still remains unclear as to how an actual assured can possess the material knowledge of all levels of staff in a company. The new definition of the terms “senior management” in section 4(8)(c) only restates the legal position under the MIA 1906. Worse still, in addition to the original burden that requires the assured to possess the material knowledge of all levels of staff in a company, the assured is also required to possess and disclose the knowledge of its agent under the IA 2015.

The author doubts that the actual assured is capable of possessing the knowledge of its agent, as in most cases, the assured and the agent belong to separate legal entities.<sup>93</sup> It is submitted that the lawmaker of the IA 2015 has underestimated the difficulty in gathering material information not only within the same company, but also the difficulty in gathering information from another company, which is even harder to perform than the former. Therefore, under the new duty of fair presentation of the IA 2015, it is highly unlikely that the assured can strictly comply with the duty. In this regard, it is submitted that Hong Kong should not adopt the reform model of the IA 2015, and it should implement a reform, which is independent from the IA 2015, on the knowledge requirement of the duty of disclosure.

**C. Formulating the reform for the knowledge requirement in relation to section 18(1) of the MIO – the “actual assured” approach**

**i. The reform strategy**

It is submitted that the current knowledge requirement under section 18(1) of the MIO is unclear as to who, in an assured company, is subject to the knowledge requirement. In *PCW Syndicates v PCW Reinsurer*,<sup>94</sup> Lord Justice Staughton expressed his opinion on this matter as follows:

It is sometimes said that a company can have no knowledge itself, and can only know things by its servants or agents; others say that there can be knowledge which is in

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<sup>93</sup> This issue will be further examined in chapter 5 of this thesis.

<sup>94</sup> *PCW Syndicates* (n71)

truth that of the company. I do not find it necessary to enter upon that debate (and if I did I would not know how to resolve it).<sup>95</sup>

The reason why Lord Justice Staughton found it unnecessary to address the problem was that the learned judge thought that section 18 was “carefully framed” to address the matters which were related to non-disclosure.<sup>96</sup> Nevertheless, as discussed in the previous sub-sections, the legal practitioners and also the legislators have failed to consider the problem from the perspective of the assured. The current duty of disclosure in Hong Kong requires the actual person, who is responsible for the arrangement of the insurance in an assured company, to possess the material knowledge of all levels of staff in order to comply with the duty. In contrast, section 18(3) of the MIO only concerns the state of mind of the actual underwriter, which suggests that the scope of the knowledge requirement on the assured side is much wider than the same requirement on the insurer side. Therefore, in order to maintain fairness between the parties to an insurance contract, it is suggested that the knowledge requirement on the assured side, with respect to section 18(1) of the MIO, should be in alignment with the same requirement on the insurer side in respect of section 18(3) of the MIO. This new reform suggestion is referred as the “actual assured” approach. In other words, under the new knowledge requirement, the only person, who is subject to the duty of disclosure, is the person that is responsible for the arrangement of the insurance in an assured company.

It may be argued that the reform can also be considered from a different perspective, which is requiring the insurer to adopt the approach in accordance with section 18(1) of the MIO, so that the whole insurance company, instead of the actual underwriter, will be subject to the knowledge requirement. This approach can also maintain fairness and unify the knowledge requirements between the assured and the insurer. Nevertheless, as identified in the above sub-sections, section 18(1) is unclear as to who should be subject to the knowledge requirement and therefore, it is unfavourable for the insurer to follow the approach of section 18(1) of the MIO.

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<sup>95</sup> *ibid* 377

<sup>96</sup> *ibid* 378



In contrast, it is favourable for the assured to adopt the “actual assured” approach. Apart from the issue of fairness, the new approach rectifies the problem of identifying the actual person who is subject to the knowledge requirement in the assured company. In this regard, it is easier for the assured to understand and comply with the requirement, in comparison with the original approach in section 18(1) of the MIO.

In other words, under the new “actual assured” approach, the material knowledge of the company director, senior managements and other staff are no longer relevant with respect to section 18(1) of the MIO, unless they are involved in the process of insurance arrangement. As criticised in the above sub-sections, it may not be feasible to include the state of mind of the company director in the knowledge requirement of the duty of disclosure, as he or she may not be involved in the process of underwriting. Therefore, the “actual assured” approach only concerns the material knowledge of the actual person who is involved in the process of insurance arrangement, and the state of mind of the senior management and other staff are only relevant when they are involved in the insurance arrangement process.

**ii. The solution – the amendment of section 18(1)**

To adopt the actual assured approach, the new section 18(1) should be amended as follows:

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 person who is responsible for the assured’s insurance (the actual assured), and the actual assured is deemed to know every circumstance which, in the ordinary course of business, ought to be known by him or her. If the assured fails to make such disclosure, the insurer may avoid the contract.

The new section 18(1) provides that the knowledge requirement of the assured is focused on the actual assured, who is the person that is responsible for the assured’s insurance. As discussed in the previous sub-section, this new provision rectifies the problem that the assured has to bear an unfair burden to disclose information that is out of his or her reach. The “actual assured” approach aims to redefine the scope of the duty of disclosure with regard to section 18(1). Under the new approach, it is easier for the assured to understand and comply with the duty of disclosure. The new approach also assists the legal practitioners to clarify the

uncertainty of the operation of the knowledge requirement. The judges only need to examine the state of mind of the actual assured who is responsible for the arrangement of the insurance in each case. In this regard, it is suggested that the “actual assured” approach also helps to ascertain the operation of the knowledge requirement for both the legal practitioners and also the assured with respect to section 18(1) of the MIO.

It is noteworthy that the adoption of the “actual assured” approach may lead to a major departure from company law in relation to the principle of “directing mind and will”. The said company law principle is sometimes referred to as “the identification doctrine”,<sup>97</sup> and it is used to “attribute an intention or actual default to the company.”<sup>98</sup> The very first case that explained the principle of “directing will and mind” was the case *Lennard's Carrying Company Limited v Asiatic Petroleum Company*.<sup>99</sup> This was a loss of cargo case where the loss was caused by a fire due to the unseaworthiness of the ship. The managing director of the managing owners knew that the ship was unseaworthy, but he did not inform the captain or the chief engineer to fix the problem. The issue was whether the managing director was liable for any actual fraud and privity under section 502 of the Merchant Shipping Act 1894. When explaining the principle of “directing mind and will”, Viscount Haldane L.C provided his observation as follows:-

...a corporation is an abstraction. It has no mind of its own any more than it has a body of its own; its active and directing will must consequently be sought in the person of somebody who for some purposes may be called an agent, but who is really the directing mind and will of the corporation, the very ego and centre of the personality of the corporation.<sup>100</sup>

Viscount Haldane L.C then held that the managing director was liable because he was in the role of managing the ship and thus, his non-disclosure of the unseaworthiness of the ship was the action of the company.<sup>101</sup> However, in *Meridian Global Funds Management Asia Ltd v Securities Commission*,<sup>102</sup> the responsible person was held to be the junior staff rather than a

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<sup>97</sup> David Kershaw, *Company Law in Context: Text and Materials*, (2012, second edition, Oxford University Press), p.139

<sup>98</sup> Birds, J. and Boyle, A. J. (eds), *Boyle & Birds' Company Law*, (2014, 9th edition, Bristol: Jordan Publishing), p.83

<sup>99</sup> *Lennard's Carrying Company Limited v Asiatic Petroleum Company* [1915] A.C. 705

<sup>100</sup> *ibid* 713

<sup>101</sup> *ibid*

<sup>102</sup> *Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 2 A.C. 500

senior staff as suggested in the *Lennard's Carrying* case.<sup>103</sup> A chief investment officer, who worked for an investment management company, purchased a large sum of shares in public issuers for the company without informing the directors. The issue was whether the company was liable for breaching the notice requirement under section 20(3) of the Securities Amendment Act 1988. The court held that the person, who was responsible for the notice requirement under the Securities Amendment Act 1988, should be the one who acquired the shares with the authority of the company, even the responsible person was not the senior management or director of the company.<sup>104</sup>

The *Meridian Global Funds Management Asia* case<sup>105</sup> is then considered to be the authority of the principle of “directing mind and will” and is applied in subsequent cases.<sup>106</sup> One of the recent examples is *Howmet Ltd v Economy Devices Ltd*.<sup>107</sup> This case concerned a device called “thermolevel”, which was used to prevent fire risk. A factory owner installed the device in his factory. The device did not function properly and as a result, the factory was eventually destroyed by a fire accident. The factory owner sued the manufacturer of the device for damages. One of the issues, in the case, was whether the factory owner knew that the device was malfunctioned. Lord Justice Jackson held that, in light of the judgement of *the Meridian Global Funds Management Asia* case,<sup>108</sup> the “directing mind and will” of the company was the maintenance team of the factory. Since all the maintenance team members knew that the device was malfunctioned, their knowledge would be attributed to the factory owner.<sup>109</sup> Therefore, one can see that the application of the principle of “directing mind and will” is a matter of context, and there is no general rule as to who is the “directing mind and will” of a company.

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<sup>103</sup> *Lennard's Carrying Company Limited* (n100)

<sup>104</sup> *Meridian Global Funds Management Asia* (n 103) 511

<sup>105</sup> *ibid*

<sup>106</sup> See, for example, *Bilta (UK) Ltd (In Liquidation) v Nazir* [2015] UKSC 23, [2016] A.C. 1, *Financial Conduct Authority v Da Vinci Invest Ltd* [2015] EWHC 2401 (Ch), 2015 WL 4744875, *Orr v Milton Keynes Council* [2011] EWCA Civ 62, 2011 WL 289967 and *Real Estate Opportunities Ltd v Aberdeen Asset Managers Jersey Ltd* [2007] EWCA Civ 197, 2007 WL 880932

<sup>107</sup> *Howmet Ltd v Economy Devices Ltd* [2016] EWCA Civ 847, 2016 WL 04446386

<sup>108</sup> *Meridian Global Funds Management Asia* (n 103)

<sup>109</sup> *ibid* [73]

The “directing mind and will” principle is also complicated by the use of anthropomorphic metaphor in case law. In *HL Bolton Engineering Co Ltd v TJ Graham & Sons Ltd*,<sup>110</sup> Lord Denning suggested that a company was similar to a human body with brain, nerve and hands.<sup>111</sup> He further held that:-

Some of the people in the company are mere servants and agents who are nothing more than hands to do the work and cannot be said to represent the mind or will. Others are directors and managers who represent the directing mind and will of the company, and control what it does. The state of mind of these managers is the state of mind of the company and is treated by the law as such.<sup>112</sup>

Such an approach is widely used in cases that involved the discussion of the principle of “directing mind and will” of a company. In *Tesco Supermarkets Ltd v Natrass*,<sup>113</sup> Lord Pearson suggested that “There are some officers of a company who may for some purposes be identified with it, as being or having its directing mind and will, its centre and ego, and its brains.”<sup>114</sup> In *Stone & Rolls Ltd (In Liquidation) v Moore Stephens*,<sup>115</sup> the question of “directing mind and will” was considered from the perspective of the “human embodiment” of a company.<sup>116</sup> Professor Susan Watson referred this approach as “organic theory”, and she criticised that such an approach did not take account of the external stakeholders, for instance external agents of the company, who may also be regarded as the “directing mind and will” of the company.<sup>117</sup>

The said approach was also criticised by Professor Eilís Ferran in her paper “Corporate Attribution and the Directing Mind and Will”. Professor Eilís Ferran criticised that although the *Meridian Global Funds Management Asia* case<sup>118</sup> had confirmed that the principle of “directing mind and will” was a matter of construction rather than anthropomorphism, judges and lawyers

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<sup>110</sup> *HL Bolton Engineering Co Ltd v TJ Graham & Sons Ltd* [1957] 1 Q.B. 159

<sup>111</sup> *ibid* 172

<sup>112</sup> *ibid*

<sup>113</sup> *Tesco Supermarkets Ltd v Natrass* [1972] A.C. 153

<sup>114</sup> *ibid* 190

<sup>115</sup> *Stone & Rolls Ltd (In Liquidation) v Moore Stephens* [2009] 1 A.C. 1391

<sup>116</sup> *ibid* [107]. It is noteworthy that this case is subject to heavy criticism and may not be authoritative. See, for example, *Bilta (UK) Ltd (In Liquidation) v Nazir* [2015] UKSC 23 [30], [48] and [81].

<sup>117</sup> Susan Watson, “How the company became an entity: a new understanding of corporate law”, J.B.L. 2015, Vol. 2, 120-141, p.137-138

<sup>118</sup> *Meridian Global Funds Management Asia* (n 103)

were still keen to use anthropomorphic metaphor to explain the “directing mind and will” principle.<sup>119</sup> Professor Eilís Ferran further criticised that such an approach “create trouble for ourselves if we try to resolve legal issues by treating a company as if it were a human being” and the rule based enquiry, which was confirmed in the *Meridian Global Funds Management Asia* case,<sup>120</sup> is the appropriate way to examine the “directing mind and will” of a company.<sup>121</sup>

Based on the above analysis, it is suggested that the “directing mind and will” principle is flexible but the scope of it is too wide. The use of anthropomorphic metaphor, in relation to the principle of “directing mind and will”, has also complicated the situation. In fact, when considering the reform of the duty of utmost good faith in England and Wales, the Law Commission also considered the problem of the “directing mind and will” of a company. The Law Commission commented that the scope of the “directing mind and will” was indefinite and the flexible approach caused considerable uncertainty.<sup>122</sup> The Law Commission also noticed that the principle of “directing mind and will” was not enough to cover all circumstances in relation to the duty of utmost good faith, and thus a special rule was required for the reform of this area of law.<sup>123</sup>

In comparison to the “directing mind and will” principle, it is suggested that the “actual assured” approach is easier to understand and follow. The “actual assured” approach identifies the responsible person who is subject to the duty of disclosure, which is more certain than the “directing mind and will” principle. The “actual assured” approach also requires the directors and senior managements to disclose material information when they are involved in the arrangement of insurance, which ensures that the duty is applicable to all levels of staff in a company. In this regard, it is suggested that the use of the “actual assured” approach may be more favourable for the Hong Kong law reform.

The potential problem of adopting the “actual assured” approach is that it may allow the assured to turn a blind eye to the information, which is not possessed by him or her personally,

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<sup>119</sup> Ferran, Eilís, *Corporate Attribution and the Directing Mind and Will* (2011). *Law Quarterly Review*, Vol. 127, pp. 239-259, 2011; University of Cambridge Faculty of Law Research Paper No. 5/2012, page 239-240

<sup>120</sup> *Meridian Global Funds Management Asia* (n 103)

<sup>121</sup> *ibid* page 258

<sup>122</sup> Law Commission (n4), para 8.10 and 8.14

<sup>123</sup> *ibid* para 22.26

but by other staff of the same company. Therefore, it is suggested that a new duty of reasonable search should also be imposed on the assured to prevent the non-disclosure of the “blind eye” knowledge of the assured.<sup>124</sup> Although the duty of reasonable search is a concept which is borrowed from the IA 2015, nevertheless, it is submitted that the reasonable search requirement will also be imposed on the insurer as a matter of fairness, and the new scope of it will be redefined in the following sections.

## **II. The second problem of the knowledge requirement – the vague definition of the term “deemed knowledge”**

### **A. The vague definition of the term “deemed knowledge” under the MIO**

The second problem of the knowledge requirement under the duty of disclosure concerns the definition of the term “deemed knowledge”. Under section 18(3)(b) of the MIO, the assured need not to disclose anything that is known or presumed to be known to the insurer. In *Garnat Trading & Shipping (Singapore) Pte Ltd v Baominh Insurance Corporation*,<sup>125</sup> the court underlined the test of the insurer’s knowledge as follows:

In the context, the test is objective. One asks what a reasonable insurer, writing the particular type or class of business concerned, would, or should, know. A reasonable underwriter is presumed to know matters which he should have known from the facts in his possession or matters which he had means of learning from the sources available to him. A reasonable underwriter is presumed to know the ordinary incidents or attributes of any peculiar or specialist risk he undertakes: every underwriter is presumed to be acquainted with the practice of the trade he insures; if he does not know, then he ought to inform himself. Because of these aspects, and absent inquiry by the insurer, only unusual elements affecting the risk have to be disclosed by the proposer.<sup>126</sup>

Particular attention should be drawn to the words “matters which he had means of learning from the sources available to him”. It is hard to identify what is available to a reasonable insurer in modern ages. For example, online publications are not classified as sources that available to a

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<sup>124</sup> The details of the duty of reasonable search will be discussed in the section II(C)(ii) of this chapter.

<sup>125</sup> *Garnat Trading & Shipping (Singapore) Pte Ltd v Baominh Insurance Corporation* [2011] 1 Lloyd’s Rep 589

<sup>126</sup> *ibid* [135]

reasonable insurer,<sup>127</sup> and thus do not fall within the category of section 18(3)(b). Again, the law has imposed a heavy burden on the assured to anticipate the mind of a reasonable insurer. In *Hua Tyan Development Ltd. v Zurich Insurance Co. Ltd.*,<sup>128</sup> Lord Neuberger expressed his view on the matter of the presumed knowledge:

The question of what an insurer is presumed to know in the course of underwriting marine insurance is not altogether a straightforward one and there is a long history of case law. For a quick reference to this area of marine insurance, one needs only to refer to leading textbooks on this subject matter.<sup>129</sup>

The judgment indicates that in the eyes of a judge, it is not easy to identify what is the scope of the insurer's knowledge requirement. Moreover, it is equally difficult for the assured to refer to leading textbooks as the subject matter itself is uneasy to understand. It indicates the actual difficulty for the assured to anticipate the insurer's knowledge.

Nevertheless, it is submitted that the most problematic part of the definition of the term "deemed knowledge" lies in the part of the assured's side. In relation to section 18(1) of the MIO, the requirement is described as an objective test with subjective element,<sup>130</sup> which suggests that it is neither an objective nor subjective test. The unclear nature of the test may lead to an unlimited scope of the requirement. In addition, the assured will not be able to observe the boundary of the requirement, as it is heavily relied upon the discretion of the judge to determine the scope of it.

Furthermore, there is no automatic formula as to what amounts to a "deemed knowledge" with regard to the duty of disclosure of the assured. It is suggested that the court may draw reasonable inferences from the characteristic of the subjected party in order to decide whether the concealed information is deemed to be known by the assured. In *Sea Glory Maritime Co, Swedish Management Co SA v AL Sagar National Insurance Co (The M/V Nancy)*,<sup>131</sup> the vessel of the assured was damaged and considered to be a constructive total loss due to a fire

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<sup>127</sup> Gilman, Templeman, Blanchard, Hopkins and Hart (n38) para 16-115

<sup>128</sup> *The Ho Feng* 7 (n16)

<sup>129</sup> *ibid* [57]

<sup>130</sup> Gilman, Templeman, Blanchard, Hopkins and Hart (n38) para 16-27

<sup>131</sup> *Sea Glory Maritime Co* (n63)

accident. The insurer rejected the claim on the ground that the assured failed to disclose several material information. One of the issues was whether the assured was deemed to know that a “U-turn” transaction for Iranian bank was forbidden in the United States.

In his judgment, Mr. Justice Blair stated that “I agree with the claimants that, as shipowners and ship managers, the question of their deemed knowledge can only be determined by considering the ordinary course of business in which they are involved.”<sup>132</sup> He further suggested that the deemed knowledge could only be proved by the witnesses who were the shipowner and the ship managers.<sup>133</sup> Based on the evidence from an underwriting expert, Mr. Justice Blair held that the assured was not deemed to know that the “U-turn” transaction was illegal in the United States, as the relevant rules had changed so frequently that it was unreasonable to expect the insurer or the claimant to trace the changes.<sup>134</sup>

From the above-mentioned judgment, one can observe that the judges are allowed to make reasonable inferences as to what is deemed to be known by the assured. Nevertheless, the legislation itself has not clearly define the scope of the “deemed knowledge”. It is suggested that the lack of certainty may lead to confusion of the application of the duty of disclosure. The example of the said confusion can be found in a Hong Kong case *Success Insurance Limited v George Kallis (Manufacturers) Limited*.<sup>135</sup> The respondent was a consignee of a cargo of denim material, which was planned to ship from Hong Kong to Limassol. The goods were lost due to the peril of the sea, and the respondent claimed against the appellant for the loss based on the insurance policy. The appellant refused to pay the claim and pleaded non-disclosure, as the consignee had not disclosed to the appellant the fact that the vessel, the name of which was stated in the bills of lading, did not reach Hong Kong and eventually the cargo was carried by another vessel. The appellant pleaded that the respondent should have known that the vessel did not reach Hong Kong, as the schedule of the vessel was advertised in the South China Morning Post. The appellant also pleaded that it was the common practices among the exporters in Hong Kong to check the schedule of the vessel when the shipping line was little known. In the Court of First Instance, it was held that the consignee was not in breach of the

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<sup>132</sup> *ibid* [307]

<sup>133</sup> *ibid* [307]

<sup>134</sup> *ibid* [309]

<sup>135</sup> *Success Insurance Limited v George Kallis (Manufacturers) Limited* CACV000133/1980



duty of disclosure, as the common practices that were established by the appellant were only applicable to large-scale organisations, and the respondent was not one of them.<sup>136</sup> Further, the court did not agree that the respondent had any ground to cast doubt on the arrangement of the carrier and hence, the respondent was not liable for non-disclosure.<sup>137</sup>

In the Court of Appeal, the three judges did not differ the judgment on the issue of non-disclosure, nevertheless, Cons, J.A. concluded his judgment with a criticism against the judgment of the first instance judge:

The learned Commissioner appears to have drawn a distinction between "large organizations" and others, in which presumably he put Wantex, when considering what is "the ordinary course of business". With respect I do not think he was entitled to draw that distinction. Nevertheless I am inclined to agree with my Lord Vice President and the Commissioner that Wantex were not under an obligation to investigate information from Seawise which, on the face of it, they had no reason to suspect.<sup>138</sup>

Nevertheless, if one refers to the judgment of the *Sea Glory Maritime Co*<sup>139</sup> case, it is suggested that the business nature of the assured company is one of the factors that needs to be considered when deciding whether a piece of information is deemed to be known by the assured. Therefore, it may be reasonable to suggest that the size of the assured company is also one of the factors that significantly affects the company practice, and thus, it should be taken into account when determining the deemed knowledge of the assured company. Nevertheless, the different opinions between the judge of the First Instance Court and the Court of Appeal in the *Success Insurance Limited*<sup>140</sup> case indicate that the current legislation is indefinite on the assessment of the deemed knowledge requirement, and therefore it is highly unlikely that the assured will be able to observe and then comply with the requirement. This problem also affects the assured when the material information can be obtained through computers and online technologies. The details of this problem will be analysed in the next sub-

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<sup>136</sup> *ibid* page 4

<sup>137</sup> *ibid* page 4

<sup>138</sup> *ibid* page 14

<sup>139</sup> *Sea Glory Maritime Co* (n63)

<sup>140</sup> *Success Insurance Limited* (n136)

section, as the IA 2015 has imposed several new provisions in order to embrace the advancement of modern technologies.

#### **B. The IA 2015 has not provided a definite scope for the disclosable knowledge**

With regard to the definition of the term “knowledge”, section 6(1) of the IA 2015 states that:

For the purposes of sections 3 to 5, references to an individual’s knowledge include not only actual knowledge, but also matters which the individual suspected, and of which the individual would have had knowledge but for deliberately refraining from confirming them or enquiring about them.

This section has not provided a clearer definition of the actual and deemed knowledge for both the assured and the insurer under the new duty of fair presentation. Nevertheless, it is suggested that on the one hand, the IA 2015 has narrowed the scope of the knowledge requirement of the insurer, but on the other hand, it has widened the scope of the deemed knowledge of the assured. Under section 18(3)(b) of the MIA 1906, the assured need not to disclose information that the insurer actually knows, ought to know or presumed to know. Whereas the IA 2015 has not provided further elaboration on the actual knowledge of the insurer, it has redefined the scope of the knowledge that an insurer ought to know and presumed to know.

Section 5(2) of the IA 2015 stipulates that the insurer ought to know two types of information. First, the insurer ought to know the information that is known by the employee and the agent of the insurer. In addition, this information ought reasonably to have passed to the actual underwriter.<sup>141</sup> Secondly, the insurer also ought to know the information which is possessed by the insurer, and it is readily available to the actual underwriter.<sup>142</sup> It is suggested that section 5(2) has now provided a clearer guidance on the knowledge that an insurer ought to know in relation to the duty of disclosure. Nevertheless, in comparison to the insurer’s knowledge requirement in the MIA 1906, the language of section 5(2) appears to have narrowed down the scope of the knowledge that an insurer ought to know.

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<sup>141</sup> The Insurance Act 2015, section 5(2)(a)

<sup>142</sup> The Insurance Act 2015, section 5(2)(b)

Section 5(3) of the IA 2015 stipulates that the insurer is presumed to know two types of information. First, the insurer is presumed to know the information which can be considered as a common knowledge.<sup>143</sup> Although the term “notoriety” in section 18(3)(b) of the MIA 1906 is omitted in the IA 2015, it is suggested that the requirement of knowing a common knowledge may already sufficiently cover the requirement of knowing a “notoriety”.<sup>144</sup> Secondly, the insurer is presumed to know the information which he or she will be expected to know in his ordinary course of business. It is suggested that under section 5(3), the insurer is only presumed to know the matters that are relevant to its class of business.<sup>145</sup> The Explanatory notes to the Insurance Bill 2015 has explained this section as follows:

Many underwriters work by class of business (such as property or professional indemnity insurance) rather than by industry sector (such as oil and gas). An insurer ought to have some insight into the industry for which it is providing insurance, but this insight may reasonably be limited to matters relevant to the type of insurance provided.<sup>146</sup>

Therefore, with regard to the duty of fair presentation, it is suggested that the IA 2015 has provided an insurer-friendly condition for the insurer to observe the scope of its own knowledge. Certainly, the new provisions of the IA 2015 have clarified the vague knowledge requirement of the insurer. It may now be easier for the assured to observe the knowledge requirement of the insurer. Nevertheless, it is suggested that the IA 2015 has also narrowed down the scope of the knowledge requirement of the insurer, which means that the assured now has a smaller chance to rely on the exception rule to escape from the liability of breaching the duty of fair presentation.

Furthermore, under the new duty of fair presentation, it is suggested that in comparison to the MIA 1906, the IA 2015 has widened the scope of the knowledge requirement of the assured.

Section 4(6) of the IA 2015 states that:

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<sup>143</sup> The Insurance Act 2015, section 5(3)(a)

<sup>144</sup> See Explanatory notes to the Insurance Bill 2015 (n29), para 67 for the change of the term “notoriety”.

<sup>145</sup> The Insurance Act 2015, section 5(3)(b)

<sup>146</sup> Explanatory notes to the Insurance Bill 2015 (n29), para 68

Whether an individual or not, an insured ought to know what should reasonably have been revealed by a reasonable search of information available to the insured (whether the search is conducted by making enquiries or by any other means).

And the definition of the word “information” is explained in section 4(7) as follows:

In subsection (6) “information” includes information held within the insured’s organisation or by any other person (such as the insured’s agent or a person for whom cover is provided by the contract of insurance).

The Explanatory Notes to the Insurance Bill 2015 has explained the effect of section 4(6) and 4(7).<sup>147</sup> These measures, together with the general duty to present the risk fairly, aim to solve the problem of “data dumping”. In the joint report which was issued by the Scottish Law Commission and the Law Commission of England and Wales in 2014, the problem was explained as follows:

The 1906 Act makes no provision about the manner in which disclosure must be made. This, when combined with confusion over what needs to be disclosed, sometimes leads to prospective policyholders giving large amounts of undigested information for the insurer to sort through and decide what is relevant. A lack of structuring and indexing combined with an overwhelming amount of information is known in extreme cases as a “data dump”.<sup>148</sup>

The report continues with the detriment that the underwriter has suffered from the data dumping practice of the assured:

For a busy underwriter, each presentation is one of many in need of assessment. Leaving insurers to navigate their own way through copious amounts of unfamiliar data with little or no signposting undermines the underwriting process. However, on a strict view of the 1906 Act, data dumping and other poor or convoluted presentations are unobjectionable. In some cases, the practice might even be employed to bury important information and yet it still arguably complies with the duty of disclosure.<sup>149</sup>

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<sup>147</sup> Explanatory Notes to the Insurance Bill 2015 (n29) paras 57-58

<sup>148</sup> Law Commission (n4) para 5.28

<sup>149</sup> *ibid*, para 5.29

It is evident that the insurer has suffered from the practice of data dumping and thus, it is understandable that the IA 2015 has imposed a new measure that requires the assured to present the risk in a reasonably clear and accessible manner.<sup>150</sup> It is suggested that this new requirement is an objective requirement,<sup>151</sup> and the consequence of breaching this requirement is the same as breaching the duty of fair presentation under the IA 2015.<sup>152</sup> There are several situations that the assured will be considered as breaching this requirement. Firstly, the assured breaches the requirement when “an overwhelming amount of undigested information” is disclosed to the insurer.<sup>153</sup> Secondly, the assured is not allowed to make “an overly brief or cryptic presentation” to the insurer.<sup>154</sup> Thirdly, the disclosure cannot be done in a “piecemeal” fashion or in an “oblique” manner.<sup>155</sup> It is noteworthy that under this requirement, the subject matter is about the form of the presentation but not the substance of the disclosed information.<sup>156</sup>

The new requirement has provided an extra defence for the insurer to reject insurance claim, which suggests that the assured is in a more unprivileged position than the position before the enactment of the IA 2015. One of the main problems of the duty of utmost good faith is that the duty is too insurer-friendly, and it is suggested that by imposing this new requirement, the IA 2015 has successfully created a friendlier environment for the insurer to underwrite the risk, but the detriment that the assured suffered has remained unchanged, if not increased. Furthermore, as the new requirement is a matter of form, it is unlikely that the assured can fully comply with this requirement, unless there is an agreed standard form of presentation with regard to the duty of disclosure. Nevertheless, it is almost impossible to formulate a universal answer on the form of risk presentation, as the presentation of risk can be affected by many factors, for example, the class of insurance, the scale of the assured company and also whether or not the assured has arranged the insurance through an agent. Therefore, it is suggested that the new requirement has increased the difficulty for the assured to comply with the duty of disclosure.

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<sup>150</sup> The Insurance Act 2015, section 3(3)(b)

<sup>151</sup> Law Commission (n4) para 7.45

<sup>152</sup> *ibid* para 7.41

<sup>153</sup> Explanatory Notes to the Insurance Bill 2015 (n29) para 47

<sup>154</sup> *Ibid* para 47

<sup>155</sup> Law Commission (n4) para 7.46

<sup>156</sup> *ibid* para 7.42

As criticised in the previous sub-sections, the lawmaker of either the MIA 1906 or the IA 2015 has failed to consider the situation from the perspective of the assured. The problem of handling a large volume of data is a common problem that is shared between both the assured and the insurer. The problem of data dumping is not a problem that is created by the assured, but rather a side effect of the advancement of technologies in the modern era. While the Law Commission has actively proposed to solve the problem of the insurer by proposing the duty of fair presentation; the Law Commission has simply ignored the need to solve the problem from the perspective of the assured.<sup>157</sup> In this regard, it is submitted that the implementation of the IA 2015 is an unsuccessful attempt to ensure fairness between the insurer and the assured.

Furthermore, section 4(6) of the IA 2015 requires the assured to conduct a reasonable search within the organisation before the risk presentation. Again, this new duty of reasonable search has imposed an unfair burden on the assured. On the one hand, the lawmaker has assumed that the busy underwriter has no time and resources to manage the big volume of data that is submitted by the assured for the purpose of risk assessment. On the other hand, the IA 2015 requires the assured to conduct a reasonable research within the whole company. The volume of data, which is handled by the assured in a company, is likely to be larger than the data that the insurer receives from the assured for the underwriting purpose. Furthermore, the intranet system of a company, based on the setting of the network, may possess information which is linked to the internet. It is suggested that the volume of data, which is possessed through the company intranet, can be almost unlimited and the scope of the reasonable search can be indeterminable.

It is noteworthy that one of the Law Commissioners suggested that the duty of reasonable search could be framed by the parties to an insurance contract and also the insurance market.<sup>158</sup> Nevertheless, it is suggested that the said view has undermined the purpose of imposing such a duty into the legislation. If a pre-contractual agreement could be made between the parties, it is more likely that the agreement would be focused on the scope of

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<sup>157</sup> The problem of handling big volume data by the assured was identified in Law Commission (n37) paras 6.68 - 6.69, but there are no follow up reform suggestions on this problem.

<sup>158</sup> House of Lords (n83), page 15, para 10 and 11

knowledge that is disclosable to the insurer by the assured. If both parties could agree on the scope of the disclosable knowledge, then there would be no necessity for the parties to discuss about the duty of reasonable search, as the issue of whether or not the knowledge is disclosable would be determined by the agreed scope of disclosable knowledge.

Further, by imposing a pre-contractual duty of reasonable search on the assured, it allows the insurer to sit back without doing any research on the risk before issuing the policy. Although section 3(4)(b) of the IA 2015 has imposed a duty of enquiry to the insurer, it does not require the insurer to conduct a reasonable search within his or her own organisation before issuing the insurance policy. In other words, the burden of searching material information is totally borne by the assured, which has not considered the possibility that the insurer and his or her company is also capable to possess material information.<sup>159</sup> In this regard, it is submitted that the new duty of reasonable search of the IA 2015 has defeated the purpose of reforming the duty of utmost good faith, and it should not be strictly adopted in the reform of Hong Kong legislation regarding the knowledge requirement.

To conclude, the IA 2015 has no doubt widened the scope of the knowledge requirement of the assured, the result of which is that the assured will face additional detriment when trying to comply with the duty of fair presentation. The duty of reasonable search is also likely to be subject to the subjective interpretation of the underwriting expert witness from the insurance industry, which may lead to the problem of professional bias. As mentioned in the previous subsection, the reform should be aimed at resolving the problems from the assured's perspective, and the IA 2015 has failed to achieve this purpose. As a result, it is suggested that the IA 2015 can be taken as a reference for the reform of the knowledge requirement, but the model of the IA 2015 should not be strictly adopted for the law reform in Hong Kong.

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<sup>159</sup> For instance, in *Carter v Boehm* (n1), it was the underwriter who knew the fact that the fort was at risk.

**C. Formulating the reform for the scope of the “deemed knowledge” – the new duty of reasonable search**

**i. The reform strategy**

It is submitted that the current law in Hong Kong and the IA 2015 have failed to address the impact of modern technologies in relation to the process of disclosure at the underwriting stage. These technologies have enhanced the capability of both the assured and the insurer to obtain information which is related to the risk, and the reform of the duty of disclosure in Hong Kong should not ignore this phenomenon. In this regard, it is suggested that both the assured and the insurer should be subject to a new duty of reasonable search during the process of underwriting. This measure will help to identify the scope of the “deemed knowledge”, and it will certainly help both parties to an insurance contract to anticipate what is disclosable under the “deemed knowledge” requirement.

The basic concept of this new duty of reasonable search is based on section 4(6) of the IA 2015, which requires the assured to conduct a reasonable search within its organisation during the process of disclosure. As mentioned in the above sub-sections, the duty of reasonable search, under the IA 2015, should not be strictly adopted in Hong Kong. Therefore, for the law reform in Hong Kong, the function of this new duty will be modified from two perspectives. Firstly, it is suggested that the duty of reasonable search should not extend to any information which can be found on the Internet, as the information on the internet is almost unlimited, and the scope of the reasonable search can be indeterminable. In other words, the reasonable search requirement only concerns the data that are reachable by the actual assured in an ordinary course of business. In relation to the information that are possessed by other staff of the same company, the actual assured, who is subject to the reasonable search requirement, still needs to disclose these information to the insurer, unless he or she can prove that a reasonable man in his or her position will not be able to access to these information. If the actual assured cannot prove that he has no authority to access the concealed information, then he or she is still liable for non-disclosure.

Secondly, the duty of reasonable search should also be imposed on the insurer as a matter of fairness, but it should only be applied in limited circumstances. The Law Commissioner, David Hertzell, when answering a question concerning the role of the insurer under the duty of fair



presentation, mentioned that the insurer is expected to perform professionally during the exchange of information at the underwriting stage.<sup>160</sup> However, it is surprising that the Law Commission decided not to impose any duty to regulate the conduct of the insurer at the underwriting stage. In this regard, to achieve fairness between the assured and the insurer, the new duty of reasonable search should be imposed on both parties to an insurance contract.

**ii. The solution – imposing new section 18(1)(b) and section 18(3)(b)**

To impose the new duty of reasonable search on the assured, section 18(1)(b) should be added as follows:

The assured is deemed to know what should reasonably have been revealed by a reasonable search of information accessible to the actual assured. Information that can be found on the internet is not deemed to be known by the assured.

The new section 18(1)(b) ensures that the actual assured is not allowed to turn a blind eye to the knowledge that is accessible by him or her. The question of whether certain information is accessible to the assured is a matter of fact. There are no circumstances that the knowledge of the others can be imputed to the actual assured. To determine whether the actual assured breaches the duty of reasonable search, there are several factors that will be taken into consideration. Firstly, it regards whether the actual assured is aware of the existence of the material knowledge. In a case where the actual assured is aware of the existence of the information, but turned a blind eye to it, the assured is liable for breaching the duty of reasonable search. However, in a case where the actual assured is not aware of the existence of the material information, then the next issue to be determined is whether the assured is able to access the information. The matter of accessibility is determined by the question of whether the assured will be able to obtain the concealed information in the ordinary course of business. If the insurer can prove that the actual assured is able to access the information in the ordinary course of business, then the actual assured is liable for the breach of the duty of reasonable search. In contrast, if the actual assured can prove that in the ordinary course of business he or she is not able to access the information, then the actual assured is not liable for the breach of the duty of reasonable search.

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<sup>160</sup> *ibid*, page 9, q10

In addition, to impose the duty of reasonable search on the insurer, section 18(3)(b) should be amended as follows:

In the absence of inquiry the following circumstances need not be disclosed, namely—

(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 his business, as such, ought to know. The insurer is also deemed to know what should reasonably have been revealed by a reasonable search of information accessible to the insurer.

Section 18(3)(b) also requires the insurer to conduct a reasonable search at the underwriting stage. The insurer is also not allowed to turn a blind eye to the information that is accessible to him or her. One of the circumstances is that the actual underwriter needs to conduct a reasonable search within his or her company in the case that the assured has also arranged another insurance cover through the same insurance company but with a different underwriter. For insurance companies with general practices, the underwriters may work by different company accounts or work by different classes of insurance. The former case means that within the same company, one single underwriter will be responsible for all classes of insurances under the name of the same assured company, and the latter case means that there will be different underwriters who are responsible for different classes of risks for the same assured company. In the latter case, the actual underwriter is required to conduct a reasonable search within his or her own company, and the said underwriter is not allowed to plead non-disclosure when the concealed information has already been submitted to another underwriter within the same insurance company, unless the actual underwriter can prove that the said information cannot be reasonably accessed by him or her.

The insurer is also required to conduct a reasonable search when he notices that material information is missing during the underwriting process. In this circumstance, the insurer may need to inquire the assured why such information is missing. It is arguable that this suggestion

is contradictory to the case law. In *WISE Ltd. v. Grupo Nacional Provincial S.A.*,<sup>161</sup> Lord Justice Rix underlined the role of the insurer in relation to the duty of disclosure as follows:

The reasonably careful underwriter is neither a detective on the one hand nor lacking in common-sense on the other hand. Mere possibilities will not put him on inquiry, and very little if anything can make up for non-disclosure of the unusual or special. Overriding all, however, is the notion of fairness, and that applies mutually to both parties, even if the presentation starts with the would-be assured.<sup>162</sup>

Nevertheless, there are two reasons to support why the said duty should be imposed on the insurer. Firstly, this reasonable search requirement does not aim to require the insurer to act as a detective; rather it aims to encourage the insurer to share the burden of obtaining material information from the assured in the process of risk assessment. The insurer does not require to obtain additional information which is irrelevant to the risk. The said duty only requires the insurer to assess the risk fairly with the knowledge that is within the reasonable reach of the insurer, and it certainly includes making a simple enquiry to the assured when the insurer notices that material information is missing.

Secondly, it is submitted that the current law is too protective towards the insurer, and this attitude leads to the unfair situation of allowing the insurer to underwrite the risk at the claims stage. On the one hand, the law does not allow the insurer to play a role as a detective at the underwriting stage, but on the other hand, the law does not restrict the insurer to act as a detective at the claims stage. In all non-disclosure cases that have been analysed in this thesis, these cases have demonstrated the ability of the insurers to conduct detailed investigations. Should the insurers of all non-disclosure cases have had done reasonable searches before entering into an insurance contract with the assured, there would have been a significant decrease in the number of non-disclosure cases that were brought to the court. In this regard, the requirement of the reasonable search may not only help to ensure fairness between the parties, but it may also help to reduce the litigation costs of both the assured and the insurer.

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<sup>161</sup> *WISE Ltd.* (n40)

<sup>162</sup> *ibid* [64]

### III. Conclusion

To conclude, the current knowledge requirement in Hong Kong has been draconian to the assured but lenient to the insurer. Although the Law Commission has correctly identified the problems of the MIA 1906, still the IA 2015 has failed to address the pitfalls of the MIA 1906, which means the IA 2015 is not a good precedent for the Hong Kong legislator to follow. With a wider scope of the knowledge requirement from the assured's perspective, the measures in the IA 2015 will only produce additional administrative work for the assured. It is suggested that there is no reason to adopt the IA 2015 approach in Hong Kong completely. Nevertheless, several new sections of the IA 2015 have provided clearer explanations of the duty of disclosure, and these sections can be used as references for the future reform in Hong Kong. Firstly, section 4(4) of the IA 2015 has stipulated the exception of the duty of the agent to comply with the knowledge requirement, which has clarified the current legal position in section 19 of the MIO.<sup>163</sup> Secondly, section 5 of the IA 2015 has provided a clearer scope and explanations on the insurer's knowledge requirement. Thirdly, section 6 has provided a clearer scope of the general definition of the knowledge requirement. The remaining sections, as far as the reform of knowledge requirement in Hong Kong is concerned, are unfavourable.

This chapter has offered two reform suggestions, which are independent from the IA 2015, for the knowledge requirement of the duty of disclosure in Hong Kong. Firstly, the new legislation should adopt the "actual assured" approach for the knowledge requirement, which is in alignment with the actual underwriter approach of the insurer, and it ensures that the assured can be able to understand and comply with the duty of disclosure. Secondly, both the assured and the insurer should be subject to a duty of reasonable search during the underwriting process. These measures may not be perfect to solve every scenario in relation to the duty of disclosure, nevertheless, they aim to provide guidance on how both parties to an insurance contract can be treated fairly and equally under the law. The current law only stresses on the burden of the assured and requires the assure to present the risk fairly. It is suggested that the said approach is unfair to the assured, and thus the current law is in need of reform. The detailed reform suggestions will be presented in chapter 6 of this thesis.

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<sup>163</sup> This exception will be further elaborated in chapter 5 of this thesis.

## Chapter 2 The Materiality And Inducement Tests Of The Duty Of Disclosure

The previous chapter has examined the knowledge requirement of the duty of disclosure for both the assured and the insurer, the purpose of which is to define the scope of the duty of disclosure. This chapter will analyse the actual operation of the duty of disclosure in law. According to the MIO, the assured is only liable for breaching the duty of disclosure if the insurer can prove that the concealed knowledge is material and induces the insurer to enter into the insurance contract. In other words, the court will examine each non-disclosure case by a twofold test, namely the materiality and inducement tests. The test of materiality is an objective test which requires the insurer to prove that the concealed knowledge is material to a prudent insurer. The test of inducement is a subjective test which requires the insurer to prove the actual degree of inducement of the concealed knowledge. This chapter, therefore, will be divided into two sections to address the problems of the materiality and inducement tests.

The first section of this chapter will consider the problem of the materiality test. The first part of this section will outline the problem of the materiality test under the MIO. This test is normally referred as the “prudent insurer test”, and it has been criticised on the ground that it is too difficult for the assured to comply with it. Even practitioners in the industry could be confused by the test. Nevertheless, the IA 2015 has not addressed this problem, and there is no significant change in the IA 2015 regarding the materiality test.

To resolve the problem, another form of the materiality test, which is known as the “reasonable insured test”, will be introduced in the second part of this section. The test had been proposed by the Law Commission in 2007, but eventually, the Law Commission had decided to abandon the test due to its own technical problems.<sup>164</sup> The test aimed to lighten the burden of the assured, but it was also criticised by practitioners and scholars that the said test was lack of certainty and it might not significantly improve the position of the assured, as the assured would still be the party who was responsible for performing the act of disclosure.<sup>165</sup> The Law Commission then concluded that the operation of the prudent insurer test is still the best option

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<sup>164</sup> Law Commission (n4) paras 5.45 to 5.48

<sup>165</sup> *ibid* para 5.47

for the industry, or at least it is better than the uncertain reasonable insured test.<sup>166</sup> Nevertheless, it is submitted that although the IA 2015 did not adopt the reasonable insured test, Hong Kong is still flexible to adopt it.

In the final part of the first section, a suggestion with reference to the materiality test will be provided for the reform of Hong Kong legislation. It is submitted that a fairer result of the materiality test can only be achieved by proposing a hybrid of both the prudent insurer test and the reasonable insured test, the aim of which is to strike a balance between the interest of both the assured and the insurer. In other words, the reform will propose a novel “third-way” test, which is materially different with the existing tests.

The second section of this chapter considers the problem of the inducement test. In the first part, it is suggested that the inducement test is not explicitly stated in section 18(2) of the MIO. It was not until the case authority *Pan Atlantic Insurance Co. Ltd v. Pine Top Insurance Co. Ltd.*<sup>167</sup> that the test was confirmed by the court as an implied requirement.<sup>168</sup> It is submitted that the ambiguity of the inducement test may cause an adverse impact on the development of the law of insurance in Hong Kong.

The second part will analyse the question of whether the IA 2015 has solved the pitfalls of the inducement test. The IA 2015 has explicitly stated the requirement of proving inducement in section 8 of the IA 2015, which has solved one of the pitfalls of the MIA 1906. Section 8 of the IA 2015 has also concatenated the inducement test and the proportionate remedies. It is suggested that the new remedies are fairer in comparison to the old single remedy under the MIA 1906. Nevertheless, similar to the inducement test in the MIA 1906, the new inducement test also has not provided a clear guidance on its operation, and the potential problem of it may be more serious than the old inducement test.

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<sup>166</sup> *ibid* para 5.47

<sup>167</sup> *Pan Atlantic* (n46)

<sup>168</sup> Nevertheless, it does not mean that the inducement test was not applied to the insurance case authorities prior to the *Pan Atlantic Insurance Co. Ltd* case, but the position of the test was unclear until it was confirmed by the *Pan Atlantic Insurance Co. Ltd*. See Eggers, Picken and Foss (n56) para 14.89-14.98

In the final part of the second section, a suggestion with reference to the subjective inducement test will be provided for the reform in Hong Kong. It is submitted that the current inducement test should be reformed, and a clearer guidance on the operation of the test should be provided in the new legislation. The application of the new inducement should be stricter than the current test, and the reform should also ensure that the test will not be abused by the insurer.

**I. The problem of the materiality test – the “prudent insurer test” is incomprehensible**

**A. The problem of the materiality test under the MIO**

Section 18(2) of the MIO provides that:

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

The materiality test is an objective test, the function of which is to determine whether the concealed facts are material to a prudent insurer. The ironical feature of this test is that although the assured is the party who needs to comply with this duty, but the law is enacted from the perspective of a prudent insurer. As a result, it is highly unlikely that the assured can understand the requirement of it. It is suggested that the materiality test itself “.....covers a wide spectrum, from matters which (if disclosed) would mean that no prudent insurer would under any circumstances have anything to do with the proffered risk to matters which the prudent insurer would wish to take into account but which would ultimately make no difference to what he would actually do.”<sup>169</sup> It is worth mentioning that the test of materiality is the same for non-disclosure and misrepresentation under the MIO.<sup>170</sup>

The word “influence”, in section 18(2), means a mere influence only.<sup>171</sup> Although section 18(2) mentions the terms “premium” and “acceptance of the risk”, the concealed fact need not have an actual effect on either changing the level of the premium or the acceptance of the risk.<sup>172</sup>

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<sup>169</sup> *Axa Versicherung AG v Arab Insurance Group (BSC)* [2015] Lloyd's Rep. IR Plus 31, [2015] EWHC 1939 [115]

<sup>170</sup> Gilman, Templeman, Blanchard, Hopkins and Hart (n38) paras 15-24

<sup>171</sup> Merkin (n42) para A-0760

<sup>172</sup> *Pan Atlantic Insurance Co. Ltd* (n46) 114

The only requirement is that the prudent insurer “would have wanted to know” the fact<sup>173</sup> and it “would have influenced a prudent underwriter in the formation of his opinion.”<sup>174</sup> The concealed fact should influence the process of assessing the risk. Moreover, the influence cannot be a mere presumption,<sup>175</sup> and it need not be decisive.<sup>176</sup> A mere influence is not sufficient to pass the test; it needs to be influential to a particular person, who is a prudent insurer. Under this requirement, a prudent insurer is a hypothetical insurer.<sup>177</sup> It is defined by Lord Justice Evans that a prudent insurer “is no more than the anthropomorphic conception of the standards of professional underwriting which the Court finds it appropriate to uphold.”<sup>178</sup> Moreover, the main theme of the test is about “...whether the materials are such that a prudent underwriter would take them into account...”<sup>179</sup>

Under section 18(2), an actual insurer is not required to act as a prudent insurer. Nevertheless, the court has to consider the characteristics of an actual insurer, before deciding whether a concealed fact has an influence on a prudent insurer.<sup>180</sup> In *Drake Insurance v. Provident Insurance*,<sup>181</sup> Lord Justice Clarke considered the effect of the non-disclosure from two perspectives. Firstly, the dispute concerned a motor risk policy, and, therefore, Clarke L.J. examined the case from the viewpoint of a prudent motor insurer.<sup>182</sup> Secondly, the actual underwriter used a “points” system for underwriting, so Clarke L.J. examined the case from the viewpoint of a prudent insurer, who was assumed to use a “points” system for assessing the risk.<sup>183</sup>

In general, the insurer bears the burden of proof of the materiality test.<sup>184</sup> In practice, the insurer can call underwriting expert witnesses to give evidence about the prudent insurer test.<sup>185</sup> However, in some cases, the court may rule on the issue of materiality by a common-sense

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<sup>173</sup> Merkin (n42) para A-0760

<sup>174</sup> *ibid*

<sup>175</sup> *Pan Atlantic Insurance Co. Ltd* (n46) 108

<sup>176</sup> *ibid* 106

<sup>177</sup> *ibid*

<sup>178</sup> *St Paul Fire & Marine Insurance Co. (UK) Ltd. v McConnell Dowell Constructors Ltd.* [1995] 2 Lloyd's Rep 116, 122

<sup>179</sup> *Pan Atlantic Insurance Co. Ltd* (n46) 113

<sup>180</sup> *Drake Insurance v Provident Insurance* [2004] 1 Lloyd's Rep IR 277 [140]

<sup>181</sup> *ibid*

<sup>182</sup> *ibid* [140]

<sup>183</sup> *ibid* [141]

<sup>184</sup> Eggers, Picken and Foss (n56) para 18.01

<sup>185</sup> Merkin (n42) para A-0761



approach,<sup>186</sup> and in these cases, the burden of proof transfers to the assured to rebut the materiality of the fact.<sup>187</sup>

It is noteworthy that a matter of materiality is a question of fact, and there is no automatic formula to determine whether certain facts are material or not.<sup>188</sup> Claims records of the assured are usually regarded as material facts for assessment of risks.<sup>189</sup> However, there are exceptional circumstances, for instance, claims records may be regarded as immaterial if they are accessible to the public, as the insurer ought to know the said records.<sup>190</sup>

It is also worth noting that the view of the assured is irrelevant to the test. The only requirement for the assured is to make a fair presentation of the risk, and this proposition is confirmed by Christopher Clarke J in *Garnat Trading & Shipping (Singapore) Pte Ltd v Baominh Insurance Corporation*.<sup>191</sup> The learned judge contented himself with the submission of the claimant that the assured's presentation of the risk "...will be fair and accurate if it would enable a prudent insurer to form a proper judgment, either on the presentation alone, or by asking questions if he was sufficiently put upon enquiry and wanted to know further details."<sup>192</sup>

The materiality test has been detrimental to the interest of the assured, and the case authority *Lambert v Co-operative Insurance Society Ltd*<sup>193</sup> is an example of the situation. The case concerned an all-risk insurance of jewellery that belonged to a couple. The proposer of the insurance, who was the wife, failed to disclose criminal convictions of her husband to the insurer. Her husband had one conviction before the conclusion of the insurance contract, and another conviction before the renewal of the contract. The wife did not disclose any of these convictions. The insurer discovered the conviction record of the husband and avoided the contract on the ground of non-disclosure. The claimant pleaded that the proper test of materiality should have been confined to what a reasonable assured would have considered for certain facts as material.

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<sup>186</sup> *ibid* para 6-044

<sup>187</sup> Eggers, Picken and Foss (n56) para 18.02

<sup>188</sup> John Dunt, *Marine Cargo Insurance* (1<sup>st</sup> edn Informa Law 2009) para 5.19

<sup>189</sup> Merkin (n42) para A-0791

<sup>190</sup> Eggers, Picken and Foss (n56) paras 8.26-8.27

<sup>191</sup> *Garnat Trading* (n126)

<sup>192</sup> *ibid* [135]

<sup>193</sup> *Lambert* (n3)

The trial judge rejected the claimant's submission on the test of materiality. However, the trial judge also held that a reasonable assured would not have considered the second conviction of the husband, which was an offence of dishonesty, as a material fact. In the Court of Appeal, the claimant's proposition was also rejected on the ground that no case authority supported the claimant's case. Lord Justice Lawton, in his judgment, expressed his concern for the test of materiality:

The present case shows the unsatisfactory state of the law. Mrs. Lambert is unlikely to have thought that it was necessary to disclose the distressing fact of her husband's recent conviction when she was renewing the policy on her little store of jewellery. She is not an underwriter and has presumably no experience in these matters. The defendant company would act decently if, having established the point of principle, they were to pay her.<sup>194</sup>

The above-mentioned judgment indicates that it can be difficult for the assured to anticipate what a prudent insurer would want to know in an underwriting process. Moreover, recent case law shows that even the practitioners in the insurance market can be confused by the test. In *Brit UW Ltd v F & B Trenchless Solutions Ltd*<sup>195</sup>, the insurance contract concerned a risk of contractor liability. The claimant was an insurer, and the defendant was a contractor for tunnels construction. The defendant, before the formation of the contract, failed to disclose to the insurer that there was a void under the railway line. A derailment occurred due to the void, and the claimant sought to avoid the insurance contract on the ground of non-disclosure and misrepresentation of the risk.

The court held that the insurer was entitled to avoid the contract. Mrs. Justice Carr, in her judgment, referred the matter of materiality in this case as "a matter of common sense" and no expert evidence was needed to reach the conclusion that the concealed facts were material.<sup>196</sup> However, the author would like to highlight the performance of the expert witnesses in this case. The expert witness for the claimant, who was referred by Mrs. Justice Carr as a "highly

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<sup>194</sup> *ibid* 491

<sup>195</sup> *Brit UW* (n58)

<sup>196</sup> *ibid* [139]

experienced underwriter”, was confused by the prudent insurer test and was only able to give an opinion on the actual situation.<sup>197</sup> The expert witness for the defendant, who was the broker of the assured, also failed to submit the evidence from the perspective of an underwriter under the test.<sup>198</sup> The performances of the practitioners indicate that the prudent insurer test is excessively harsh and severe to the assured, who is likely to be a layman in both insurance and law.

Another problem of the prudent insurer test is that no man can act as a prudent insurer except the insurers themselves. Nevertheless, the law does not require the insurer to act in a prudent way,<sup>199</sup> but rather requires the assured, who has no knowledge about how to act as a prudent insurer, to conceive of the mind of a prudent insurer. If the legislation does not require the insurer to act prudently, then it is unfair to request the assured to comply with such a high standard of requirement. Furthermore, although the judges can draw a reasonable inference from the prudent insurer test, they may also rely on the insurer to testify whether certain facts are influential to a hypothetical prudent insurer, which may lead to a biased judgment against the assured. In this regard, it is submitted that the materiality test is in need of reform. The next issue to be considered is what are the options that are available for the law reform in Hong Kong.

## **B. The prudent insurer test under the IA 2015 and the abandoned reasonable insured test – which test is better?**

It is submitted that there are two reform options for the materiality test in Hong Kong, namely the prudent insurer test in the Insurance Act 2015 and the reasonable insured test. A comparison between the two tests will be provided in the following sub-sections, the aim of which is to compare the advantages and disadvantages of the two tests.

### **i. The prudent insurer test under the IA 2015**

The test of materiality is stipulated in section 3 of the IA 2015. Section 3(4) states that:

(4) The disclosure required is as follows, except as provided in subsection (5)—

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<sup>197</sup> *ibid* [126]

<sup>198</sup> *ibid* [128]

<sup>199</sup> See *Pan Atlantic Insurance Co. Ltd* (n46)

- (a) disclosure of every material circumstance which the insured knows or ought to know, or
- (b) failing that, disclosure which gives the insurer sufficient information to put a prudent insurer on notice that it needs to make further enquiries for the purpose of revealing those material circumstances.

Section 3(4)(a) is identical to section 18(2) of the MIA 1906, and section 3(4)(b) has not altered the common law position on the duty of disclosure.<sup>200</sup> The application of section 3(4) was examined in *Young v Royal and Sun Alliance Plc*.<sup>201</sup> This case concerned insurance policies that covered several commercial premises of the assured. A fire accident occurred and the premises were seriously damaged. The assured claimed £7,200,000 under the policy, but the insurer rejected the claim on the ground of non-disclosure. The non-disclosure was about the fact that the assured was the director of four other companies which were insolvent. The assured argued that the follow-up email dated 24 March 2017, which was sent by the insurer, amounted to a waiver of disclosure. The email stated that “Insured has never Been declared bankrupt or insolvent/Had a liquidator appointed.”<sup>202</sup>

In relation to section 3(4)(b) of the IA 2015, Lady Wolffe observed that it was applicable in cases where “the insurers were faced with several documents submitted by the insurer which, collectively, would constitute the fair presentation and where discrepancies between them might invite further enquiry.”<sup>203</sup> Lady Wolffe also commented that section 3(4)(b) would be considered in situations where “by reason of some feature of the presentation, the insurer was placed under a duty to make further enquiry”, but the *Young* case<sup>204</sup> did not fall within these categories and neither parties tried to argue the case on the basis of section 3(4)(b).<sup>205</sup>

Lady Wolffe also examined the submission of the assured and the broker. She commented that the phrase “in any business capacity”, which was used in the submission of the broker in relation to the prior insolvency in relation to the assured, was “a very board formulation”. She

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<sup>200</sup> Explanatory Notes to the Insurance Bill 2015 (n29) para 46

<sup>201</sup> *Young* (n10)

<sup>202</sup> *ibid* [11]

<sup>203</sup> *ibid* [78]

<sup>204</sup> *ibid*

<sup>205</sup> *ibid*

also noted that the statement in relation to the prior insolvency was “a statement of affairs without conclusion” and it was “virtually meaningless”.<sup>206</sup> In relation to the follow-up email, which was sent by the insurer based on the presentation of the broker, Lady Wolffe commented that the email was not a question or an enquiry, and no reasonable reader would consider the email as a waiver.<sup>207</sup> Thus, Lady Wolffe concluded that there was no express or implied waiver in this case. It is noteworthy that this case focused on the discussion of waiver and the actual operation of the new duty of fair presentation was not fully examined. Therefore, at this moment, this case should only be treated as a reference for the use of the new duty of fair presentation under the IA 2015, and the actual operation of the duty is still subject to the clarification of future cases.

Apart from section 3 of the IA 2015, the matter of materiality is further explained in section 7(3)<sup>208</sup>, 7(4) and 7(5)<sup>209</sup> of the IA 2015. Both section 7(3) and 7(5) have not made any significant change in the definition of materiality.<sup>210</sup> The most successful attempt to clarify the materiality test is made in section 7(4), which states that:

Examples of things which may be material circumstances are—

- (a) special or unusual facts relating to the risk,
- (b) any particular concerns which led the insured to seek insurance cover for the risk,
- (c) anything which those concerned with the class of insurance and field of activity in question would generally understand as being something that should be dealt with in a fair presentation of risks of the type in question.

Section 7(4) is imposed as guidance for the assured to comply with the duty of fair presentation,<sup>211</sup> as explained by the Law Commission:

The most significant example is the third: circumstances which those in the market would generally understand should be covered. We hope that insurers, brokers and

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<sup>206</sup> *ibid* [80]

<sup>207</sup> *ibid* [92]

<sup>208</sup> The Insurance Act 2015, section 7(3) states that “A circumstance or representation is material if it would influence the judgment of a prudent insurer in determining whether to take the risk and, if so, on what terms.”

<sup>209</sup> The Insurance Act 2015, section 7(5) states that “A material representation is substantially correct if a prudent insurer would not consider the difference between what is represented and what is actually correct to be material.”

<sup>210</sup> Explanatory notes to the Insurance Bill 2015 (n29) para 75

<sup>211</sup> Law Commission (n4) para 6.12

policyholders will work together to develop guidance and protocols about what should be disclosed, to put flesh on the bones of this structure.<sup>212</sup>

In other words, the matter of materiality will still be examined upon the unique circumstance of each case.<sup>213</sup> This is a positive attempt to encourage the parties to a contract to cooperate closely in order to resolve the problems of materiality. Nevertheless, the legal effect of the said section still remains in doubt, and it is subject to the future case law to confirm and elaborate the application of section 7(4).

Furthermore, section 7(4)(a) and 7(4)(b) have provided clearer guidance on the duty of disclosure of the assured. Nevertheless, it is suggested that section 7(4)(c) can be problematic. Section 7(4)(c) requires the assured to disclose information that are concerned with the class of insurance and field of activity. While the term “field of activity” can be interpreted as business activity of the assured (and no doubt the assured is familiar with the said activity), the term “class of insurance” may suggest that section 7(4)(c) requires the assured to understand the general market practice of underwriting a particular class of risk, which is unlikely to happen in a real-life situation. One may suggest that the insurer can provide a written protocol to the assured for each class of risk before the disclosure. Nevertheless, this action makes no actual difference with the current market practice. During the underwriting process, the established practice is that the insurer has to inform the assured what are the relevant facts and knowledges that need to be disclosed.<sup>214</sup> assured relies heavily on the instruction of the insurer to disclose relevant facts and knowledge to the insurer. In this regard, the instruction of the insurer already amounts to a protocol of the disclosable facts and knowledge. Nevertheless, non-disclosure is more likely to happen when a particular material information is not requested by the insurer, and meanwhile, the assured does not realise that the particular information is material to the risk. In other words, non-disclosure may exist, or most likely to exist outside the general market practice. Therefore, it is submitted that while section 7(4)(a) and 7(4)(b) can act

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<sup>212</sup> *ibid* para 6.14

<sup>213</sup> Explanatory notes to the Insurance Bill 2015 (n29) para 76

<sup>214</sup> For instance, Financial Conduct Authority, Insurance Conduct of Business Sourcebook 5.1.4 states that “A firm should bear in mind the restriction on rejecting claims (ICOBS 8.1.1R (3)). Ways of ensuring a customer knows what he must disclose include:

(1) explaining to a commercial customer the duty to disclose all circumstances material to a policy, what needs to be disclosed, and the consequences of any failure to make such a disclosure”

In Hong Kong, please refer to The Code of Conduct for Insurers paragraph 10(a), which requires the insurer to explain what information that is required to be disclosed in the proposal form.

as an indicator of the disclosable information regarding the duty of disclosure, section 7(4)(c) may not lead to any significant improvement on the current situation.<sup>215</sup> As a result, it is suggested that except section 7(4) has provided a positive attempt to solve the current problems, on the whole, the IA 2015 has not solved any problem that has been identified in the previous sub-section. Nevertheless, in the process of reform consultation, the Law Commission proposed the reasonable insured test as an alternative of the prudent insurer test, which is worth to be taken into consideration for the reform of Hong Kong commercial insurance law.

## **ii. The abandoned reasonable insured test**

In 2007, the Law Commission made an attempt to replace the prudent insurer test with the reasonable insured test, the draft provisions of which were as follows:

We provisionally propose that, in order to be entitled to a remedy for the insured's non-disclosure or misrepresentation, the insurer must show that:

(1) had it known the fact in question it would not have entered into the same contract on the same terms or at all; and

(2) it must also show either:

(a) that a reasonable insured in the circumstances would have appreciated that the fact in question would be one that the insurer would want to know about; or

(b) that the proposer actually knew that.<sup>216</sup>

Contrary to the prudent insurer test, the reasonable insured test considers the issue of materiality from the perspective of the assured. It is suggested that the reasonable insured test is more reasonable than the current prudent insurer test. The rationale of the duty of disclosure lies in the imbalance of information between the insurer and the assured, as the assured is in a more privileged position than the insurer in obtaining information which is related to the risk.<sup>217</sup> Nevertheless, there is also another form of imbalance of knowledge, which is the knowledge of risk assessment, between the assured and the insurer. Such an imbalance position is often

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<sup>215</sup> It may also be arguable that the burden of proof is too high to be met by the assured under the new duty of fair presentation. See House of Lords (n83) page 94, para 2, Memorandum submitted by the Insurance Law Research Group, University of Southampton

<sup>216</sup> Law Commission, Insurance Contract Law: Misrepresentation, Non-Disclosure and Breach of Warranty by the Insured A Joint Consultation Paper (Law Com CP No 182, 2007) para 5.84

<sup>217</sup> Nevertheless, the significance of this argument is reduced due to the advancement of modern technologies, please refer to chapter 1 of this thesis.

ignored by the practitioners. The assured is not capable of understanding how the risk can be prudently assessed by the insurer, as it requires the assured to possess the professional knowledge of risk assessment. Conversely, both the assured and the insurer are capable to understand the duty from the perspective of a reasonable insured, as it does not require any professional knowledge. Under the reasonable insured test, the assured only needs to disclose the material information that the insured actually knows, or the insured expects that the insurer wants to know. The implied effect of this approach is that the insurer needs to take an active role to obtain information, which is needed to assess the risk accurately, from the assured. The insurer is also obliged to effectively communicate with the assured on the matter of disclosure. Otherwise, it is likely that the reasonable insured test will allow the insured to escape from the liability of innocent non-disclosure.

Nevertheless, the reasonable insured test was eventually abandoned by the Law Commission. The first reason of the abandonment, as mentioned in the Law Commission Paper, was that there was not a unified standard for the reasonable insured test. The manner of the assured's disclosure would be subject to various factors, such as the class and size of the business, and also the use of insurance broker.<sup>218</sup> The consequence of adopting the test would be that "obtaining expert evidence will be almost impossible and the net result will be to give the trial judge a very wide discretion in each case."<sup>219</sup>

With respect, it is submitted that this statement does not reflect the true position of the prudent insurer test, and also ignores the nature of the reasonable insured test. Firstly, the prudent insurer test itself is not a test with a single standard, and the requirement of it is also altered due to the nature of the insured risk. In *Drake Insurance Plc v. Provident Insurance Plc*,<sup>220</sup> the insurer tried to avoid the motor insurance contract, on the basis that the assured did not disclose a previous speeding conviction to the insurer. The insurer had adopted a point system for assessing the risk. Under the point system, the previous conviction of the assured did not affect the premium as it was completely settled through negotiation. As a result, the Court of Appeal held that the insurer was not entitled to avoid the insurance contract, as the conviction

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<sup>218</sup> *ibid* para 5.46

<sup>219</sup> *ibid* para 5.46

<sup>220</sup> *Drake Insurance Plc* (n181)



record did not lead to any inducement.<sup>221</sup> When considering the matter of materiality in this case, Lord Justice Clarke underlined the characteristics of the prudent insurer as follows:

It was no doubt for that reason that it was common ground that the speeding conviction was material, since the reasonably prudent motor insurer would regard speeding convictions as material. However, that depends upon what characteristics of the reasonably prudent insurer can be taken into account. It seems clear that some characteristics of the particular insurer should be taken into account in order to identify what the reasonably prudent insurer would regard as material. For example, in the case of a proposed motor insurance, it would surely be appropriate to ask what the reasonably prudent motor insurer would regard as material.<sup>222</sup>

Lord Justice Clarke further held that to apply the prudent insurer test in this case, it was not merely a question of what a “prudent motor insurer” would have in mind, but what a “prudent motor insurer”, who adopted the point system in assessing the risk, that would have in mind.<sup>223</sup> The judgment indicates that the prudent insurer test is also subject to alteration due to the nature of the insurance risk, and also the practice of each insurance company.

Secondly, the test of reasonable insured aims to solve the problem of professional bias, and it is unnecessary to ask for expert evidence in order to determine whether the concealed information is material to the risk. The reasonable insured test requires no more than the knowledge that a reasonable man will know or be expected to know, from the perspective of the assured, during the process of purchasing insurance. Therefore, the problem that it is impossible to obtain expert evidence, in relation to the reasonable insured test, is not a disadvantage, but rather a favourable outcome to moderate the standard of the prudent insurer test that is too harsh for the assured.

The second reason for the abandonment is that the reasonable insured test may not be able to improve the assured’s position, as the burden is still on the assured to disclose knowledge and

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<sup>221</sup> *ibid* [75]

<sup>222</sup> *ibid* [140]

<sup>223</sup> *ibid* [141]

facts to the insurer.<sup>224</sup> However, it is submitted that this proposition is not feasible. The fundamental procedure for the underwriting process involve two elements which are unchangeable, namely the disclosure of information from the assured and the risk assessment from the insurer. No matter how the requirement of disclosure changed, the burden would still be on the assured to disclose facts and knowledge. Therefore, the significance of the reform does not lie in whether or not the assured bears the responsibility to disclose facts but lies in how the assured complies with the requirement. The reasonable insured test has introduced a new standard which the assured is capable of understanding and complying with it, and that is the most significant element that the legislator needs to consider regarding the reform of the duty.

Finally, the Law Commission concluded its decision of the abandonment as follows:

We accepted that a “reasonable insured” test would introduce an unknown and untested concept into the law. In Australia, where a similar reform was introduced in 1984, subsequent legislation has been required in order to clarify how it should be applied. It would take time for judges to develop a consistent approach, and during this time it would be even more difficult to advise businesses about what they were expected to disclose.<sup>225</sup>

The conclusion concerns not only the legal effect of the reform but also the actual impact to the insurance industry if the reasonable insured test is adopted. Nevertheless, as criticised in the previous sub-sections, the IA 2015 has not improved the unfair condition of the assured except the enactment of section 7(4). Nevertheless, at this stage section 7(4) can only act as guidance on the matter of disclosure, and the scope and legal effect of this section are still remained in doubt. In any event, the effect of the IA 2015 is also subject to clarification from the future case law, and therefore the reasons for the abandonment of the reasonable insured test are unsound.

To conclude, it is suggested that the reasonable insured test may lead to a fairer outcome than the prudent insurer test with regard to non-disclosure cases. Nevertheless, it is noteworthy that

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<sup>224</sup> Law Commission (n4) para 5.47

<sup>225</sup> *ibid* para 5.48

the reasonable insured test has its own problems,<sup>226</sup> for example, the said test may not be able to accurately define the scope of the disclosable knowledge regarding the duty of disclosure, and the insurer may not be able to assess the risk fairly due to the indefinite scope of the duty.<sup>227</sup> The other criticism is that the insurer has no means to anticipate and prove the mind of the assured and thus, the reasonable insured test can be problematic for the insurer. Therefore, to avoid the problems of both the prudent insurer test and the reasonable insured test, it is submitted that Hong Kong should reform the materiality test by adopting a “third-way approach”, which is a hybrid of the prudent insurer test and the reasonable insured test. It is suggested that the new approach is the only way to preserve the interests of both the assured and the insurer.

### **C. The reform suggestion with regard to the materiality test - The “third-way approach”**

Based on the analysis of the previous sub-sections, it is submitted that both the prudent insurer test and the reasonable insured test may not be able to ensure fairness during the process of risk underwriting. The prudent insurer test is too difficult for the assured to understand as the requirement involves professional knowledge, which even the practitioners can be confused by the test. The reasonable insured test may not be sufficient to protect the insurer’s right to assess the risk fairly, and it may be against the original intention of imposing the duty of utmost good faith, as the assured is not in the best position to make a judgment on the matter of materiality. Therefore, it is suggested that both the prudent insurer test and the reasonable insured test have failed to preserve the best interests of the parties to an insurance contract. The only possible solution for reforming the materiality test is to strike a balance between the prudent insurer test and the reasonable insured test. In other words, a new third-way test will be introduced for proving materiality. The third-way test is a two-fold test. Firstly, the insurer needs to prove that under the prudent insurer test, the non-disclosed circumstance is material to the risk, the requirement of which is the same as the materiality test under the MIA 1906 and the MIO. Secondly, the assured is entitled to raise a defence that under the reasonable assured test, he or she would not have expected that the non-disclosed circumstance is material to the

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<sup>226</sup> For example, see H.Y. Yeo and N. Lye, “Re-visiting pre-contractual duties in Malaysian insurance law” [2016] *Journal of Business Law* 139 153-154

<sup>227</sup> Martin Bakes, “Pre-contractual information duties and the Law Commissions’ review” in Baris Soyer(ed), *Reforming marine and commercial insurance law* (Informa London) page 51-52

risk from the point of view of a reasonable assured. The details of the new two-limb test will be provided in the following sections.

**i. The first limb test: the prudent insurer test**

The first limb of the test requires the insurer to prove that the concealed circumstance is material to the risk, the approach of which is the same as the MIA 1906 and the MIO. The burden of proving materiality is borne by the insurer. The insurer needs to prove that the concealed circumstance has an influence on the underwriting decision, but such an influence need not be decisive. In general, there are two ways of proving materiality under the prudent insurer test. The first way is that the relevant parties who are responsible for the insurance arrangement can give testimony as to whether the concealed circumstance is material. For instance, in the case *Dalecroft Properties Ltd v Underwriters Subscribing To Certificate Number 755/BA004/2008/OIS/00000282/2008/005*,<sup>228</sup> Mr. Isted, who was the principal of the underwriters of the property insurance contract in dispute, submitted to the court that the concealed circumstances, namely the poor conditions of the insured property, were material to the risk and if he had known the poor conditions of the property, he would not have renewed the insurance contract.<sup>229</sup> It is upon the judge to decide whether the testimony is reliable or not. In this case, the judge considered Mr. Isted's evidence reliable and helpful while the evidence of Mr Horowitz, who was the director of the assured, had to be approached with considerable caution.<sup>230</sup>

The second way is that the insurer can call for expert witnesses to testify on the matter of materiality. In the *Dalecroft Properties Ltd* case,<sup>231</sup> Mr. Pipe was instructed by the assured and Mr. Clegg was instructed by the insurer to testify on the matter of materiality. Both of the expert witnesses were underwriters with considerable experiences of underwriting property risk. Again, it is upon the judge to decide whether the expert evidence is reliable or not. In *Dalecroft*

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<sup>228</sup>*Dalecroft Properties Ltd v Underwriters Subscribing To Certificate Number 755/BA004/2008/OIS/00000282/2008/005* [2017] Lloyd's Rep. IR 511

<sup>229</sup> *ibid* [124]

<sup>230</sup> *ibid* [11]

<sup>231</sup> *ibid*

*Properties Ltd* case,<sup>232</sup> although both expert witnesses were considered to be impressive witnesses by the judge, Mr. Clegg's evidence was proved to be more preferable.<sup>233</sup>

At this stage, the first limb of the new materiality test, which is introduced to solve the problem of the materiality test of the MIO, is the same as the original materiality test of the MIO. It is the second limb of the test, namely the reasonable assured test, that alters the original materiality test and considers the matter of materiality from the perspective of the assured.

## **ii. The second limb test: the reasonable assured test**

For the second limb of the "third-way" materiality test, it is suggested that the reasonable assured test should be adopted as a defence of non-disclosure.<sup>234</sup> After the insurer has proved materiality under the prudent insurer test, the burden now shifts to the assured to raise a defence under the reasonable assured test. Under the said test, the assured needs to prove that a reasonable assured, in his or her position, would not have expected that the insurer would like to know the concealed information during the process of underwriting. Similar to the prudent insurer test, the reasonable assured test will require the person who is responsible for the arrangement of insurance to testify about whether the concealed information would have been considered to be material for a prudent insurer from the perspective of a reasonable assured. Again, it is also upon the judge to decide whether the testimony is reliable. This approach can solve the problems that have been identified in the previous sub-sections. The new test considers the matter of materiality from the perspectives of both the assured and the insurer, which balance the interests of both parties to the insurance contract. This measure fixes the problem of the original materiality test that considers the matter of materiality from the perspective of the insurer only. The court can now examine the evidence that is submitted from the perspective of both the assured and the insurer, which has changed the "one-sided" situation in the original prudent insurer test. It is suggested that, under this new test, both the assured and the insurer are required to communicate with each other actively, and the parties to an insurance contract are encouraged to explicitly define the scope of material knowledge which is required to be submitted to the insurer. The assured is also encouraged to keep written

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<sup>232</sup> *ibid*

<sup>233</sup> *ibid* [147], [148], [156] and [158]

<sup>234</sup> The term "reasonable assured" is used in this section to distinguish with the "reasonable insured" test as proposed by the Law Commission in the 2007 paper.

records of the communications with the insurer during the process of disclosure. When a dispute arises in the court, the assured can then rely on the written records to prove that whether he or she has acted reasonably during the process of disclosure.

### **iii. The solution**

To adopt the third way materiality test, section 18(1) will be amended as follows:

(1)(a) 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 person who is responsible for the assured's insurance (the actual assured), and the assured is deemed to know every circumstance which, in the ordinary course of business, ought to be known by the actual assured, unless it is a knowledge of fraud perpetrated by the assured. If the assured fails to make such disclosure in the absence of a valid defence, the insurer may avoid the contract.

Section 18(1)(d) will be added as follows:-

For the purpose of section 18(1)(a), the assured is entitled to raise a defence on the ground that a reasonable assured would not have expected that the material circumstance is disclosable to the insurer.

It is submitted that the scope of the material information is encouraged to be agreed between the parties to an insurance contract during the process of disclosure. However, in a case that the scope of the disclosable knowledge is not agreed between the parties, then the court needs to examine the state of mind of the both the insurer and the assured in each case in order to determine whether the concealed information is material. Both the prudent insurer test and the reasonable assured test, that are adopted in the new materiality test for the law reform in Hong Kong, are objective tests.

The operation of the new test can be elaborated in the following hypothetical situations. In a case where the assured company is a newly established company, and the actual assured has no experience about insurance arrangement, the actual assured is not liable for non-disclosure if the assured reasonably believes that the concealed fact is immaterial for the insurer.

The test of what the reasonable assured is required to disclose is a matter of fact. For instance, in a situation where the assured and the insurer have renewed the same motor insurance contract for two times and the insurer has requested the assured to provide previous motor accident record for the purpose of risk assessment and calculation of premium, the assured cannot conceal previous motor accident record even if the insurer has failed to ask the assured to provide this information in the third renewal. The reason is that in the previous contract renewal, the assured should have learnt that the previous motor accident record, which had been requested by the insurer in the previous renewals, is material to the risk, and therefore he or she cannot rely on the second limb of the test to escape from the liability of non-disclosure.

In practice, the adoption of the third-way materiality test may also lead to a fairer outcome than the current prudent insurer test. For example, the problem that has been identified in the case *Lambert v Co-operative Insurance Society Ltd*<sup>235</sup> will no longer exist. The assured will not be liable for non-disclosure in that case, as a reasonable assured would not have expected that her husband's convictions of purchasing stolen goods are material information that needs to be disclosed for her insurance policy of jewellery.

Further, the new third-way materiality test may also solve the problem that has been identified in the case *Brit UW Ltd v F & B Trenchless Solutions Ltd*.<sup>236</sup> With the adoption of the third-way materiality test, both parties to the insurance contract in the *Brit UW Ltd*<sup>237</sup> case will be able to fairly testify on the matter of materiality in relation to the non-disclosure, and it has eliminated the chance for the court to give a biased judgment against the assured as the new test considers the matter of materiality from the perspective of both the assured and the insurer. It is suggested that the new third-way test can certainly ensure the fairness between the parties to an insurance contract, and it may also help to reduce the disputes in relation to non-disclosure in Hong Kong.

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<sup>235</sup> *Lambert* (n3)

<sup>236</sup> *Brit UW Ltd* (n58)

<sup>237</sup> *ibid*

## II. The problem of the inducement test – the absence of the inducement test from the legislation

### A. The problem of the subjective inducement test

#### i. The problem in relation to the actual inducement

The second problem of the duty of disclosure regards the inducement test. Before the enactment of the IA 2015, the subjective inducement test had been held to be an implied test with respect to the duty of disclosure in an insurance contract.<sup>238</sup> It is a myth that why such an obligation had not been expressly stated in section 18(2) of the MIA 1906. Nevertheless, case law indicated that the insurer had to satisfy both the objective materiality and subjective inducement tests in the case of non-disclosure. As far as the latter test is concerned, the insurer needed to prove that there was a subjective inducement by a non-disclosed knowledge,<sup>239</sup> but such knowledge need not be the only cause to form an insurance contract.<sup>240</sup> The test of the actual inducement was about “what the insurer would have done if the fact had been disclosed.”<sup>241</sup> The insurer needed to prove that “but for the assured’s presentation of the risk they would have acted differently, either by refusing to write the risk at all or by writing it only on different terms.”<sup>242</sup> In general, only an actual underwriter could prove an actual inducement.<sup>243</sup> The problem of proving actual inducement was well addressed by Colman J in his judgment in *North Star Shipping Ltd v Sphere Drake Insurance Plc*.<sup>244</sup> This case concerned a war risk policy of the vessel “The North Star”, and the insurer contended non-disclosure on the ground that the assured did not disclose several material facts to the insurers, some of which concerned criminal proceedings against the owner of the vessel. After carefully considering the evidence before him, Colman J held that the insurer was entitled to avoid the contract based on non-disclosure, as the non-disclosed facts of the criminal proceedings would have deterred the insurer to enter into the insurance contract with the assured.<sup>245</sup> Regarding the test of inducement, Colman J expressed his observation as follows:

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<sup>238</sup> *Pan Atlantic Insurance Co. Ltd* (n46) 105

<sup>239</sup> *Assicurazioni Generali SpA v ARIG Insurance Group* [2003] 1 Lloyd’s Rep IR 131 [62]

<sup>240</sup> *ibid* [62]

<sup>241</sup> Merkin (n42) para A-0768

<sup>242</sup> *ibid* para A-0764

<sup>243</sup> Gilman, Templeman, Blanchard, Hopkins and Hart (n38) para 15-39. The term “actual underwriter” means the particular person who assessed the risk in dispute.

<sup>244</sup> *North Star Shipping Ltd v Sphere Drake Insurance Plc* [2005] 2 Lloyd’s Rep 76, [2005] EWHC 665 (Comm)

<sup>245</sup> *ibid* [257] – [258]



In evaluating the underwriters' evidence it is important to keep firmly in mind that all their evidence is necessarily hypothetical and that hypothetical evidence by its very nature lends itself to exaggeration and embellishment in the interests of the party on whose behalf it is given. It is very easy for an underwriter to convince himself that he would have declined a risk or imposed special terms if given certain information. For this reason, such evidence has to be rigorously tested by reference to logical self-consistency, and to such independent evidence as may be available.<sup>246</sup>

In Hong Kong, the inducement test is also not explicitly stated in the MIO, and the legislation has not provided any guidance on this matter. It is suggested that the test is heavily relied on the judges to distinguish between the matter of facts and opinions of the insurer in relation to the inducement of the undisclosed knowledge. In a situation where judges are affected by the exaggerated opinion from the insurer, it may lead to an unfair result to the assured.

This approach also fails to consider the fact that the decision of risk undertaking is not solely based on the result of risk assessment, but it also involved some other considerations such as commercial interest and relationship. In addition, the MIA 1906 and MIO also did not require the insurer to act prudently in order to prove non-disclosure under both materiality and inducement tests, which suggests that the insurer can exaggerate the degree of inducement without any legal consequence.<sup>247</sup> Nevertheless, it is noteworthy that the actual inducement test is a subjective test and regardless of the matter of exaggeration, the insurer still needs to meet the subjective test and proves that the breach of duty of disclosure induced the contract. Cases subsequent to the *North Star Shipping* case<sup>248</sup> also did not reflect the problem of exaggeration in relation to the effect of the actual inducement of the non-disclosure.<sup>249</sup> In this regard, the

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<sup>246</sup> *ibid* [254]

<sup>247</sup> It is noteworthy that Lord Mustill made a deduction that the insurer is presumed to be reasonable under the law because in the old days a party to a suit was not allowed to testify on his or her own behalf. See *Pan Atlantic* (n46), 117

<sup>248</sup> *North Star Shipping* (n247)

<sup>249</sup> See, *Zeller v British Caymanian Insurance* [2008] Lloyd's Rep IR 545, *Crane v Hannover* [2010] Lloyd's Rep IR 93, *A C Ward v Catlin (Five)* [2010] Lloyd's Rep IR 695, *Persimmon Homes v Great Lakes* [2011] Lloyd's Rep IR 101, *Bate v Aviva Insurance UK Ltd* [2014] Lloyd's Rep. IR 527, *Sea Glory Maritime Co and Another v AL Sagr National Insurance Co (The "MV Nancy")* [2014] Lloyd's Rep IR 112, *Involnert Management Inc v Aprilgrange Ltd and Others Ais Insurance Services Ltd (First Third Party) Oamps Special Risks Ltd (Second Third Party)* [2015] Lloyd's Rep. IR 661, *Axa Versicherung Ag v Arab Insurance Group (BSC)* [2015] Lloyd's Rep. IR Plus 31 and *Brit Uw Ltd v F & B Trenchless Solutions Ltd* [2016] Lloyd's Rep. IR 69

problem of exaggeration, as identified in the *North Star Shipping* case,<sup>250</sup> may have little significance.

**ii. The problem in relation to the presumption of inducement**

The other problem of the inducement test regards the presumption of inducement. In *Assicurazioni Generali SpA v ARIG*,<sup>251</sup> Lord Justice Clarke held that, there was no presumption of inducement merely based on the fact that the concealed-facts were proved material.<sup>252</sup> Nevertheless, there are situations that inducement can be presumed in non-disclosure cases. In *St. Paul Fire & Marine Insurance Co. (UK) Ltd. v McConnell Dowell Constructors Ltd. and others*,<sup>253</sup> the appellants were the construction companies on the Marshall Islands. The appellants had purchased a Contractors All Risks policy, which was underwritten by the respondent and other three insurance companies. A serious subsidence had occurred in the construction site of the appellants, and the appellants launched a claim against the respondent under the insurance policy. The respondent discovered that the appellants had not disclosed two reports which concerned the soil investigation and also the design of the foundation of the buildings within the construction site, and thus the respondent rejected the claim. The Court of Appeal held that the appellants were liable for non-disclosure and misrepresentation. However, with respect to the proof of inducement, three of the four insurers had given evidence on the effect of the concealed reports, but the last insurer, which was Prudential Assurance Co, had not given any evidence on the issue of actual inducement, as the actual underwriter had left Prudential.<sup>254</sup> The Court of Appeal, therefore, had to decide on whether Prudential could rely on a presumption of inducement to discharge the burden of proving inducement. Relying on the evidence that was given by the three underwriters other than Prudential, the Court of Appeal held that “There is no evidence to displace a presumption that Mr. Earnshaw like the other three was induced by the non-disclosure or misrepresentation to give cover on the terms on which he did. In my judgment, these insurers also have discharged their burden of proof.”<sup>255</sup> Although a

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<sup>250</sup> *North Star Shipping* (n247)

<sup>251</sup> *Assicurazioni Generali SpA* (n242)

<sup>252</sup> *ibid* [62]

<sup>253</sup> *St. Paul Fire* (n179)

<sup>254</sup> *ibid* 121

<sup>255</sup> *ibid* 127

presumption of inducement was successfully applied in the *St. Paul Fire & Marine Insurance Co. (UK) Ltd.* case,<sup>256</sup> it is noteworthy that such a presumption was rebuttable by the assured.

The use of presumption of inducement in the *St. Paul Fire & Marine Insurance Co. (UK) Ltd.* case<sup>257</sup> was followed by a more recent case *International Management Group (UK) Ltd v Simmonds*.<sup>258</sup> This case concerned a cancellation insurance policy, which covered a series of cricket matches between the India team and Pakistan team. The claimant had signed an agreement for broadcasting the matches, but the matches in September 2000 were eventually cancelled by the government of India. The claimant launched a claim against the respondent under the policy. The respondent discovered that the claimant had concealed material fact which was related to the government permission of the cricket matches prior to the formation of the contract, and thus the respondent avoided the contract on the grounds of non-disclosure and misrepresentation.<sup>259</sup> The court held that the respondent was entitled to avoid the insurance contract. One of the following insurers, Brockbank Syndicate, could not submit any evidence on the matter of actual inducement, as the actual underwriter had left the company and made a request to obtain unauthorised information from the company in exchange of his submission to the court. The court held that Brockbank Syndicate was not obliged to comply with the request of the actual underwriter, and the court had to decide on whether a presumption of inducement could be applied in this case. Since the respondent was one of the two leading underwriters for the insurance policy, the court held that the following underwriters in this case were entitled to rely on the presumption of inducement.<sup>260</sup> Therefore, it is suggested that in the case of an insurance risk which is underwritten by co-insurers, the followers of the leading underwriter are entitled to rely on a presumption of inducement if the leading underwriter can successfully prove the actual inducement in a non-disclosure case.

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<sup>256</sup> *ibid*

<sup>257</sup> *ibid*

<sup>258</sup> *International Management Group (UK) Ltd v Simmonds* [2004] 1 Lloyd's Law Rep IR 247, [2003] EWHC 177 (Comm)

<sup>259</sup> It is noteworthy that in this case, the respondent was entitled to reject the claim on the ground of breaching an express warranty.

<sup>260</sup> [151] – [152]

Another situation, where a presumption of inducement is applicable, is that the actual underwriter is absent from the court with a good reason. In *Mundi v Lincoln Assurance Ltd*,<sup>261</sup> it concerned a life insurance contract that commenced in June 1997. During the contract period, the husband of the assured deceased, and the assured launched a claim against the insurer, but the insurer rejected the claim based on non-disclosure of a series of medical records, which suggested that the husband was not in a good health condition. Although the actual underwriter was not available to submit evidence for this case, the court concluded that the underwriter was entitled to rely on a presumption of inducement and the contract was avoided on the ground of non-disclosure.<sup>262</sup>

It is suggested that the judge had drawn a reasonable inference on the presumption of inducement in the *Mundi* case.<sup>263</sup> Nevertheless, it is noteworthy that a presumption of inducement may not be applicable when the actual underwriter is not available without an acceptable reason. In *Lewis v Norwich Union Healthcare Ltd*,<sup>264</sup> this case concerned a risk of income protection, and the insurance contract was commenced on 1<sup>st</sup> January 2000. During the underwriting process, the assured had disclosed to the insurer that he had suffered from bowel syndrome and also neck pain. In 2002, the assured claimed against the insurer on the grounds that he had suffered from incontinence and back injury, and as a result, the assured was incapable of returning to work. Upon investigation, the insurer discovered that the assured had visited his doctor on 26<sup>th</sup> July 1999, and this visit was not disclosed to the insurer. In this regard, the insurer avoided the insurance contract on the ground of non-disclosure.

The judge held that in this case, firstly, the matter of materiality was not in dispute, as the underwriting experts of both parties had agreed that the visit on 26<sup>th</sup> July 1999 was a material fact. The issue, therefore, came to the test of inducement. The insurer, in this case, had not called any evidence from the actual underwriter, Ms Ford, who had left the insurance company in 2005. The judge held that in this situation, it was relied on the court to make reasonable

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<sup>261</sup> *Mundi v Lincoln Assurance Ltd* [2006] 1 Lloyd's Rep IR 353

<sup>262</sup> *ibid* [68]

<sup>263</sup> *ibid*

<sup>264</sup> *Lewis v Norwich Union Healthcare Ltd* [2010] Lloyd's Rep. IR 198

inference on the matter of inducement, namely, to infer what the actual underwriter would have thought in the situation when the visit of the assured was disclosed to Ms Ford.<sup>265</sup>

Judging from the evidence before him, the learned judge held that the expert evidence, which was submitted by the insurer in order to prove inducement, was not accepted by the court, as the actual underwriter had not acted as prudent as the expert witnesses of the insurer.<sup>266</sup> The court also examined the evidence from the assured and concluded that the actual underwriter would not have been induced by the visit on 26<sup>th</sup> July 1999, as the visit concerned a knee pain of the assured, and the doctor had found nothing abnormal. Therefore, the court held that the insurer was not entitled to avoid the insurance contract on the ground of non-disclosure. Although the judges in England and Wales had carefully exercised their discretion in applying the presumption of inducement, it is suggested that the legislation in Hong Kong should provide a clear guidance on the application of the said presumption. The problem of the current legislation in Hong Kong, in relation to the unclear scope of application of the presumption of inducement, can be found in a Hong Kong case *Lam Charn Yung v Axa China Region Insurance Company (Bermuda) Ltd formerly known as National Mutual Insurance Company (Bermuda) LTD*.<sup>267</sup>

In this case, the plaintiff was the assured who suffered from breast cancer, and the defendant was the insurer, who issued a life insurance policy to the assured dated 19<sup>th</sup> March 1997. The assured submitted a claim form on 12<sup>th</sup> May 1998 to notify the insurer that she was confirmed to suffer from breast cancer in a medical examination. Upon further investigation, the insurer rejected the claim and rescinded the contract based on material non-disclosure, as the assured did not disclose to the insurer that the mass in the assured's breast was first noticed by the assured during a medical examination on 24<sup>th</sup> September 1996, which was prior to the conclusion of the insurance policy. The assured insisted that there was no material non-disclosure, as at the time being it was not confirmed that the indefinite breast mass, together with the breast pain, amounted to the breast cancer.

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<sup>265</sup> *ibid* [94]

<sup>266</sup> *ibid* [94]

<sup>267</sup> *Lam Charn Yung v Axa China Region Insurance Company (Bermuda) Ltd formerly known as National Mutual Insurance Company (Bermuda) LTD DCCJ1522/2004*

Mr. Justice Ng held that the assured was liable for breaching the duty of disclosure. Firstly, he had underlined the law that the non-disclosure need not be fraudulent or negligent, and the mentality of the assured was irrelevant in respect of the duty of disclosure.<sup>268</sup> Mr. Justice Ng further held that the understanding of the assured was also irrelevant when deciding whether certain information was material to the insurer.<sup>269</sup>

Mr. Justice Ng had also explained in his judgment about his understanding of the presumption of inducement, where he had cited *MacGillivray on Insurance Law*<sup>270</sup> to support his understanding.<sup>271</sup> At the end of his judgment, Mr. Justice Ng held that the insurer was entitled to rely on a presumption of inducement to discharge its burden of proving non-disclosure.<sup>272</sup> However, the author would like to highlight how Mr. Justice Ng relied on the passage of *MacGillivray on Insurance Law* to establish the presumption of inducement. Firstly, Mr. Justice Ng expressed his opinion on the materiality of the undisclosed document:

Here I have found that the materiality of the undisclosed matters was obvious (see paragraphs 121-123 above) and Mr Chan gave evidence that if the underwriter had been told about the undisclosed material information in respect of the 24/9/96 and 3/1/97 FPA Visits, he would have called for further information and in all probability either refused the risk or accepted it on different terms.<sup>273</sup>

He further commented on the performance of the insurer as follows:

In my view, a prudent insurer would have carried out further investigations either with the Plaintiff and/or the FPA or sought independent medical or gynaecological opinion/tests in relation to the Plaintiff's breast condition before risk appraisal. But National Mutual accepted the Application without any relevant enquiries.<sup>274</sup>

Mr. Justice Ng then turned to the reason why the actual underwriter did not testify for this case. The reason was that the actual underwriter had left the company and was working for a

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<sup>268</sup> *ibid* [39]

<sup>269</sup> *ibid* [40]

<sup>270</sup> Birds, Milnes; Lynch (n39)

<sup>271</sup> Lam Charn Yung (n270) [150]

<sup>272</sup> *ibid* [151]

<sup>273</sup> *ibid* [151]

<sup>274</sup> *ibid* [151]

competitor of the insurer, which Mr. Justice Ng found it an acceptable reason.<sup>275</sup> Mr. Justice Ng then concluded his judgment as follows:

I therefore accept that a presumption arose in favour of the Defendant that National Mutual was induced by the Plaintiff's non-disclosure and/or misrepresentations to issue the Policy on the terms it did. The Plaintiff did not adduce any contradictory evidence to displace such presumption. In my view, the Defendant has on balance discharged its burden of proof.<sup>276</sup>

To sum up, Mr. Justice Ng had relied on English law principles to determine whether the presumption of inducement was applicable to the case that the actual underwriter was absent from the court with a good reason. Nevertheless, it is suggested that the position of English law may not have been entirely clear on this issue. In *Axa Versicherung Ag* case,<sup>277</sup> Mr Justice Males expressed his comment on the matter of presumption of inducement as follows:

It is sometimes said that the presumption of inducement will only come into play in cases in which for good reason the insurer is unable to call the underwriter who wrote the risk in question. I doubt, however, whether this is a rule of law, although no doubt it will generally be true as a matter of fact.<sup>278</sup>

The application of the presumption of inducement, as suggested by the Mr Justice Males, was not a rule of law, but it was a matter of fact which was subject to the reasonable inference from the court. Although it is suggested that Mr. Justice Ng was correct to hold in favour of the insurer in the *Lam Charn Yung* case,<sup>279</sup> it is suggested that Hong Kong judges who will follow the approach in *Lam Charn Yung* case<sup>280</sup> in the future may not be able to aware that such an application of the presumption of inducement is not a rule of law, and the application of the said presumption should be exercised with great caution. In this regard, it is suggested that a clear guidance should be provided for the law reform in Hong Kong in order to avoid potential injustice that may be caused by the misuse of the said presumption.

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<sup>275</sup> *ibid* [151]

<sup>276</sup> *ibid* [151]

<sup>277</sup> *Axa Versicherung Ag* (n170) [119]

<sup>278</sup> [119]

<sup>279</sup> *Lam Charn Yung* (n270)

<sup>280</sup> *ibid*

Furthermore, due to the competitive nature of the insurance market and also the high level of labour mobility, it is not uncommon that the actual underwriter will not be able to testify due to his or her resignation. This approach may lead to a “short-cut” for the insurer to avoid proving inducement when the actual underwriter has acted negligently during the process of risk assessment, as the decision of risk acceptance may not be solely based on the materiality of the disclosed information, but it may also be based on some other considerations, for example, commercial interest or business relationship between the parties.<sup>281</sup> Therefore, a mere presumption of inducement, which is solely based on the materiality of the undisclosed facts, may be unfair to the assured. In this regard, it is submitted that a radical reform should be proposed on the inducement test regarding the duty of disclosure in Hong Kong commercial insurance law, the purpose of which is to clarify the proper application of the inducement test, and also ensures that the assured will be treated fairly under the test.

### **iii. The inducement test in the IA 2015 is insufficient to solve the problems**

Under the IA 2015, the insurer is now required to prove inducement in order to seek remedies, and now there are different degrees of inducement that the insurer is required to establish. Although the real operation of the new inducement test is still a myth, the author will provide some observations on the new inducement test and suggest whether the new inducement test is a good precedent for Hong Kong to follow.

Section 8(1) of the IA 2015 states that:

- (1) The insurer has a remedy against the insured for a breach of the duty of fair presentation only if the insurer shows that, but for the breach, the insurer—
  - (a) would not have entered into the contract of insurance at all, or
  - (b) would have done so only on different terms.

Although the term “inducement” is not explicitly stated in this section, it is suggested that section 8 of the IA 2015 aims to concatenate the inducement test and the proportionate remedies and in a sense, section 8 has codified the inducement test.<sup>282</sup> The remedy, which the insurer is entitled in a case of breaching the duty of fair presentation, depends on the action that the

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<sup>281</sup> Merkin (n42) A0-773

<sup>282</sup> Explanatory notes to the Insurance Bill 2015 (n29) para 78



insurer would have been taken if the risk was fairly presented. In addition, the breach of the duty is now divided into two categories, namely either reckless or deliberate, and neither reckless nor deliberate.<sup>283</sup>

The positive effect of this section is that the insurer is now more flexible to select the remedies for the breach of the duty, and the new section has ensured that the assured will no longer need to face an “all or nothing” situation regarding the breach of the duty. It is no doubt that section 8(1) of the IA 2015 has required the insurer to prove inducement in order to seek remedy against the assured when there is a breach of the duty of fair presentation, which is a better approach than the implied inducement test in the MIA 1906 and MIO. Nevertheless, the IA 2015 has not provided guidance on how the actual inducement can be proved. The IA 2015 also has not addressed the issue of the presumption of inducement, in particular, the application of such a presumption where the insurer is not available to testify in the court. In this regard, it is suggested that the IA 2015 has not solved the problems of the current inducement test in Hong Kong, and a reform of legislation is needed in Hong Kong.

It may be arguable that case law has already explained how the inducement test is operated and thus, there is no necessity to reform the legislation in Hong Kong. Nevertheless, in the situation where the reader has no or little knowledge of insurance law, it may not be easy for the said reader to identify the relevant cases. In this regard, it is submitted that if a detailed guidance can be provided in the legislation, the requirements of the inducement test will be more accessible to the reader of the legislation.

#### **B. Formulating the reform for the inducement test of the duty of disclosure - the detailed inducement test**

For the inducement test in relation to non-disclosure, it is suggested that a detailed guidance should be provided for the application of the said test. Firstly, for the actual inducement test, as it is a subjective test which the insurer may exaggerate the actual degree of inducement, it is suggested that a clear guidance should be given in order to prevent the insurer from abusing

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<sup>283</sup> This part of the IA 2015 will be examined in chapter 4 of this thesis in detail.

the test. Secondly, for the application of the presumption of inducement, it is suggested that the legislation should restrict the use of the presumption in limited circumstances only.

**i. The additional requirement for the insurer proving actual inducement**

The major problem of the actual inducement test is that during the process of underwriting, the insurer is still relied on his or her experience, rather than a systematic approach, to determine whether he or she should underwrite a risk or not. In *Highlands Insurance Co. v. Continental Insurance Co.*,<sup>284</sup> Mr. Justice Steyn commented on the nature of underwriting, and stated that “Underwriting is not a science: it is a matter of judgment. Taking into account the differences relating to interest, type of business, information as to loss record, protections, premium, line, total exposure, and so forth...”<sup>285</sup>

Therefore, when the insurer is requested to testify about the degree of inducement in a non-disclosure case, the insurer is likely to testify in accordance with his or her own subjective view. This experiential approach suggests that there is no measure to prevent the insurer to overestimate or exaggerate the effect of the inducement. Nevertheless, the experiential nature of the underwriting judgment does not prevent the underwriter from developing a systematic approach in relation to risk underwriting. For instance, in the case *Drake Insurance v. Provident Insurance*,<sup>286</sup> the motor insurance premium of the Provident Insurance was calculated by a points system, the judgment of which was based on the past driving records of the assured. Under this system, speed conviction within the past 5 years carried 10 points and an accident that involved “fault” element carried 15 points. The judgment of the underwriter would have been depended on the total add up to the points. If the assured scored below 17 points, the insurer would have charged the assured a normal premium. If the assured scored 17 to 59 points, the assured would have been charged with a higher premium in proportion to the score of the points system. If the assured scored 60 points or above, the risk would have been declined by the insurer. With the adoption of a similar systematic underwriting criterion, the judgment of underwriting is no longer a subjective view of the actual underwriter only, but also a

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<sup>284</sup> *Highlands Insurance Co. v. Continental Insurance Co.* [1987] 1 Lloyd's Rep. 109. It should be noted that this case was held in 1987, but the nature of insurance underwriting had not been changed since then regardless of the use of modern technology.

<sup>285</sup> *ibid* 114

<sup>286</sup> *Drake Insurance* (n181)

matter of fact with objective element, and the insurer is unlikely to exaggerate the effect of the inducement. A systematic underwriting criterion is easier for the court to determine the actual effect of the inducement as there is an objective system to follow, and it ensures that the court can determine the effect of the inducement fairly. Therefore, the reform of the inducement test should encourage the use of a systematic criterion for the underwriting process.

## **ii. The restriction of the application of the presumption of inducement**

The second problem of the inducement test is about the application of the presumption of inducement. As suggested in the previous sub-sections, the complexity of the presumption of inducement may lead to the misuse or abuse of the said presumption by the insurer, and therefore the legislation in Hong Kong should clarify the use of the said presumption. The reform should unambitiously restrict the use of the presumption of inducement in two situations only. Firstly, the presumption is only applicable to the following underwriters when the leading underwriter has proved actual inducement. This is a reasonable measure as in most cases which involve co-insurers, although the underwriting decision is made independently by each insurer, it is highly likely that the judgment of the leading underwriter may affect the decision making process of each of the following underwriter.<sup>287</sup> It may also be impractical to require all following underwriters to prove actual inducement in non-disclosure cases, as it is unlikely that the following underwriters may have any direct communication with the assured and thus it is difficult for them to prove actual inducement.

Secondly, it is suggested that the presumption of inducement is only applicable when the actual underwriter is absent from court with a good reason. It is suggested that the requirement of good reason is not clearly identified, and it is upon the judges to examine the conditions of each cases. For instance, as suggested in *International Management Group (UK) Ltd* case,<sup>288</sup> a request of obtaining unauthorised information from an actual underwriter who had left the company amounted to a good reason for the application of the said inducement. As the presumption of inducement may provide a “shortcut” approach for the insurer to escape from

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<sup>287</sup> See *Assicurazioni Generali SpA* (n242) for the discussion about the significance of the leading underwriter in the case of involving co-insurers.

<sup>288</sup> *International Management Group (UK) Ltd* (n261)

the liability of proving inducement, the legislation should also make clear to the reader of the law that the said presumption should only be applied with great caution.

### **iii. The solution**

To introduce the detailed inducement test in the Hong Kong legislation, firstly, it is necessary to underline the inducement test in the legislation expressly. Section 18(1) of the MIO should be amended as follows:

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, had the required disclosure been made, the insurer would not have entered into the contract on any terms, the insurer may avoid the contract.

To further explain the operation of the actual inducement test and the presumption of inducement, section 18(2)(b) should be added as follows:

For the purpose of section 18(1), whether the insurer is induced by the assured's disclosure or not, in each case, is a question of fact, and there should not be a presumption of inducement unless there is a justifiable ground for such a presumption.

This provision expressly includes the requirement of inducement under the duty of disclosure. It is suggested that as a reform solution, the underwriter can only submit the evidence regarding the degree of actual inducement from two categories. Firstly, the insurer can only prove actual inducement of a non-disclosed information by submitting a record of a similar case which he or she handled in the past. The submitted case, as an evidence, needs to demonstrate that the underwriter faced a similar case before, but he or she rejected to underwrite the risk due to the disclosure of such material knowledge. Secondly, the underwriter can only prove actual inducement by referring to a systematic underwriting criterion which is used in his or her company, and he or she has strictly complied with the criterion. With the adoption of these new requirements, the proof of actual inducement becomes a matter of fact rather than a matter of opinion, which ensures that the judge will not be unduly influenced by the subjective view of the

insurer. It also ensures that the assured can be protected from the biased testimony of the insurer.

Nevertheless, it is understandable that the above two requirements are too idealistic, and it may be unfair to the insurer if he or she cannot submit evidence outside the said categories. Therefore, the reform should not impose these two requirements as compulsory requirements of the law, but they should be referred as persuasive evidence which the court should give weight to. The underwriters are still allowed to submit their own subjective opinions, but it is suggested that the court should give less weight to such subjective evidence.

### **III. Conclusion**

To conclude, the current materiality test in Hong Kong is too difficult for the assured to understand and comply with it. At times, even the practitioners can be confused with the requirement of proving materiality. In relation to the application of the presumption of inducement, it may lead to an unfair result that the insurer can rely on the presumption to escape from its liability to prove inducement.

Although the IA 2015 has not imposed any fundamental reform with regard to the materiality test and inducement test, nevertheless, it is suggested that there are two elements which are worthy for the legislator in Hong Kong to take into account when considering the reform of the duty of disclosure in Hong Kong. Firstly, it is the reasonable insured test which is eventually abandoned by the Law Commission. Although the test itself may not be sufficient to ensure fairness in relation to the risk assessment, nevertheless, it is certain that the test has significantly addressed some issues that the current materiality test has failed to deal with. For instance, in the *North Star Shipping v Sphere Drake Insurance*,<sup>289</sup> Lord Justice Waller has expressed his concern on the potential injustice that may be caused by the current state of law regarding the disclosure of moral hazard, and he suggested that the Law Commission should further review the possibility of adopting the reasonable insured test to confine these injustices.<sup>290</sup>

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<sup>289</sup> *North Star Shipping* (n247)

<sup>290</sup> *ibid* [19] – [20]

Secondly, the IA 2015 has concatenated the degree of inducement with the proportionate remedies, which aims to provide a more flexible approach in comparison to the old single remedy approach in the MIO and the MIA 1906. Nevertheless, since the IA 2015 has not imposed any change of the requirement of proving inducement, it is suggested that detailed guidelines of the inducement test should be developed in Hong Kong in order to prevent the potential injustices that may arise from the application of the current inducement test.

In relation to the original reform suggestions, the author would like to emphasise the effect of these suggestions from two perspectives. Firstly, in relation to the third-way materiality test, the core rationale of the test is that it encourages both the assured and the insurer to communicate during the process of information disclosure actively. The new test also encourages the assured and the insurer to agree on a scope of information that is material to the risk. If the matter of materiality can be mutually understood and committed by both parties to an insurance contract at the pre-contractual stage, then it may lead to a positive result and there will be fewer disputes about non-disclosure.

In relation to the detailed actual inducement test, it is submitted that the additional requirement of proving actual inducement can moderate the unfair situation which is likely to be dominated by the exaggerated views of the insurers. In addition, the reform has provided a detailed guidance on the application of the presumption of inducement, the purpose of which is to ensure that the insurer cannot escape from its own liability to prove inducement, as it is a crucial requirement for the insurer to prove that the non-disclosure of the assured has affected the decision making of the insurer. If the actual inducement cannot be proved, then the insurer should not be entitled to avoid the insurance contract. In any event, it is submitted that both the materiality and inducement tests in Hong Kong are insufficient to ensure fairness between the parties to an insurance contract, and it is certain that the law is in need of reform. The detailed reform proposal will be provided in chapter 6 of this thesis.

## Chapter 3 Misrepresentation In The Marine Insurance Ordinance

This chapter will examine the two major problems for the duty not to misrepresent in relation to utmost good faith.<sup>291</sup> Firstly, the problem is that the inducement test is poorly defined. Since the inducement tests of non-disclosure and misrepresentation were not expressly stated in the legislation, one had to look up the definition of the tests in the case authorities; however, they did not provide a clear answer to this question. While the majority of case law<sup>292</sup> suggested that the two inducement tests shared similar characteristics and legal requirements, there was a case authority, namely *Involnert Management Inc. v Aprilgrange Ltd and others*,<sup>293</sup> which suggested that the two inducement tests were different. The existence of the *Involnert Management Inc*<sup>294</sup> case highlights the problem that, without the written inducement tests in the legislation, the interpretation of the tests will remain vague, and the results of disputes will be unpredictable, as the tests are open to interpretation of the judges. To avoid confusion in this area of law, it is submitted that a specific inducement test should be stated in the legislation.

The second problem is that the current law is not clear as to whether the Misrepresentation Ordinance, which is identical to the Misrepresentation Act 1967 in England and Wales, is applicable to utmost good faith cases. This issue is complicated by the different evolutions of the law of misrepresentation under utmost good faith and general contract law. As discussed in the introduction of this thesis, the duty not to misrepresent and the duty of disclosure originated from the duty of utmost good faith. In the 18<sup>th</sup> century, the duty of utmost good faith was incorporated into common law by Lord Mansfield in the judgment of *Carter v Boehm*,<sup>295</sup> the purpose of which was to 'harmonise the law merchant and the common law'.<sup>296</sup> Later, Sir Mackenzie D Chalmers drafted the Marine Insurance Act 1906, and it came into force on 21<sup>st</sup> December 1906. The remedy of avoidance was the only remedy available for the party who suffered from misrepresentation under the duty of utmost good faith. In this regard, the juristic

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<sup>291</sup> Although these two problems were not observed by the Hong Kong scholars and judges, the author alleged that they may also occur in Hong Kong, as the law of Hong Kong and England and Wales are of similar nature.

<sup>292</sup> See, for example, *Pan Atlantic* (n46), *Wise Ltd* (n40) and *Limit No. 2 Ltd v Axa Versicherung AG* [2008] Lloyd's Rep 330

<sup>293</sup> *Involnert Management Inc. v Aprilgrange Ltd and others* [2015] 2 Lloyd's Law Rep. 289

<sup>294</sup> *ibid*

<sup>295</sup> *Carter* (n1)

<sup>296</sup> Eggers, Picken and Foss, (n56) para 1.11

basis of misrepresentation concerning utmost good faith switched from a plain common law duty to the one that comprised both statutory and common law.

In general contract law, the development of the doctrine of misrepresentation is less straightforward; as Rix J put it, the law was developed in a “piece meal manner”.<sup>297</sup> It remained a hybrid of common law and equity until the enactment of the Misrepresentation Act 1967.<sup>298</sup> Most significantly, the remedy of damages was allowed to be granted by the court upon discretion in lieu of or in addition to the remedy of rescission.

It is evident from the above observation that the development of the doctrine of misrepresentation about utmost good faith is different from the same doctrine under general contract law, but there is no clear indication as to whether the Misrepresentation Ordinance is applicable to utmost good faith cases. The major problem is that the insurer may treat the Misrepresentation Ordinance as an alternative way, in addition to the current duty of utmost good faith, which is already draconian to the assured, to escape from the liability of paying indemnity. This problem will no doubt worsen the situation of the assured in utmost good faith cases. To avoid this unfair situation, a reform solution should be proposed to forbid the application of the Misrepresentation Ordinance in utmost good faith cases.

To examine the above two problems and provide reform suggestions, this chapter will be divided into two sections. The first section concerns why a written inducement test is desired for both non-disclosure and misrepresentation. The main reason for such a reform suggestion is that without a written inducement test, the reader of the law will be confused by the question of whether non-disclosure shares the same inducement test with misrepresentation. In this regard, there are two research questions to be considered. Firstly, the question is whether non-disclosure is distinguishable from misrepresentation. Secondly, the question is whether non-disclosure shares the same inducement test with misrepresentation. At the end of the section, a written inducement tests will be formulated based on the answers to these research questions.

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<sup>297</sup> *Avon Insurance plc & Ors v Swire Fraser Ltd & Anor.* [2000] C.L.C. 665 [20]. See also H.G. Beale (ed.), *Chitty on Contracts* vol. 1 (32nd edn. Thomas Reuters, 2015 and Second Supplement 2017) para 7-001, which suggested that the law of misrepresentation is developed in a piece meal manner.

<sup>298</sup> *ibid* para 7-001



The second section of this chapter identifies the problem of the applicability of the Misrepresentation Ordinance in utmost good faith cases. It is submitted that such an application should not be allowed for two reasons. Firstly, the Misrepresentation Act 1967, as the origin of the Misrepresentation Ordinance, was not designed to be applicable to the cases in relation to utmost good faith, and therefore, an application of the Misrepresentation Ordinance may cause potential injustice to the parties to the insurance contract. Secondly, the case authorities of insurance contract law in England and Wales also suggested that the application of the Misrepresentation Act 1967 was undesirable in the context of utmost good faith. This section will be concluded with a solution to the problem, which is an express statement in the MIO forbidding the application of the Misrepresentation Ordinance to utmost good faith cases.

**I. The first problem of the duty not to misrepresent – the invisible inducement test**

The first problem of the duty not to misrepresent regards the requirement of proving inducement. The test is not stated in the legislation, and therefore case law is solely relied upon to define the scope of the test. However, there are at least two questions that are not adequately addressed by case law in this area of law. Firstly, the question is whether non-disclosure is distinguishable from misrepresentation in terms of the legal requirement and effect. The significance of this question is that if they are not distinguishable, then it may not be likely that the inducement tests are the same, and vice versa.

Secondly, the question is whether non-disclosure shares the same inducement test with misrepresentation about the proof of causation. The significance of this question is that even when non-disclosure and misrepresentation are two distinct concepts, they may still share the same inducement test. At present, the reader of the law may have different interpretations of the inducement tests, the adverse effect of which is that without a unified definition of the tests, the duties may not be objectively assessed by the practitioners, properly explained to the assured and fairly applied in different disputes. It is therefore submitted that to formulate a reform solution on this problem; the two research questions, as mentioned above, need to be carefully considered and answered.

### **A. Is non-disclosure distinguishable from misrepresentation in the context of utmost good faith?**

Judging from the layout of the MIO, one may easily observe that non-disclosure, which is governed by section 18 of the legislation, is entirely different from misrepresentation, which is governed by section 20 of the legislation. In short, these duties are different as non-disclosure involves a concealment of material fact, and misrepresentation involves a false representation. However, in the case authorities, it has been suggesting that the two duties are practically indistinguishable. The classic judgment of the *Pan Atlantic Insurance Co Ltd*<sup>299</sup> case suggested that in many situations, it was very difficult to be aware of the slight difference between non-disclosure and misrepresentation.<sup>300</sup> Subsequent cases in England and Wales follow this view without criticism, and the usual expression is that non-disclosure and misrepresentation are “both sides of the same coin.”<sup>301</sup> This position in English law is followed by Hong Kong judge in the case *The Ming An Insurance Co. (H.K.) -Ltd v Chan Man Dun and Chan Sze Lok*,<sup>302</sup> where non-disclosure and misrepresentation were being considered together by the judge as a whole, rather than as two separate duties.<sup>303</sup> Therefore, it is suggested that there is no definite answer to the question of whether non-disclosure and misrepresentation are distinguishable. In theory, these two duties are different, but in practice, the difference is insignificant. This vague answer, however, is the cause of the major problem of the operation of the duties, which is about the requirement of proving inducement for both non-disclosure and misrepresentation.

The paradox of this area of law is that if non-disclosure and misrepresentation are two distinguishable duties, these duties should be subjected to different requirements to prove materiality and inducement. While both section 18 and section 20 have expressly defined the materiality tests, which are identical to each other, the tests of inducement are not mentioned in the legislation. Since there is no answer to the question of whether non-disclosure is distinguishable from misrepresentation, the reader of the law is unable to make a reasonable deduction about whether these two duties share the same or different inducement tests. This phenomenon reveals that there are problems of accessibility and predictability in this area of

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<sup>299</sup> *Pan Atlantic* (n46)

<sup>300</sup> *ibid* 133

<sup>301</sup> See, for example, *Wise Ltd* (n40) [46] and *Limit No. 2 Ltd* (n295) [81]

<sup>302</sup> *The Ming An Insurance Co. (H.K.) Ltd v Chan Man Dun and Chan Sze Lok* HCMP2437/2004

<sup>303</sup> *ibid* [36]

law. The most significant problem is that without a written inducement test stated in the legislation, it is difficult for the reader of the law to observe an objective standard of the inducement tests that can be fairly and equally applicable to all utmost good faith cases. Although this problem was not revealed in Hong Kong case authorities, the case *Involnert Management Inc.*<sup>304</sup> in England and Wales indicated that this problem was not fictional, and the judgment of this case will be analysed in the next sub-section in order to examine the question of whether the inducement test of non-disclosure should be the same as misrepresentation.

**B. The same or different inducement test? The case analysis of *Involnert Management Inc. v Aprilgrange Ltd and Others***

The *Involnert Management Inc. v Aprilgrange Ltd and others*<sup>305</sup> case concerned a yacht insurance, where the insurer pleaded that the assured had breached the duty of utmost good faith on two grounds. Firstly, the insurer alleged that the assured did not disclose the actual value of the yacht. While the assured submitted that the actual value of the yacht was €13 million, it was later discovered by the insurer that the actual value of the yacht was in the range €7 and €8.5 million only. Secondly, the insurer alleged that the market value of the yacht was misrepresented by the assured. The assured submitted to the insurer that the value of the yacht was believed to be €13 million. However, the insurer discovered that it was a mistaken belief. Evidence suggested that the assured intended to sell the yacht at the amount of €8 million, which indicated that the assured did not have reasonable belief that the yacht was worth €13 million.

Mr. Justice Leggatt held that the insurer was entitled to avoid the insurance contract on the ground of non-disclosure of the actual market value, but rejected the pleading of misrepresentation in relation to the belief of the assured about the value of the yacht. The learned judge stated in his judgment that, in the case of non-disclosure, the question of inducement was about “what the insurer would have done if told that fact.”<sup>306</sup> On the contrary, in

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<sup>304</sup> *Involnert Management Inc.* (n296)

<sup>305</sup> *Involnert Management Inc.* (n296)

<sup>306</sup> *ibid* [214]

the case of misrepresentation, the question of inducement was about “what the insurer would have done in the absence of that representation.”<sup>307</sup>

It appears that the wording of the above two questions, as identified by Mr. Justice Leggatt, is different. However, as discussed in the previous sub-section, case authorities did not indicate a fundamental difference between the two inducement tests in a practical sense. Nevertheless, Mr. Justice Leggatt further elaborated that the distinction was not academic, but rather a practical difference that would lead to different outcomes under the same triable issue.<sup>308</sup>

In the present case, the insurer did not contend that the assured had a duty to disclose the opinion of the manager about the market value of the yacht, but only pleaded non-disclosure of the true market value of the yacht. With regard to the actual belief of the manager about the market value of the yacht, the question of “what the insurer would have done if the true belief was told” to the insurer was different from the question of “what the insurer would have done if the wrong belief was not told” to the insurer. In this regard, the learned judge concluded that the mistaken belief of the value of the yacht did not induce the insurer to enter into the insurance contract, and as a result, the insurer was not entitled to avoid the contract on the ground of misrepresentation of the mistaken belief. Conversely, the insurer had the right to avoid the contract on the ground of non-disclosure of the actual market value of the yacht. This approach, as referred to by Mr. Justice Leggatt, suggested that there was at least a difference between the questions of inducement in relation to non-disclosure and misrepresentation. . The *Involnert Management Inc.*<sup>309</sup> case highlighted the new possibility that the questions of inducement of the two duties are distinguishable.

This approach is subject to heavy criticism from the editors of the authoritative textbook “*Arnould: Law of Marine Insurance and Average*” from two perspectives. Firstly, it is suggested that there was no previous case law which supported such a distinction of the questions of inducement.<sup>310</sup> In the *Involnert Management Inc* case,<sup>311</sup> Mr. Justice Leggatt only cited two

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<sup>307</sup> *ibid* [214]

<sup>308</sup> *ibid* [215]

<sup>309</sup> *Involnert Management Inc.* (n296)

<sup>310</sup> Gilman, Templeman, Blanchard, Hopkins and Hart (n38) para 15-34

<sup>311</sup> *Involnert Management Inc.* (n296)

cases to support his judgment, namely *Raiffeisen Zentralbank Österreich AG v Royal Bank of Scotland Plc*<sup>312</sup> and *St Paul Fire & Marine Ins Co (UK) Ltd v McConnell Dowell Constructors Ltd*.<sup>313</sup> While the learned editors of *the Arnould* rightly pointed out that the *Raiffeisen Zentralbank Österreich AG*<sup>314</sup> case was distinguishable as it was not an insurance case,<sup>315</sup> the *St Paul Fire*<sup>316</sup> case did not address the issue about the distinction of inducement tests. Therefore, the judgment of the *Involnert Management Inc.*<sup>317</sup> case, in relation to the distinction of questions of inducement, was unprecedented and unpersuasive.

Secondly, in light of the enactment of the Insurance Act 2015, the fact that the Law Commission did not impose any new clause to distinguish the questions of inducement suggested that the original approach, which was the single inducement test, remained unchanged.<sup>318</sup> Section 3(3)(c) of the IA 2015 provides that:

(3) A fair presentation of the risk is one—

(c) in which every material representation as to a matter of fact is substantially correct, and every material representation as to a matter of expectation or belief is made in good faith.

This section provides a general definition of the duty not to misrepresent under the new duty of fair presentation. While section 7(3) has explicitly unified the materiality tests between the duty of disclosure and the duty not to misrepresent,<sup>319</sup> the inducement test of the duty of fair presentation is set out in section 8(1) of the IA 2015, which states:

(1) The insurer has a remedy against the insured for a breach of the duty of fair presentation only if the insurer shows that, but for the breach, the insurer—

(a) would not have entered into the contract of insurance at all, or  
(b) would have done so only on different terms.

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<sup>312</sup> [2011] 1 Lloyd's Rep. 123

<sup>313</sup> [1995] 2 Lloyd's Rep. 116

<sup>314</sup> *Raiffeisen Zentralbank Österreich AG* [2011] 1 Lloyd's Rep. 123

<sup>315</sup> *ibid* [193]

<sup>316</sup> *St Paul Fire* (n179)

<sup>317</sup> *ibid*

<sup>318</sup> *ibid*

<sup>319</sup> Explanatory Notes to the Insurance Bill (n29) para 75. See also Peter MacDonald Eggers QC, 'The fair presentation of commercial risks under the Insurance Act 2015' in Malcolm Clarke and Baris Soyer (Eds.), *The Insurance Act 2015: A New Regime for Commercial and Marine Insurance Law* (Informa 2016)

Apparently, there is only one inducement test under the new duty of fair presentation. Further evidence can be found in the Law Commission report, which states:

We have brought material representations within the duty of fair presentation alongside disclosure because there is often little practical difference between a non-disclosure and a misrepresentation: breaches often concern the same information, and the same inducement test and remedies for breach apply.<sup>320</sup>

In other words, these new sections have not altered the legal position that non-disclosure shares the same inducement test with misrepresentation. In the absence of evidence to the contrary, it is submitted that the new Act does not support the judgment of *Involnert Management Inc*<sup>321</sup> that there is a distinction between the questions of inducement of non-disclosure and misrepresentation.

To conclude, the *Involnert Management Inc* case<sup>322</sup> has suggested that both the legislation and common law have not accurately defined the nature and operation of the inducement tests. Without an explicit definition of the tests, judges, in England and Wales, and in Hong Kong, may make new interpretations on the questions of inducement, or even the inducement tests, which can be different from the majority of case law. Judges may even make alternative interpretations that are distinct from the *Involnert Management Inc* case.<sup>323</sup> This approach is likely to cause unfair prejudice to the parties to an insurance contract, as the outcome of an utmost good faith case may become unpredictable. Furthermore, without a precise definition of the inducement tests, it is highly unlikely that the reader of the law will be able to understand the operation of the duties correctly, which will no doubt limit the accessibility of the law. It is therefore submitted that the inducement tests should be explicitly stated in the legislation.

### **C. Formulating the written inducement tests as a solution to the current problem**

To formulate the written inducement tests for the law reform in Hong Kong, there are two questions to be answered. Firstly, the question regards whether the inducement tests should be different from each other. Secondly, it regards what the wording of the inducement tests in the

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<sup>320</sup> Law Commission (n4) para 7.47

<sup>321</sup> *Involnert Management Inc* (n296)

<sup>322</sup> *ibid*

<sup>323</sup> *ibid*

legislation should be. To answer these questions, the author has gathered 49 cases<sup>324</sup> with the keywords “inducement” and “utmost good faith” which are reported in the Lloyd’s Insurance and Reinsurance Law Report after the decision of the *Pan Atlantic case*<sup>325</sup> up to the year of 2016. It is suggested that a comprehensive analysis of these 49 cases will lead to answers to the above two questions, which will assist the formulation of the written inducement tests.

**i. Analysis of the inducement tests via case law**

For the first question, the analysis of the 49 cases has pointed to two facts. Firstly, all the 49 cases, except the *Involnert Management Inc*<sup>326</sup> case, have indicated that under the same triable issue, the result of a pleading of non-disclosure would not be different from a pleading of misrepresentation. Secondly, it is also evident that there is not any case, before or after the *Involnert Management Inc*<sup>327</sup> which supports the idea that the inducement tests were different for non-disclosure and misrepresentation. These two facts have suggested that the *Involnert Management Inc*<sup>328</sup> approach is unprecedented. Hence, non-disclosure and misrepresentation should not be distinguished, and they should share the same inducement test.

For the second question about the language of the inducement tests, firstly, among the 49 cases, there are only 12 cases<sup>329</sup> where the judges have fully examined the inducement tests with a written definition for the inducement test of non-disclosure. It is noteworthy that none of the cases has provided a written definition of the inducement test of misrepresentation; it is suggested that this is another piece of evidence to suggest that the inducement test of non-disclosure is the same as misrepresentation.

Further, among these 12 cases, there are two typical types of expression of the inducement test. The first type of expression is in the form of examining the inducement test by the facts of each case. For example, in the case *New Hampshire Insurance Co v Oil Refineries Ltd*,<sup>330</sup> the

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<sup>324</sup> These 49 cases are summarised in the Annex 1 which are appended to this thesis.

<sup>325</sup> *Pan Atlantic Insurance Co* (n46). The reason of analysing cases after, but not before, the *Pan Atlantic* is that the *Pan Atlantic* was the first case that explicitly confirmed the application of the inducement tests in non-disclosure and misrepresentation cases.

<sup>326</sup> *ibid*

<sup>327</sup> *ibid*

<sup>328</sup> *ibid*

<sup>329</sup> The 12 cases are listed in the Annex 1.

<sup>330</sup> *New Hampshire Insurance Co v Oil Refineries Ltd* [2003] Lloyd’s Rep IR 386

judge considered the inducement from the perspective of the actual underwriter, who was Mr Higgins, and held that “I cannot say how much more Mr Higgins would have charged if he had known of the flower growers' claim, but I do know that it would have been more, and that is enough.”<sup>331</sup> In another case, *Wise Ltd v Grupo Nacional Provincial SA*,<sup>332</sup> the inducement test was also put in a specific context: “Mr Bennett had given evidence at trial that had he known that the risk he was being asked to cover included the carriage of watches, he would not have written the risk.”<sup>333</sup> These expressions have clearly indicated the actual operation of the inducement test. Nevertheless, as case facts can be various in different legal disputes, this type of expression may not be useful for the establishment of an objective standard of the inducement test.

The second type of expression is a definition of the inducement test. There are 4 cases<sup>334</sup> using this kind of expression, and they are highly useful for deciding what the wording of the inducement test should be. This type of expression can also be further divided into two forms. The first form could be found in *St Paul F & M Ins v McConnell Dowell*,<sup>335</sup> where the expression of the inducement test was “What the insurer would have done if the true fact (the foundation and ground condition) was told to the insurer.”<sup>336</sup> A similar expression could be found in *Hill v. Citadel Insurance*,<sup>337</sup> which stated that “An underwriter would have been induced if the misrepresentation or non-disclosure materially affected the decision.”<sup>338</sup> The wordings of these two expressions are simple and clear, but they may not be detailed enough to demonstrate the logical linkage of proving causation in utmost good faith cases.

Another form of expression could be found in *Brotherton v Aseguradora Colseguros SA (No 2)*,<sup>339</sup> which claimed that “Whether a material non-disclosure induced the actual underwriter to act to his prejudice depends likewise upon whether the circumstances withheld would, if known, have caused him to act differently, either by not writing the insurance at all or by only writing it

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<sup>331</sup> *ibid* [45]

<sup>332</sup> *Wise Ltd* (n40)

<sup>333</sup> *ibid* [97]

<sup>334</sup> The 4 cases are listed in the Annex 1.

<sup>335</sup> *St Paul Fire* (n179)

<sup>336</sup> *ibid* 301

<sup>337</sup> [1995] LRLR 218

<sup>338</sup> *ibid* 233

<sup>339</sup> [2003] Lloyd's Rep IR 746



on different terms.”<sup>340</sup> A similar definition could also be found in *Assicurazioni Generali SpA v ARIG*,<sup>341</sup> which maintained that the insurer “must therefore show at least that, but for the relevant non-disclosure or misrepresentation, he would not have entered into the contract on those terms.”<sup>342</sup> This kind of expression is generally referred as the “but for” test in law, and it is widely used in subject matters for both civil and criminal law. In comparison with other kinds of expression, these kinds of expression have highlighted all the significant factors for proving inducement, and therefore it should be taken as a model of formulating the written inducement test for the law reform in Hong Kong.

## ii. The solution

The findings of the above sub-section have suggested that, firstly, non-disclosure and misrepresentation are not distinguishable and secondly, there is no evidence to suggest that there is a difference between the inducement tests of non-disclosure and misrepresentation. Based on these findings, it is suggested that the reform solution, which is a written inducement test in the legislation, should be subject to two principles. Firstly, the written inducement should be one single test which applies to both non-disclosure and misrepresentation. Secondly, the effect of applying the inducement test, in the case of both non-disclosure and misrepresentation, should not lead to different outcomes on the same triable issue.

Further, based on the case analysis of the previous sub-section, the exact wordings of the written inducement test should include three elements. Firstly, the subject of the test should be referred to as the “insurer/underwriter”. Secondly, as the inducement test is applied to a hypothetical situation, the verb phrase of the test should be “would have been induced” or “would have done”. Thirdly, the logical linkage of proving causation is based on the “but for” test, and therefore the test should be formulated as “if Event A had happened, then it would have led to Event B.” In the context of utmost good faith, Event A is either the absence of “non-disclosure” or “misrepresentation”, and Event B is “would not have entered into the insurance contract” or “would have entered into the insurance contract under different terms”.

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<sup>340</sup> *ibid* [18]

<sup>341</sup> *Assicurazioni Generali SpA* (n242)

<sup>342</sup> *ibid* [62]

Based on the above two principles and three elements, it is submitted that the reform solution can be in the form of adding sub-sections in both section 18 and 20 of the Marine Insurance Ordinance in Hong Kong. In section 18, in addition to the existing 5 sub-sections, section 18(6) could be added and state:

For a claim of non-disclosure, the insurer/underwriter needs to prove that had the material circumstance been disclosed, the insurer/underwriter would not have entered into the insurance contract, or would have entered into the insurance contract in different terms.

In section 20, section 20(8) could be added and state:

For a claim of misrepresentation, the insurer/underwriter needs to prove that should the material misrepresentation not have been made, the insurer/underwriter would not have entered into the insurance contract, or would have entered into the insurance contract under different terms.

The wordings of the two additional sub-sections suggest that these tests are identical to each other and therefore, there should not be any difference in the operation of the inducement tests, and the outcomes between non-disclosure and misrepresentation should not be different for the same issue in utmost good faith cases. It is noteworthy that since these two additional sub-sections have similar wordings to section 8(1) of the IA 2015, it is suggested that the IA 2015 may also be another suitable model for reforming the inducement tests in Hong Kong.

One could argue that since the doctrine of misrepresentation in general contract law does not have a written inducement test in the relevant legislation, it suggests that it is unnecessary to have a written inducement test for the legislation in relation to utmost good faith. Nevertheless, it is submitted that a comparison between misrepresentation in general contract law and utmost good faith cases should always be conducted with caution. These two types of misrepresentation, despite sharing some common features, are fundamentally different to each other, and the fact that there is not a written inducement test for the legislation of misrepresentation in general contract law does not mean that the same approach is correct in the context of utmost good faith. The coming section will examine how these two types of

misrepresentation are different, and explain the reasons why the application of these two types of misrepresentation should be separated.

## **II. The second problem of the law of misrepresentation – the vague boundary between utmost good faith and the Misrepresentation Ordinance**

The second problem is about whether the Misrepresentation Ordinance is applicable to utmost good faith cases. As discussed in the previous chapters, the current duty of utmost good faith has already provided an overwhelmingly strong protection to the insurer due to the problem of information asymmetry at the underwriting stage. Nevertheless, it is evident from the case law that the insurers in England and Wales have tried to make use of the Misrepresentation Act 1967, which is identical to the Misrepresentation Ordinance in Hong Kong, to bring an alternative allegation of breaching the duty of utmost good faith. For instance, in *HIH Casualty v Chase Manhattan Bank*,<sup>343</sup> the insurer sought to avoid a time variable contingency risk policy over five movies based on several non-disclosure and misrepresentation allegations under the duty of utmost good faith. Alternatively, the insurer also sought damages based on section 2(1) of the Misrepresentation Act 1967. The House of Lords held that the insurer might have been entitled to seek damages under section 2(1) of the Misrepresentation Act 1967.<sup>344</sup> Nevertheless, since the remedy of avoidance was granted to the insurer, the damages were not awarded.

This proposition is confirmed by the case authority *Argo Systems v Liberty Insurance*.<sup>345</sup> The insurer contended that the assured was in breach of a warranty and the duty of utmost good faith of the insurance contract, which concerned a hull insurance of a floating casino. One of the issues in this case was whether the insurer had affirmed the insurance contract and whether the insurer could still claim damages under section 2(1) of the Misrepresentation Act 1967 as an alternative remedy of avoidance. HHJ Mackie QC held that, firstly, in general, the insurer was entitled to claim damages under section 2(1) of the Misrepresentation Act 1967, which had been confirmed in the judgment of the *HIH Casualty* case.<sup>346</sup> Secondly, the learned judge also held that under section 2(1), the remedy of damages might not have been opened to the insurer in

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<sup>343</sup> [2003] Lloyd's Rep IR 230

<sup>344</sup> *ibid* [5]

<sup>345</sup> [2011] 2 Lloyd's Rep. 61

<sup>346</sup> *HIH Casualty* (n346) [45]

the case where the remedy of avoidance was lost under section 20 of the MIA 1906.<sup>347</sup> The logic behind this judgment, as mentioned by the learned judge, was that if such an alternative remedy was available to the insurer, it would be surprising to see that there was no such record of granting such a remedy in the past case authorities. It is noteworthy that the learned judge had expressed his view that the Court of Appeal should have conducted the full debate of this issue, but the attempt was in vain as the Court of Appeal did not address this issue.

In general, due to the powerful single remedy approach of the duty of utmost good faith, it is highly unlikely that the insurer will sue the assured for damages under the Misrepresentation Act 1967. Nevertheless, the above two cases have suggested that theoretically, the Misrepresentation Act 1967 is applicable to insurance contracts as an alternative remedy for breaching the duty of utmost good faith. This approach, if allowed, will no doubt worsen the current unfair situation of the assured in relation to the duty of utmost good faith.

In the following, the problem of the applicability of the Misrepresentation Act 1967 to utmost good faith cases will be analysed from two perspectives. Firstly, judging from the outset and the contents of the Misrepresentation Act 1967, it is submitted that the said Act was not designed to be applicable to cases in relation to utmost good faith. Secondly, the recent case law also suggests that the application of the Misrepresentation Act 1967 may undermine the rationale for the duty of utmost good faith.

At the end of this section, a reform solution for this problem will be proposed. Although this problem cannot be observed from Hong Kong case law, it is still likely to occur in Hong Kong as the MIO and the Misrepresentation Ordinance are both identical to the legislations in England and Wales. Therefore, as a reform solution, it is suggested that section 17 of the MIO should include an additional statement that the Misrepresentation Ordinance in Hong Kong is not applicable to utmost good faith cases.

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<sup>347</sup> *ibid*

**A. The Misrepresentation Act 1967 was not designed to be applicable to utmost good faith cases**

This section will analyse the applicability of the Misrepresentation Act 1967 to utmost good faith cases from two perspectives. Firstly, the rationale for the enactment of the Misrepresentation Act 1967 will be examined. Secondly, the contents of the Misrepresentation Act 1967 will be analysed. The purpose of these analyses is to demonstrate that the Misrepresentation Act 1967 was not designed to embrace utmost good faith cases, and therefore the Misrepresentation Ordinance in Hong Kong also should also not be applicable to utmost good faith cases.

**i. The rationale for the enactment of the Misrepresentation Act 1967**

As discussed, it is submitted that there is no definite answer to whether the Misrepresentation Act 1967 is applicable to utmost good faith cases. Nevertheless, the Tenth Report (Innocent Misrepresentation) of the Law Reform Committee may indicate the rationale for the enactment of the Misrepresentation Act 1967, and it may shed some light on the question of whether the said Act should be applicable to utmost good faith cases.

Before the enactment of the Misrepresentation Act 1967, there were three problems with the law of misrepresentation which were identified by the Law Reform Committee in the Tenth Report:

First, in the majority of the memoranda we have received the restrictions on the right to rescind a contract on account of misrepresentation are attacked as being too stringent, although opinions differ as to the extent to which rescission should be made easier; secondly, there is an almost unanimous demand for a remedy in damages, either in addition to, or in lieu of, rescission, thirdly, it is said by those speaking from practical experience of sales and other commercial transactions that there ought to be some curtailment of the freedom to exclude liability for misrepresentation by a provision in the contract in cases where the parties are not bargaining as equals.<sup>348</sup>

The first problem, as identified by the Law Reform Committee, was resolved by the enactment of section 1 of the Misrepresentation Act 1967. Similarly, the third problem was resolved by the

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<sup>348</sup> Law Reform Committee, Tenth Report (Innocent Representation), 1962, cmnd 1782, para 2

enactment of section 3 of the Misrepresentation Act 1967, which was subsequently amended by the Unfair Contract Terms Act 1977 and the Consumer Rights Act 2015 (c. 15). The fact that section 1 and 3 of the Misrepresentation Act 1967 were not directly relevant to insurance contract cases may be an indication that the said Act was not designed to be applicable to utmost good faith cases. In any event, the second problem, as identified by the Law Reform Committee in relation to the remedy of damages, appeared to be relevant to utmost good faith cases, and this problem was resolved by the enactment of section 2 of the Misrepresentation Act 1967.

The key question, therefore, is whether section 2 was designed to be applicable to utmost good faith cases. Judging from the contents of the Tenth Report, it is submitted that the said section 2 was not designed to be applicable to utmost good faith cases. There are two pieces of evidence to support this observation. Firstly, in the said report, the Committee members identified the unique features and the problems of a wide range of contracts regarding the law of misrepresentation. These contracts included contract of sale of land,<sup>349</sup> sale of shares,<sup>350</sup> partnership, agency and service agreement,<sup>351</sup> sale of car<sup>352</sup> and hire-purchase agreement.<sup>353</sup> The term "insurance contract", as a special type of contract which is highly relevant to the doctrine of misrepresentation, was not mentioned in the report. Secondly, the Committee members also considered the effect of the enactment of the Misrepresentation Act 1967 with reference to other legislation, namely, the Sale of Goods Act 1893 and<sup>354</sup> the Companies Act 1948.<sup>355</sup> Again, the MIA 1906 was not mentioned in the report. These observations appeared to indicate that insurance contracts were not under the consideration of the committee members. In the absence of evidence to the contrary, it is suggested that the enactment of the Misrepresentation Act 1967 does not embrace contract of insurance, which also means that the Misrepresentation Ordinance is unlikely to be applicable to utmost good faith cases.

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<sup>349</sup> *ibid* para 6-7

<sup>350</sup> *ibid* para 8

<sup>351</sup> *ibid* para 10

<sup>352</sup> *ibid* para 11

<sup>353</sup> *ibid* para 19-20

<sup>354</sup> *ibid* para 14-16

<sup>355</sup> *ibid* para 18

## ii. The contents of the Misrepresentation Act 1967

The second reason why the Misrepresentation Act 1967 should not be applicable to utmost good faith cases is that functionally speaking, the said Act does not have any effect on utmost good faith cases. Section 2(1) of the Misrepresentation Act 1967 provides that:

Where a person has entered into a contract after a misrepresentation has been made to him by another party thereto and as a result thereof he has suffered loss, then, if the person making the misrepresentation would be liable to damages in respect thereof had the misrepresentation been made fraudulently, that person shall be so liable notwithstanding that the misrepresentation was not made fraudulently, unless he proves that he had reasonable ground to believe and did believe up to the time the contract was made the facts represented were true.

In short, section 2(1) provides that a party, who suffers from a negligent misrepresentation, is entitled to seek damages. However, the effect of the said section should be read together with section 2(2) of the Misrepresentation Act 1967, which provides that:

Where a person has entered into a contract after a misrepresentation has been made to him otherwise than fraudulently, and he would be entitled, by reason of the misrepresentation, to rescind the contract, then, if it is claimed, in any proceedings arising out of the contract, that the contract ought to be or has been rescinded, the court or arbitrator may declare the contract subsisting and award damages in lieu of rescission, if of opinion that it would be equitable to do so, having regard to the nature of the misrepresentation and the loss that would be caused by it if the contract were upheld, as well as to the loss that rescission would cause to the other party.

The effect of section 2(2) is illustrated in the case *UCB Corporate Services Ltd v Kenneth Roy Thomason, Christian Ann Thomason*.<sup>356</sup> The appellant contended that the respondent misrepresented their financial status and hence, the waiver agreement was rescinded on the ground of misrepresentation. The respondent argued that according to section 2(2) of the Misrepresentation Act 1967, the appellant was not entitled to rescind the contract. The appellant, as the respondent contended, was only entitled to recover the additional sum of money that the respondent would have paid to secure the waiver agreement.

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<sup>356</sup> *UCB Corporate Services Ltd v Kenneth Roy Thomason, Christian Ann Thomason* [2005] EWCA Civ 225, 2005 WL 460737

In the Court of Appeal, Lord Justice Latham held that the appellant was not entitled to rescind the waiver agreement.<sup>357</sup> Hence, the appellant had no right to seek damages under section 2(2) of the Misrepresentation Act 1967.<sup>358</sup> In his judgment, Lord Justice Latham considered the effect of section 2(2) as follows:

The Committee was concerned that if rescission was permitted after a contract had been performed, that might result in injustice if rescission would cause hardship which was out of proportion to the loss occasioned by the misrepresentation. The question is therefore whether the judge was correct in coming to the conclusion that he did on the facts in relation to loss and then equating, as he clearly did, damages to the loss he had so identified.<sup>359</sup>

Lord Justice Latham further held that section 2(2) aimed to strike a balance between the consequence of rescinding the contract and the loss that was caused by the misrepresentation.<sup>360</sup> Therefore, it is submitted that the effect of section 2(2) is to prevent any potential detriment that the representor would suffer from the rescission of the contract. In this regard, the relevant question, about the applicability of the Misrepresentation Act 1967 to utmost good faith cases, is whether the said section 2 can achieve the purpose of preventing potential detriment in the context of utmost good faith cases.

It is submitted the answer of this question can be found in the insurance case authority *Highlands Insurance Co. v. Continental Insurance Co.*<sup>361</sup> In this case, the policy concerned a reinsurance contract of property risks. In the insurance slip, it was stated that the insured properties had installed the sprinkler system. Later, a fire accident happened in one of the insured properties and the reassured claimed against the reinsurer. Upon investigation, the reinsurer discovered that the property had not installed the sprinkler system, and as a result, the insurer avoided the contract on the ground of misrepresentation.

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<sup>357</sup> *ibid* [37]

<sup>358</sup> *ibid* [37]

<sup>359</sup> *ibid* [36]

<sup>360</sup> *ibid* [37]

<sup>361</sup> *Highlands Insurance* (n287)



Mr. Justice Steyn held that the reinsurer was entitled to avoid the contract. The reassured argued that Mr. Justice Steyn should have considered the effect of section 2(2) of the Misrepresentation Act 1967, which required the court to determine whether damages should be granted in lieu of rescission in the case of innocent misrepresentation. Mr. Justice Steyn rejected this contention and held that there was no equitable situation to consider the effect of section 2(2) where an insurance contract was avoided on the ground of breaching the duty of utmost good faith.<sup>362</sup> The learned judge expressed his view as follows:

The rules governing material misrepresentation fulfil an important 'policing' function in ensuring that the brokers make a fair representation to underwriters. If s. 2(2) were to be regarded as conferring a discretion to grant relief from avoidance on the grounds of material misrepresentation the efficacy of those rules will be eroded.<sup>363</sup>

In other words, section 2(2) is not meant to be applicable to utmost good faith cases. The reasons for this is that , firstly, the juristic basis of the remedy of rescission, under the Misrepresentation Act 1967, is apparently different from the remedy of avoidance under the MIA 1906. Secondly, as the remedy of damages is not available to the insurer under section 20 of the MIA 1906, there is no reason to support that section 2(2) can be applicable to utmost good faith cases. By this logic, one can easily reach the conclusion that the Misrepresentation Act 1967, as a whole, was not designed to be applicable to utmost good faith cases, and therefore, it cannot be treated as an alternative allegation by the insurer in the case of breaching the duty of utmost good faith.

**B. The trend of case law suggests that the Misrepresentation Act 1967 is not applicable to utmost good faith cases**

After considering the effect and rationale for the Misrepresentation Act 1967, this section will provide a thorough analysis of the recent trend in insurance cases which has involved the pleadings in relation to the Misrepresentation Act 1967, the purpose of which is to demonstrate that the application of the Misrepresentation Ordinance in utmost good faith cases is undesirable. These cases are all reported cases in Lloyd's Insurance and Reinsurance Law

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<sup>362</sup> *ibid* 118

<sup>363</sup> *ibid*

Reports between the years of 1995 and 2016. In these 21 years, there are 14 cases<sup>364</sup> in which the term “Misrepresentation Act 1967” can be found in the Lloyd’s Insurance and Reinsurance Law Reports. Among these 14 cases, there are 10 cases, namely, *Agnew v Länsförsäkringsbolagens AB*,<sup>365</sup> *Arts & Antiques Ltd v Richards*,<sup>366</sup> *Avon Insurance Plc and Ors v Swire Fraser Ltd and Anor*,<sup>367</sup> *Barings Plc v Coopers & Lybrand*,<sup>368</sup> *Dornoch Ltd v Mauritius Union Assurance Co Ltd*,<sup>369</sup> *HIH v New Hampshire*,<sup>370</sup> *Kingscroft & Ors v Nissan Fire & Marine (No 2)*<sup>371</sup>, *Kyle Bay Ltd v Underwriters to Policy 0190570801*,<sup>372</sup> *Lloyd's v Leighs*,<sup>373</sup> *Pa (gi) Ltd v Gicl 2013 Ltd and Another*,<sup>374</sup> which are irrelevant to the application of the Misrepresentation Act 1967 to utmost good faith cases.

In the remaining four cases, none of them was successful in claiming damages under section 2 of the Misrepresentation Act 1967. In *Argo Systems v Liberty Insurance*<sup>375</sup>, the damages were not granted because there was a breach of warranty, and the insurer was discharged from the liability from the date of the breach. Avoidance could not be granted under the MIA 1906 because the insurer affirmed the contract. Similarly, in *HIH Casualty v Chase Manhattan Bank*<sup>376</sup>, since the remedy of avoidance was granted to the insurer, the remedy of damages was not awarded.

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<sup>364</sup> To be precise, there are 14 cases which are reported in 19 different case reports.

<sup>365</sup> [1997] 6 Lloyd's Rep IR 33. The Swedish Defendant's case of setting aside the allegation of misrepresentation based on Lugano Convention article 5(1) was dismissed.

<sup>366</sup> [2014] 1 Lloyd's Rep IR 219. This case concerned an issue estoppel and abuse of process, a claim of misrepresentation appeared in the statement of claim, but it was not addressed by the Court.

<sup>367</sup> *Avon Insurance Plc and Ors* (n300). The insurer claimed against the broker under section 2(1) of the Misrepresentation Act 1967, and utmost good faith was only mentioned as a reference of explaining the test of inducement. This case was dismissed as the insurer could not prove misrepresentation.

<sup>368</sup> [2003] 1 Lloyd's Rep IR 566. This was a case between the banks and auditors, and utmost good faith in the context of insurance law was not examined.

<sup>369</sup> [2006] 1 Lloyd's Rep IR 127. This was a case about a misrepresentation occurred in Mauritius, and the main issue was about conflict of laws but not utmost good faith.

<sup>370</sup> [2001] 1 Lloyd's Rep IR 596. The main issue of this case was about the effect of the waiver of right clause in the insurance policies.

<sup>371</sup> [1999] 1 Lloyd's Rep IR 603. This case concerned breaching the duty of utmost good faith in reinsurance contract and section 1(1) of the Misrepresentation Act 1967 was cited to explain the general principle of misrepresentation that rescission can be granted when the misrepresentation is incorporated into the contract.

<sup>372</sup> [2006] 1 Lloyd's Rep IR 718. The assured sought to avoid the settlement contract by pleading misrepresentation, it was irrelevant to the duty of utmost good faith, and the case was dismissed.

<sup>373</sup> [1997] 6 Lloyd's Rep IR 289. The assureds sought to rescind the insurance membership contract due to fraudulent misrepresentation, which was irrelevant to the duty of utmost good faith.

<sup>374</sup> [2016] Lloyd's Rep IR 125. This case concerned an agreement of business transfer of a protection payment insurance.

<sup>375</sup> *Argo Systems* (n348)

<sup>376</sup> *HIH Casualty* (n346)

The other two cases were of similar nature. In *Kumar v AGF Insurance Ltd and Others*,<sup>377</sup> this case concerned a professional indemnity insurance in relation to a law firm. Avoidance and damages were not granted because the remedies were excluded by the non-avoidance clause in the contract. In *Toomey v Eagle Star Insurance Co (No 2)*,<sup>378</sup> this case concerned an application for a summary judgment which was made by the assured about a claim of indemnity. The insurer raised defences on the grounds of non-disclosure and misrepresentation. The assured pleaded that the contract could not be avoided, and damages could not be recovered because of an exclusion clause in the contract. The court held that there was a triable case as the exclusion clause only excluded innocent but not negligent non-disclosure and misrepresentation.

To sum up, over the past two decades, there were only four cases which were relevant to the application of the Misrepresentation Act 1967 in utmost good faith cases, and none of them was successful in claiming damages under the Misrepresentation Act 1967. Among these four cases, two of them were unsuccessful because there were alternative remedies available to the insurer, and the other two were unsuccessful because of the effect of exclusion clauses in the insurance contracts. The reasons behind this phenomenon are that, firstly, under insurance contract law, there is already a wide range of remedies, which are available for the parties to an insurance contract. For instance, the remedy of avoidance which was granted in the *HIH Casualty*<sup>379</sup> case, or another remedy in relation to the breach of warranty which was granted in *THE "COPA CASINO"*<sup>380</sup> case. Secondly, it is suggested that the parties to an insurance contract may have developed their own market practice to protect themselves from the loss of misrepresentation. One of the examples, as demonstrated in the *Kumar*<sup>381</sup> case and the *Toomey*<sup>382</sup> case, is that the exclusion clauses in relation to rescission or avoidance were added in the insurance contracts. Therefore, the parties to an insurance contract do not need to seek the alternative remedy under the Misrepresentation Act 1967. The recent case trend of insurance law, as mentioned above, simply suggests that the application of the Misrepresentation Act 1967 is undesirable in the context of utmost good faith, and hence for the

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<sup>377</sup> [1999] 1 Lloyd's Rep IR 147

<sup>378</sup> [1995] 4 Lloyd's Rep IR 314

<sup>379</sup> *HIH Casualty* (n346)

<sup>380</sup> *Argo Systems* (n348)

<sup>381</sup> *Kumar* (n382)

<sup>382</sup> *Toomey* (n383)

reform of law in Hong Kong, the Misrepresentation Ordinance should also not be applicable to utmost good faith cases.

### **C. Reform suggestion for the applicability of the Misrepresentation Ordinance to utmost good faith cases**

The current legislation in Hong Kong has not addressed the issue of whether the Misrepresentation Ordinance is applicable to utmost good faith cases. Based on the above analysis, it is submitted that the Misrepresentation Ordinance should not be applicable to utmost good faith cases, and this approach should be clearly stated in the relevant legislation. The simplest way to solve this problem is by adding a statement in section 17 of the Marine Insurance Ordinance, which provides that 'The Misrepresentation Ordinance is not applicable to the cases which involved the disputes of utmost good faith.' By imposing this additional wording, it is clear to the reader of the law that the Misrepresentation Ordinance cannot act as an alternative pleading for breaching the duty of utmost good faith.

### **III. Conclusion**

The doctrine of misrepresentation in relation to the duty of utmost good faith still has much to be desired. On the one hand, it is not clear as to how non-disclosure is distinguishable from misrepresentation in relation to the operation and outcome of the law. On the other hand, the potential applicability of the Misrepresentation Act 1967 in utmost good faith cases has also confused the situation.

The IA 2015 has combined non-disclosure and misrepresentation into the new duty of fair presentation, which can be taken as a good direction to resolve the problem of the distinction between non-disclosure and misrepresentation. In any case, it is submitted that a clearer guidance on the difference between the inducement tests regarding non-disclosure and misrepresentation is much desired.

Further, in this chapter, the author seeks to clarify the position of the Misrepresentation Ordinance in utmost good faith cases. The purpose of the clarification is to eliminate the uncertainties and to ensure that the duty not to misrepresent in insurance contract cases can be operated equitably and independently. Based on the rationale behind the enactment of the

Misrepresentation Act 1967 and also the recent trend of insurance cases which involved the the application of the Misrepresentation Act 1967, it is suggested that the most suitable solution for this problem is to separate the jurisdictions between the Misrepresentation Ordinance and the duty of utmost good faith in insurance contract law. In any event, it is submitted that the duty not to misrepresent in insurance contract law is in need of reform, and the detailed reform proposal will be provided in chapter 6 of this thesis.

## Chapter 4 The Remedies For The Breach Of The Duty Of Utmost Good Faith/Fair Presentation

This chapter will focus on the remedies for the breach of the duty of utmost good faith/fair presentation in the context of insurance law. There are two major problems in this area of law. The first problem regards the insurer's duty of utmost good faith. The second problem regards the issue of disproportionality under the MIO and IA 2015 in relation to the remedies with respect to the breach of the duty of utmost good faith/fair presentation.

For the first problem, it is submitted that the scope of the insurer's duty is poorly defined. While reasonable inference can still be drawn from the *Banque Keyser v. Skandia*<sup>383</sup> case for the pre-contractual duty of the insurer, there is no scope for the insurer's duty of utmost good faith at the post-contractual stage. The result of which is that the breach of duty can only be examined by the court on a case-by-case basis, since there is no legislation that expressly addresses this area of law, therefore the existence of this area of law can hardly be observed. The result of claiming under this area of law is also rarely predictable, as there is no clear guidance of law to follow.

The problem of the insurer's duty of utmost good faith can be further complicated by the single remedy of avoidance under the MIO. When there is a breach of duty by the insurer, the assured will prefer a monetary award to compensate for the loss that the assured has suffered. Nevertheless, the single remedy approach under the MIO only allows the party that has suffered a breach to seek the remedy of avoidance. The only consequence of this remedy is that the insurance contract will be treated as if it had never existed, and as a result, the assured will not be able to claim indemnity under an avoided insurance contract. This may be a favourable remedy for the assured before the loss has materialised, but it is certainly not an adequate measure for the assured after the loss has materialised and a claim has proceeded, as the avoidance of contract will allow the insurer to escape from the liability to pay indemnity under the insurance policy. Since there is no adequate remedy for the assured to claim against the insurer under the duty, it is therefore suggested that under the MIO, it serves no purpose for the

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<sup>383</sup> *La Banque* (n21)

insurer to comply with the duty, as there is no consequence for the insurer to breach the duty of utmost good faith. This approach is no doubt oppressive and unfair to the assured.

It is submitted that the IA 2015 has also not solved the aforementioned problem, as although the IA 2015 has imposed a new duty of fair presentation, this is only followed by the assured and not the insurer. The IA 2015 has also abolished the remedy of utmost good faith under the MIA 1906, but the nature of the insurance contract, as a contract of utmost good faith, has remained unchanged. Academics suggest that this approach may allow the judges to revisit the insurer's duty of utmost good faith,<sup>384</sup> but the current situation is that the IA 2015 has not solved the problems regarding the insurer's duty. Therefore, to reform this area of law in Hong Kong, the author suggests that section 17 of the MIO should be amended to ensure that the insurer also owes an operable duty of utmost good faith. The author also suggests that the reform of law should ensure that there is an adequate remedy for the assured to claim against the insurer under the said duty.

The second problem of the remedies for the breach of utmost good faith/fair presentation is that there is a problem of disproportionality of the remedies. Under the MIO, the remedy of avoidance applies to all wrongdoers, regardless of the seriousness of the breach. In most cases, the effect of the breach can be minor and not involve any fraudulent behaviour, but the single remedy approach suggests that the innocent wrongdoers, who commit minor mistakes, and the fraudulent wrongdoers, who commit major mistakes, will be treated the same under the law. This approach is no doubt unfair to the innocent assureds who only commit minor mistakes.

In addition, it is arguable that the harshness of the remedy of avoidance is disproportionate to the consequence of breaching the duty of utmost good faith. The reason is that once the insurance contract is avoided, the assured is no longer under the protection of any insurance cover. The assured must bear the whole loss amount, which is supposed to have been covered by an insurance contract. If the risk had been fairly presented, one of the likely consequences is

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<sup>384</sup> See, for example, Baris Soyer, "The insurer's duty of utmost good faith: is the path now clear for the introduction of new remedies" in Malcolm Clarke and Baris Soyer (Eds.), *The Insurance Act 2015: A New Regime for Commercial and Marine Insurance Law* (Informa 2016)

that the insurer would have charged a higher premium for the risk. Nevertheless, instead of compensating the insurer for the additional premium, the remedy of avoidance provides a good excuse for the insurer to avoid the liability of indemnifying the assured. It is therefore submitted that the remedy is disproportionate and unfair to the assured.

The IA 2015 has introduced a new set of remedies to rectify the problem of disproportionality. The remedy of avoidance was removed from the MIA 1906, and the IA 2015 has imposed various new remedies to address different levels of a breach of the new duty of fair presentation. Nevertheless, judging from the details of the IA 2015, it is submitted that the new remedies may not be as proportionate as they appear. Therefore, the author suggests that Hong Kong should not strictly follow the English law approach when reforming the remedies of utmost good faith/fair presentation.

To examine the above-mentioned problems and to formulate reform suggestions for the problems, this chapter will be divided into two sections. In the first section, the problem of the insurer's duty will be examined in relation to the scope and the remedy of the duty. A reform solution for the insurer's duty of utmost good faith will be provided at the end of the section. In the second section, the problem of disproportionality will be examined in the context of the MIO, MIA 1906 and the IA 2015. At the end of the second section, a reform solution will be provided for Hong Kong legislation, the proposal of which should be more proportionate than the current law under the MIO of Hong Kong, as well as the IA 2015 of England and Wales.

#### **I. The first problem of the remedies – an inoperable insurer's duty of utmost good faith**

It is submitted that the current state of the insurer's duty of utmost good faith is unsatisfactory for two reasons. Firstly, the scope of the insurer's duty is not clearly defined. Secondly, even if the scope is clearly defined for the insurer's duty, there is no adequate remedy for the assured to claim against the insurer. It is submitted that the two problems point to the same fact that the insurer's duty is inoperable under English law, and therefore this area of law is in need of reform. In the following sub-sections, the problems of the scope and the remedy will be examined. In the final sub-section, it is submitted that section 17 of the MIO should be amended to reform the insurer's duty of utmost good faith.



### A. The unclear scope of the insurer's duty of utmost good faith

It is submitted that the source of the insurer's duty can be traced back to the classic case authority *Carter v Boehm*,<sup>385</sup> where Lord Mansfield held that:

Good faith forbids either party by concealing what he privately knows, to draw the other into a bargain, from his ignorance of that fact, and his believing the contrary. But either party may be innocently silent, as to grounds open to both, to exercise their judgment upon.<sup>386</sup>

The judgment clearly suggested that the duty of utmost good faith was intended to be applicable to both parties, and the insurer was also forbidden to conceal any information that was material to the risk.<sup>387</sup> Sir Mackenzie D Chalmers, who was the draftsman of the MIA 1906, observed this nature of the duty and stated in his book, *Chalmers' Marine Insurance Act 1906*, that the duty of utmost good faith was intended to be applicable to both parties to an insurance contract, although the conduct of the assured was more often to be questioned.<sup>388</sup>

The problem is that none of the above authority has expressly defined the scope of the insurer's duty of utmost good faith. One can only draw reasonable inference from the existing authorities to determine the scope of the duty. In general, the insurer's duty can also be divided into the pre-contractual and post-contractual duties. For the pre-contractual duty, the mainstream view is that the insurer's duty should be identical to the assured's duty of utmost good faith. This school of thought, which originated from the case *Carter v Boehm*,<sup>389</sup> is explained by Professor Merkin as follows:

Clearly, the arrival of a ship, given as an example of what an insurer has to disclose, is something that decreases rather than increases the risk and would justify the avoidance of the policy by the assured. It does not follow from this that merely because an insurer has to disclose circumstances which reduce the risk under the policy there are no other

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<sup>385</sup> *Carter* (n1)

<sup>386</sup> *ibid.* page 1910

<sup>387</sup> This proposition is also supported by modern case law such as *C.T.I. v. Oceanus* [1984] 1 Lloyds Law Rep 477. See page 525, where Stephenson, L.J. agreed that the duty of utmost good faith is a mutual duty.

<sup>388</sup> Sir Mackenzie D Chalmers and E R Hardy Ivamy, *Chalmers' Marine Insurance Act 1906* (Tenth Edition, Tottel Publishing 1993), p.24

<sup>389</sup> *Carter* (n1)

classes of fact which may be regarded as material for the purposes of the insurer's duty, although it is logical to suggest that Lord Mansfield's illustration demonstrates the extent of the insurer's duty contemplated at the time.<sup>390</sup>

As further elaboration of the judgment of Lord Mansfield, Professor Merkin concludes that as far as the insurer's duty is concerned, the materiality requirement of the insurer's duty is applicable to information which will decrease the insured risk.<sup>391</sup> The scope of the duty is further examined in *Banque Keyser v Skandia*.<sup>392</sup> This case concerned several credit insurance policies between the insurer and the assureds. The assureds failed to repay the loans that were borrowed from the banks, and as a result the banks claimed against the insurers under the policies. However, the insurers denied the liabilities, because the assureds had fraudulently misrepresented the value of the gemstones, which were held as security against the loans. The banks contended that the insurer had failed to disclose the broker's fraud, namely the presentation of false cover notes, and the banks were entitled to recover the payments from the insurer on the ground of utmost good faith. In the first instance court, Steyn J held that the banks were entitled to recover the loans from the insurers on the grounds of utmost good faith. Nevertheless, Steyn J did not follow the mainstream thought that the insurer's duty was identical to the assured's duty, but rather invented a new approach to addressing the scope of the duty. Surprisingly, Steyn J's starting point for the judgment was also *Carter v Boehm*,<sup>393</sup> but he reached the conclusion that the scope of duty of the insurer was undefined under English law.<sup>394</sup> Steyn J suggested that, in relation to the duty of the insurer, the only requirement would be that the insurers present the risk fairly, because in the case that they did not, they would have breached the duty of utmost good faith. In addition, this would have influenced the judgment of the assured to enter into the contract.<sup>395</sup> Since the degree of influence was not identified by Steyn J, the scope proposed by him was simply about whether the insurer had presented the risk in good faith as a general principle, and not about a set of precise conditions that were stipulated in section 18, 19 and 20 of the MIA 1906. This general good faith approach led Steyn J to conclude that the insurer was in breach of the duty of utmost good faith by failing to disclose the fraud of its agent.

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<sup>390</sup> Merkin(n42) Para A-0676

<sup>391</sup> *ibid*

<sup>392</sup> [1987] 1 Lloyd's Rep 69

<sup>393</sup> *Carter* (n1)

<sup>394</sup> *Banque Keyser* (n397) 94

<sup>395</sup> *ibid*

Steyn J's proposition was rejected by Slade LJ in the Court of Appeal.<sup>396</sup> Slade LJ was of the opinion that the scope that was identified by Steyn J was too broad and did not reflect the requirement of section 18 of the MIA 1906.<sup>397</sup> The learned judge held that:

In adapting the well-established principles relating to the duty of disclosure falling upon the insured to the obverse case of the insurer himself, due account must be taken of the rather different reasons for which the insured and the insurer require the protection of full disclosure. In our judgment, 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.<sup>398</sup>

Contrary to the general good faith approach, Slade LJ's approach narrowed down the scope of the duty to the non-disclosure of material facts that were either in relation to the risk or the claim. While the former approach was in line with Professor Merkin's observation of the spirit of *Carter v Boehm*,<sup>399</sup> the latter approach was not supported by the highest authority. In the House of Lords,<sup>400</sup> Lord Jauncey suggested that the scope of the duty should have been narrowed to the situation that the non-disclosed information would influence the risk. For example, an insurer would breach the duty of utmost good faith if he did not disclose the fact that an insured ship had already completed the voyage prior to the conclusion of the marine insurance contract.<sup>401</sup>

Although the House of Lords judgment is legally correct and matches with the spirit that originates from *Carter v Boehm*,<sup>402</sup> it is submitted that this approach suffers from a lack of practicability. Firstly, the House of Lords judgment suggested that the pre-contractual duty of the insurer was a reflection of the assured's duty. However, there are some areas in which the insurer's duty cannot be accurately reflected by the assured's duty. For example, the prudent

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<sup>396</sup> *La Banque Financière v. Westgate* [1988] 2 Lloyd's Law Rep 513

<sup>397</sup> *ibid* 544 - 545

<sup>398</sup> *ibid* 545

<sup>399</sup> *Carter* (n1)

<sup>400</sup> *Banque Keyser* (n21)

<sup>401</sup> *ibid* 389

<sup>402</sup> *Carter* (n1)

assured test, which is a reflection of the prudent insurer test, as stipulated in section 18 and 20 of the MIA 1906, is an objective test. In the event that the court decides on using the prudent insurer's test, underwriters are called to submit evidence for the judges as a reference of the mainstream insurer's view. In other words, the market practice helps to regulate the conduct of the insurer and formed an objective standard of how a prudent insurer will act in a particular situation. This, however, is not applicable to the situation of an insurer's duty of utmost good faith. There is no objective standard of how a prudent assured will work on a particular underwriting situation, as there is no market trend and behaviour that regulates the attitude of the assured during the underwriting process. Furthermore, save and except for those large companies who have their own insurance departments, it is highly unlikely that the assured can systematically assess the risk before purchasing insurance. Therefore, it is unlikely that in the situation where the insurer is in breach of the duty, the other assured in the market will be able to testify under the prudent assured test. The problem with this approach is that the situation will heavily rely upon the judges to draw a reasonable inference from the situation on a case-by-case basis. Although this approach is flexible, it is also unpredictable, which no doubt affects the accessibility of law.

The other problem of the reflection approach is the remedy. Since the remedy for the assured's duty of utmost good faith is avoidance as a reflection of the duty, the only remedy for the insurer's duty can also only be the remedy of avoidance, yet this can be meaningless to the assured. In addition to that, the enactment of the IA 2015 has introduced a duty of fair presentation, which repealed the utmost good faith of the assured under section 18 and 20 of the MIA 1906. The legal requirements are now more detailed, and are uniquely decided based on the assured's duty of utmost good faith, which are not applicable to the insurer's duty. For instance, section 3(3)(b) of the IA 2015 requires the assured to disclose information to the insurer in a manner which is "reasonably clear and accessible to a prudent insurer". One of the reasons for introducing this requirement, as discussed in chapter 2 of this thesis, is to avoid data dumping. This is a technical point which exists in practice during the underwriting process. This, however, is not applicable to the situation where the disclosure is made by the insurer to the assured. The insurer, as the decision by the House of Lords identified, only needs to disclose material information that will affect the risk. It is rarely the case that the insurer will

possess enough information, which is related to the risk, to commit “data dumping” to the assured.

The other potential problem is that section 8 and schedule I of the IA 2015 has introduced a new set of remedies that are awarded depending on the seriousness of the breach by the assured.<sup>403</sup> In particular, the IA 2015 has imposed a proportionate reduction of claim, which allows the insurer to reduce the payment for the claim in accordance with the percentage of the increase in the premium, should the breach not have been committed by the assured. It is submitted that this approach is meaningless for the insurer’s duty. For example, as a reflection of the assured’s remedy, the insurer’s duty can impose a new remedy that allows the assured to proportionately reduce the premium bases on the degree of inducement of the breach. The proportionate remedy, for the assured’s duty, can discourage the assured to present the risk unfairly, as the amount of reduction of a claim can be significant.<sup>404</sup> This approach, on the other hand, is less significant for the insurer, because the premium amount is normally much lower than the claim amount. Therefore, a proportionate reduction of a premium is not an effective remedy to discourage unfair presentation by the insurer. As a result, it is suggested that at this stage, since the insurer’s duty is still developing, a simpler and clearer remedy is more favourable for the insurer’s duty of utmost good faith. Hence, the decision by the House of Lords, which may suggest a reflection of a complicated proportionate reduction of claim, may not be preferable to solve the current problem in relation to the insurer’s duty of utmost good faith.

In this regard, it is submitted that the general good faith approach, which was imposed by Steyn J in the first instance court may be more operable for the insurer’s duty of utmost good faith. Although it is arguable that the approach deviated from the spirit of *Carter v Boehm*,<sup>405</sup> this approach is easier to follow, as it does not include the technical issues that are suggested above. More importantly, it ascertains that the insurer is also bound to perform in good faith, which ensures the fairness between the parties.

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<sup>403</sup> The details will be discussed in section II of this chapter.

<sup>404</sup> For the details of the operation of the proportionate remedy, please refer to section II of this chapter.

<sup>405</sup> *Carter* (n1)

The other point in favour of Steyn J's approach is that this approach is also applicable to an insurer's post-contractual duty of utmost good faith. While the pre-contractual duty of the insurer has an indefinite scope, it is suggested that the post-contractual duty has no scope at all. The mainstream approach to mirror the assured's duty at the pre-contractual stage is not applicable to the post-contractual duty, as the current materiality and inducement tests are decided for risk underwriting. Furthermore, for the pre-contractual duty of the assured, it is clearly stated in both the MIO and the MIA 1906, as well as the IA 2015, and therefore it is easy for the insurer's duty at the pre-contractual stage to reflect the assured's duty. For the post-contractual duty of both the insurer and the assured, none of the legislation has addressed this area of law. In terms of case law, the mainstream view is that the application of post-contractual duty of the assured has no practical effect.<sup>406</sup> In this regard, it is highly unlikely that the post-contractual duty of the insurer can be reflected from the assured's duty at the post-contractual stage.

In addition to the mirror approach, the only perspective that one can take to analyse the post-contractual duty of the insurer is to study case law that is relevant to this issue. Nevertheless, it is submitted that this approach has little significance in defining the scope of the duty. In both the Lloyd's Law Report and the Lloyd's Insurance and Reinsurance Law Report, there are 21 English cases that have referred to the term "post-contractual duty of utmost good faith" since 1996.<sup>407</sup> Among these cases, there are only a small number that have identified what amounts to a breach of post-contractual duty for the insurer.

In *Drake Insurance Plc (In Provisional Liquidation) v Provident Insurance Plc*,<sup>408</sup> Lord Justice Rix held that it was a matter of bad faith for the insurer to avoid the insurance contract in the situation where the assured had not disclosed a no-fault accident to his motor insurer.<sup>409</sup> Although Lord Justice Rix did not clearly underline what the scope for the post-contractual duty was, it was submitted that the operation of such a duty was not as complicated as the same

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<sup>406</sup> See Merkin (n42), para A-0666. See also Law Commission, Reforming Insurance Contract Law, Issues Paper 7: The Insured's Post-Contract Duty of Good Faith (July 2010), para 6.4 – 6.49. Nevertheless, it does not mean that the post-contractual duty of utmost good faith does not exist, and for the future potential issue on the post-contractual duty, the Law Commission has not removed section 17 as a general principle of utmost good faith.

<sup>407</sup> Please refer to Annex 2 for the summary of the cases. These cases were all held after *The Pan Atlantic* case in 1995, which the inducement test was confirmed by the House of Lords for the duty of utmost good faith.

<sup>408</sup> *Drake Insurance* (n181)

<sup>409</sup> *ibid* [91] – [93]. Judging from the content, it is logical to deduce that a matter of bad faith amounts to a breach of utmost good faith. See also Gürses, O. (2016). 'What does 'utmost good faith' mean?' *Insurance Law Journal*, 27, 124-134.

duty at the pre-contractual stage. Lord Justice Rix examined the case facts and balanced the two possibilities, namely, the consequence that the assured would face when the insurer avoided the contract, and the consequence that the insurer would face when the assured had disclosed the no-fault accident to the insurer.<sup>410</sup> Lord Justice Rix concluded that the insurer was in breach of good faith to avoid the contract based on the non-disclosure of the no-fault accident by the assured. It is submitted that this approach is entirely different from the mirror approach as mentioned above, but rather similar to Steyn J's approach, which is to examine the situation as a general question of good faith.

In another case, *K/S Merc-Scandia v Certain Lloyd's Underwriters*,<sup>411</sup> Lord Justice Longmore identified that there were two situations that required the insurer to perform in good faith at the post-contractual stage.<sup>412</sup> The first situation was that the underwriter had a right to the knowledge based on an express/implied term under an insurance contract.<sup>413</sup> The second situation was that under liability insurance, the post-contractual utmost good faith arose when the insurer took over the defence of the claim from the assured.<sup>414</sup> The insurer must have acted in good faith and considered the interest of the assured when incurring costs during the process of defence.<sup>415</sup>

This duty was illustrated in *Cox v Bankside*,<sup>416</sup> where the insurer contended that the assured was liable to bear the cost that had incurred for the defence of the claim, which had been taken over by the insurer. This proposition was rejected by the Court of Appeal, and it was held that the remedy of rescission was not the only remedy available to the assured in the situation

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<sup>410</sup> *ibid* [82], [93]

<sup>411</sup> [2001] 1 Lloyd's Rep IR 802

<sup>412</sup> *ibid* page 814. This proposition is acknowledged by Judith Prakash J in *Stansfield v Consumers' Assoc of Singapore* [2012] Lloyd's Rep. IR Plus 13, but Judith Prakash did not go further to identify the scope of the post-contractual duty of the insurer.

<sup>413</sup> It is submitted that, this situation, however, has little significance in practice, as the breach of contractual terms will allow the parties to seek remedies for the loss, and it may not be necessary for the parties to seek remedies under the duty of utmost good faith. Nevertheless, a claim in relation of utmost good faith is always a good alternative for suing the opposite party under an insurance contract when there is a breach of contractual terms. Please refer to Annex 2 and 3 for the case summaries that involve this approach.

<sup>414</sup> *K/S Merc-Scandia* (n416) [22]

<sup>415</sup> *ibid*. This duty was illustrated in the case *Cox v Bankside* [1995] 2 Lloyd's Rep. 437, where the insurer contended that the assured was liable to bear unlimited cost incurred in the event that the insurer had taken over the defence of a claim. This proposition was rejected by the Court of Appeal, and the court held that it was wrong to hold that the remedy of rescission was the only remedy available to the assured in the situation where the insurer was in breach of the duty of utmost good faith. See 462-463

<sup>416</sup> *ibid*

where the insurer was in breach of the duty of utmost good faith.<sup>417</sup> Similar to the case of *Drake Insurance Plc*,<sup>418</sup> the court ruled on this issue by simply asking a general question of good faith, namely whether the insurer was allowed to incur unlimited costs without the consent of the assured in defending a claim. Again, without acknowledging any previous authorities or technical requirements, as mentioned in the House of Lords decision on *Banque Keyser*,<sup>419</sup> the court held in favour of the assured on this issue. These authorities suggested that although Steyn J's approach may not be favourable when judging the matter from the perspective of pre-contractual duty only, if viewing the insurer's duty, including both pre-contractual and post-contractual duties, as a whole, the simple approach that was proposed by Steyn J's may not be unfavourable.

To sum up, it is suggested that the recent cases, for both pre-contractual duty and post-contractual duty, have not provided a clear definition for the scope of the duty of utmost good faith for the insurer to comply with. Nevertheless, these cases have suggested that the application of the post-contractual duty of the insurer is entirely different from the approach of the pre-contractual duty, which was suggested in the House of Lords decision on *Banque Keyser*.<sup>420</sup> While it may be possible to identify the scope of the pre-contractual duty of the insurer by reflecting the assured's duty, the apparent fact regarding the operation of the post-contractual duty is that, since there is no scope for the duty, the duty is no longer limited to the action of disclosure or presentation. As a result, there is no room for the application of the materiality or inducement test. In other words, the scope of the insurer's post-contractual duty is indefinite, and the said duty is inconsistent with the insurer's pre-contractual duty. The current state of law is no doubt uncertain and this is unfavourable for the parties to an insurance contract. It is therefore submitted that the law needs to provide a certain scope for the reader of the legislation to comply with and to be able to foresee the consequences of the breach of duty by the insurer.

Nevertheless, it is submitted that the scope of the duty is not the most problematic part of this area of law. The most problematic aspect is that the single remedy of avoidance is inadequate

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<sup>417</sup> *ibid* 462-463

<sup>418</sup> *Drake Insurance* (n181)

<sup>419</sup> *La Banque Keyser* (n21)

<sup>420</sup> *ibid*



for the needs of the assured. No matter how clear the scope of the duty has been stated in the law,<sup>421</sup> without an adequate remedy, this area of law becomes meaningless. In the following section, the issue of an inadequate remedy for the insurer's duty will be examined.

### **B. The inadequate remedy for the insurer's duty of utmost good faith**

The problem of a lack of adequate remedy for the insurer's duty of utmost good faith, as in the case of the scope of the insurer's duty, is also illustrated in *Banque Keyser v. Skandia*.<sup>422</sup> In the first instance court, Steyn J held that the banks were entitled to recover their losses from the insurer by damages. In response to the single remedy approach of utmost good faith, Steyn J was of the view that instead of strictly complying with the single remedy approach, the legal principle and policy reason should have been taken into consideration in the situation where the insurer was in breach of the duty of utmost good faith. Since in the present case, damages were the only remedies that were useful to the banks, it would be unjust and unfair if the said remedies were not granted to the banks.<sup>423</sup>

However, this decision was rejected by the Court of Appeal. In his judgment, Slade LJ noticed that there had been no reported cases in England and Wales that had ever granted damages as remedies under the duty of utmost good faith. It was concluded that the duty was a statutory duty but not a contractual obligation, and therefore the assureds were not entitled to claim damages.<sup>424</sup> The other reason was that it was rarely the case that the insurer could possess any information, which was material to the risk, that the assured had no knowledge of. As a result, the remedy of avoidance was deemed adequate to serve the purpose of protecting the insurer from information asymmetry.

Slade LJ also noticed that there were cases in which the insurer had possessed material information that the assured had no knowledge of before the formation of the insurance contract. Nevertheless, Slade LJ was of the view that the remedy of avoidance was not entirely inadequate for the assured. In the situation where the assured could discover the breach before any loss occurred under the policy, the remedy of avoidance provided an option for the assured

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<sup>421</sup> Which is not the case at present.

<sup>422</sup> *ibid*

<sup>423</sup> *Banque Keyser* (n397) 96

<sup>424</sup> *La Banque* (n401) 546

to avoid the contract and obtain a refund of premium. In most cases, such a breach of duty would only be discovered after the loss happened, and such a remedy would not be adequate for the assured in cases where the breach was committed by the insurer.<sup>425</sup> The learned judge also suggested that the remedy of avoidance may be inadequate for the insurer in the situation where the breach had induced the insurer to accept a risk at a far lower premium than it should have been charged.<sup>426</sup>

The learned judge agreed that in the present case, the remedy of avoidance was inadequate to the assured, nevertheless, he rejected Steyn J's judgment for four reasons. Firstly, since the remedy of avoidance originated from the Court of Equity, it was highly unlikely that damages could be granted under the duty of utmost good faith, as there was no such option under the law of equity.<sup>427</sup> Secondly, since the legal requirement of non-disclosure required the insurer to pass the prudent insurer test, if the same requirement had been transferred to the assured, it was highly unlikely that damages could be assessed, as the current law had not considered the requirement of the prudent assured test. Thirdly, there were no sections in the MIA 1906 that expressly stated that damages were available under the duty of utmost good faith. Lastly, if the court had allowed the banks to seek damages under tort law, such a creation of new obligation would open a floodgate of claims in relation to any conduct before and after the conclusion of the insurance contract, the approach of which was unfavourable to ensure certainty between the parties to an insurance contract.

In the House of Lords, the decision of the Court of Appeal was upheld by the judges, and it was held that the banks were not entitled to damages, as the insurer did not have any duty to disclose the fraud of its agent to the banks. Lord Templeman added in his judgment that even if the insurer was in breach of the duty of disclosure in the context of utmost good faith, the only sound remedy would be the avoidance of contract and return of premium.<sup>428</sup>

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<sup>425</sup> *ibid* 547

<sup>426</sup> *ibid* 548. Nevertheless, it is suggested that this situation rarely happens in commercial practice.

<sup>427</sup> *ibid* 550

<sup>428</sup> *Banque Keyser* (n21) 387-388

The judgment of *Banque Keyser v Skandia*<sup>429</sup> is problematic as Slade LJ did not proffer a solution to the problem. Furthermore, the statement that damages should not be granted because section 17 does not expressly mentioned this remedy may not comply with the legal logic of the MIA 1906. One of the examples is that in section 18 and 20 of the MIA 1906, the inducement tests are not expressly stated in the legislation. Nevertheless, in the *Pan Atlantic* case,<sup>430</sup> the House of Lords held that the inducement tests were implied in the legislation.<sup>431</sup> If Slade LJ's logic that the legal requirement is not mentioned in the legislation and therefore does not exist is correct, then the said inducement tests would not be implied in section 18 and 20. Thus, it is submitted that the judgment of Slade LJ may not be legally sound.

From the above analysis, one can observe that the judges in England and Wales took conservative approaches to the problem that there is no adequate remedy for the assured under the duty of utmost good faith. On the one hand, the judges admitted the fact that the remedy of avoidance is inadequate for the assured, but on the other hand, the judges have simply refused to grant damages, ignoring the fact that there is no other available option for the assured. The factors as to whether the remedy originated from the Court of Equity, or whether it is the original intention of the draftsman of the MIA 1906 to include damages as a remedy of utmost good faith, are relevant, but these factors are not useful in order to overcome the inadequacy.

The Law Commission, although aware of the problem, has not taken any action to solve it, and the IA 2015 has been totally silent on this issue. In the Law Commission Report, the reason for this attitude is explained by the Commissioners as follows:

We do not envisage that the courts will readily regard the removal of avoidance as an opportunity to find that damages are payable for breach of good faith, having showed no such appetite in the past. However, judicial intervention may be appropriate in an extreme case.<sup>432</sup>

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<sup>429</sup> *ibid*

<sup>430</sup> *Pan Atlantic* (n46)

<sup>431</sup> *ibid* 105

<sup>432</sup> Law Commission (n4) para 30.53

In other words, the removal of avoidance offered the court an opportunity to revisit the issue of whether damages can be awarded for a breach of the duty of utmost good faith by the insurer. Nevertheless, judicial intervention may not be the best way to address the problem, because case law in England and Wales had clearly rejected the proposition that damages can be awarded for breach of the duty of utmost good faith.<sup>433</sup> In this regard, it is submitted that the reform of the insurer's duty of utmost good faith may require legislative change rather than judicial intervention.

In Hong Kong, although there have been three court cases that have cited the *Banque Keyser v Skandia*<sup>434</sup> as an authority,<sup>435</sup> there has only been one case that has discussed the issue of utmost good faith, namely *Wunsche Handelsgesellschaft International Mbh v General Accident Insurance Asia Limited*.<sup>436</sup> In this Hong Kong case, the court held that the remedy of avoidance was the only remedy that was available for the insurer's breach of utmost good faith and therefore, even if the assured's plead was successful, which in this case was not, there was no option other than the remedy of avoidance, which was not available to the assured.<sup>437</sup> Since this judgment has not touched upon the issue of legitimacy of granting remedies other than avoidance under the duty of utmost good faith, it is submitted that in Hong Kong, it is unlikely that this problem can be solved solely through case law. Therefore, this potential problem should be solved by reforming the current legislation with regard to the utmost good faith.

### **C. Formulating the new insurer's duty of utmost good faith as a solution for the current problem**

After examining the two problems above, this section aims to propose a reform for the scope, as well as the remedy for the insurer's duty of utmost good faith. The first part of this sub-section regards the reform approach for the scope of insurer's duty. Since the scope of the insurer's duty is indefinite, the reform cannot be achieved by a legislative change, and a judicial development is preferred. The second part regards the reform strategy of the remedy for the insurer's duty. Since the problem of the remedy is caused by the existing legislative provision, it

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<sup>433</sup> David Kendall and Harry Wright, *Practical Guide to the Insurance Act 2015* (Informa 2017) Para 11.3-11.4.

<sup>434</sup> *Banque Keyser* (n21)

<sup>435</sup> The three cases are *UBC (Construction) Limited and Sung Foo Kee Limited Construction List No. 11 of 1991*, *Wunsche Handelsgesellschaft* (n19) and *Secretary for Justice and Shum Chiu and the others HCAL 101/2005*

<sup>436</sup> *ibid*. The case fact is mentioned in the Introduction of this thesis.

<sup>437</sup> *ibid* [17]

is submitted that the reform should be introduced through a legislative change, namely, the amendment of section 17 of the MIO. Judicial intervention is not preferred, as the House of Lords has already confirmed, in the case of *Banque Keyser v Skandia*,<sup>438</sup> that damages cannot be awarded for the breach of the duty of utmost good faith. Therefore, in the following subsection, a detailed reform recommendation will be provided for reforming the insurer's duty of utmost good faith.

**i. The approach of formulating the scope of the insurer's duty of utmost good faith**

In relation to the first problem, since current English and Hong Kong law do not have a definite answer for the scope of the insurer's duty, it may not be favourable to impose a concrete definition such as non-disclosure and misrepresentation for the assured's duty as a reform suggestion. Thus, it is suggested that a further judicial development would seem to be more desirable than a legislative change in relation to the scope of the insurer's duty of utmost good faith.

Nevertheless, regardless of the matter of flexibility, it is submitted that, at this stage, to ensure fairness between the parties to an insurance contract, it is still necessary to decide the operation and the legal requirement of the insurer's duty of utmost good faith. The existing approach, as mentioned in the above sections, is a choice between Steyn J's approach, which is a general good faith approach, and the House of Lord's approach, which is a mirror approach of the assured's duty. For the reasons that have been given above, and as a matter of elimination, the author is of the view that Steyn J's approach should be adopted, as the mirror approach is simply inapplicable to the post-contractual duty of the insurer, and it certainly causes more uncertainty and inconsistency by distinguishing between the pre-contractual and post-contractual duty of the insurer. It is arguable that this approach is very unfavourable for the insurer. However, considering the current state of law, which is one-sided for the insurer, this reform may have a positive impact on preserving a balance between the parties to an insurance contract. Furthermore, the relatively low amount of case authorities in relation to the insurer's duty of utmost good faith suggests that this area of law has a limited application in practice, and

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<sup>438</sup> *Banque Keyser* (n21)

it will not have a destructive impact on the balance of interest for the parties to an insurance contract.

**ii. The approach of imposing an adequate remedy for the insurer's duty of utmost good faith**

In addition, it is submitted that the development of the scope of the insurer's duty heavily would rely on an adequate remedy for the insurer's duty of utmost good faith. Without an adequate remedy, there will be no chance that judges will be able to identify what the scope of the duty is in the future, because there is no necessity to do so, as the duty is a claim without remedy. Therefore, for the reform proposal, the second problem has to be solved by way of imposing a clear and adequate remedy in the legislation. This is the only way to encourage judges to make further developments and establish the scope of the insurer's duty for the future.

Based on the two considerations above, the author suggests that damages, as an alternative remedy to avoidance, should be imposed to reform the insurer's duty of utmost good faith. Furthermore, there are at least two ways to achieve this purpose. The first is to impose the remedy by way of discretion of the court. This solution is suggested by Peter Macdonald Eggers QC in his article 'Remedies for the failure to observe the utmost good faith', where he suggested that the remedy of avoidance should only be granted upon discretion. In the case where it is disproportionate to award avoidance to the parties,<sup>439</sup> the court can consider awarding damages to ascertain fairness.<sup>440</sup> It is suggested that the operation of this discretionary remedy is similar to the operation of the Misrepresentation Act 1967, where section 2(2) of the Act allows the court to award damages in replacement of rescission if the court considers it appropriate.<sup>441</sup> The advantages of this approach are that, firstly, it provides flexibility for the court to consider what is the most appropriate remedy for the suffering party on a case-by-case basis. Secondly, it does not require a drastic change of law, as the remedies are granted by judicial discretion, which is likely to minimise the impact and cost of legal

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<sup>439</sup> Peter Macdonald Eggers, 'Remedies for the Failure to Observe the Utmost Good Faith' (2003) *Lloyd's Maritime and Commercial Law Quarterly*, p.249

<sup>440</sup> The author also suggests that in appropriate cases it is also possible to grant both avoidance and damages for the breach of utmost good faith.

<sup>441</sup> Peter Macdonald Eggers (n444) p.269

reform.<sup>442</sup> Nevertheless, it is submitted that certainty is a problem of this approach, as there is no juristic basis to ensure what the requirements of the judicial discretion are, and the result of the breach becomes unpredictable. The accessibility of the law may also become a problem, as the reader of the legislation may not be able to identify the existence of such a discretion, which may not be favourable for a jurisdiction like Hong Kong, where utmost good faith may not be understood by the insurance practitioners in general.<sup>443</sup>

The second way of reforming the remedy of utmost good faith is to transfer the duty of utmost good faith from a statutory duty to an implied term of insurance contract, which allows the party that has suffered to seek damages. For instance, section 14(1) of the Insurance Contract Act 1984 in Australia stipulates that:

A contract of insurance is a contract based on the utmost good faith and there is implied in such a contract a provision requiring each party to it to act towards the other party, in respect of any matter arising under or in relation to it, with the utmost good faith.

The Australian reform is not without its own problem. For instance, the scope of the duty and the assessment of damages are not clearly defined in the legislation, and confusions have arisen in many cases.<sup>444</sup> Furthermore, in *Manifest Shipping Co Ltd v Uni-Polaris Shipping Co Ltd and others*, Lord Hobhouse held that breaching the duty of utmost good faith was not a breach of an implied term, and thus there was no remedy in damages.<sup>445</sup> Although a legal reform is intended to solve the problem of the inadequacy of the remedy for the insurer's duty, the way of transforming the duty from an operation of law to an implied term may further complicate the problem. Therefore, it is suggested that strictly following the Australian approach would also not be an appropriate type of reform in Hong Kong. Nevertheless, it is submitted that the solution to this issue in Hong Kong law should consider both reform approaches and preserve the advantages of both approaches.

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<sup>442</sup> *ibid* p.278

<sup>443</sup> The matter of certainty was explained by the Peter Macdonald Eggers QC in his article. Objectively, this approach has minimal impact on certainty in a jurisdiction where the insurance practitioners have a good understanding of insurance law. Nevertheless, it may not be the case in Hong Kong, and it is suggested in the later part of this subsection that a more conservative approach will be adopted for the reform proposal.

<sup>444</sup> For the problems of the Australian law reform, please see Robert Merkin, *Reforming Insurance Law: Is there a case for reverse transportation?* a report for the English and Scottish Law Commissions on the Australian Experience of insurance law reform.

<sup>445</sup> See, for instance, *Manifest Shipping Co Ltd v Uni-Polaris Shipping Co Ltd and others (The "Star Sea")* [2001] 1 Lloyd's Rep IR 247 [47] – [49]

### iii. The solution

The significance of reforming the insurer's duty of utmost good faith is to provide a new possibility of seeking remedies other than the remedy of avoidance by the assured. To achieve this purpose, the only amendable section under the MIO is section 17, because section 18 and 20 are concerned with the duty of utmost good faith of the assured at the pre-contractual stage, and section 19 is concerned with the duty of disclosure of the agent to insure. Therefore, firstly, the new section 17 should be able to provide the remedy of damages for the assured. The discretionary approach is a good approach; however, the problem is that it is not stated in the legislation and it lacks certainty and accessibility for the reader of the legislation. Alternatively, although the Australian reform has solved the problem of accessibility, the operation of the duty of utmost good faith as an implied term has further complicated the operation of the duty. Additionally, it also deviates from the traditional English law approach that the duty of utmost good faith is a common law duty but not an implied term of contract, thus this approach may not be favourable for Hong Kong. It is submitted that, to preserve a balance between the two approaches, a discretion from the judges to award damage should be expressly imposed in section 17 of the MIO as an alternative remedy of avoidance for breaching the duty of utmost good faith.

Secondly, it is suggested that the new section 17 should be separated from section 18, 19 and 20 of the MIO. For the cases in relation to non-disclosure and misrepresentation by the assured, it is submitted that the insurer will claim against the assured under a new duty of fair presentation, which covers section 18, 19 and 20 of the MIO.<sup>446</sup> The new section 17 only covers the duty of utmost good faith for the insurer, and any other potential utmost good faith issues that are not identified at present, but may appear in the future as time goes by. The new section should ensure that there is an element of flexibility for the future development in this area of law. It is therefore suggested that the reform should be done by way of amending the language of section 17 of the MIO in Hong Kong, which reads as follows:

A contract of insurance is a contract based on the utmost good faith and, if the utmost good faith be not observed by either party, the contract may be avoided by the other

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<sup>446</sup> The details of this new duty of fair presentation for the law reform in Hong Kong, which is different from the said duty under the IA 2015, will be discussed in section II of this chapter.



party. The court or arbitrator may declare the contract subsisting and award damages in lieu of avoidance, if of opinion that it would be equitable to do so, having regard to the nature of the breach of utmost good faith and the loss that would be caused by it if the contract were upheld, as well as to the loss that avoidance would cause to the other party.

To separate the duty of utmost good faith from the duty of fair presentation, section 17(2) should be added to the MIO as follows:

This section does not apply to matters arising under or in relation to the duty of fair presentation, which is provided in section 18, 19 and 20 of this ordinance.

This reform has solved the problems that are identified in this section from several perspectives. Firstly, it is suggested that a total removal of the remedy of avoidance may not be favourable, as there are still circumstances in which avoidance is a suitable remedy for the assured; namely, where the breach is identified before the loss has occurred. In this situation, the assured can avoid the contract, recovering the premium from the insurer and seek other insurance coverage from another insurer. The problem of the remedy of avoidance under the utmost good faith is that it cannot be the sole remedy for the duty, as the parties to an insurance contract may have different needs of remedies for the compensation of the loss caused by the breach.

Secondly, to address the need of the assured under utmost good faith, the reform of the legislation has added the remedy of damages in section 17 as a statutory remedy. The wording of it is identical to the Misrepresentation Act 1967 and the Misrepresentation Ordinance, which ensures that the assessment of damages and the requirement of discretionary remedy will not be deviated from the traditional English law approach. Since damages have been added to the legislation as a statutory remedy, the award of damages under the reformed section 17 will be of a discretionary nature, which ensures that there is enough flexibility for the judges to consider the detriment of granting avoidance on a case-by-case basis.

Furthermore, by imposing damages as a statutory remedy for the assured, it also solves the problem of the scope of the duty for the insurer. In the previous sub-section, it is submitted that

firstly, as a whole, the duty of utmost good faith of the insurer is not clearly defined. Secondly, by dividing the duty into pre-contractual and post-contractual duty, these two duties have separate legal requirements and applicability, which is confusing. The language of the reformed section 17 suggests that such a discrepancy between the pre-contractual and post-contractual duty of the insurer no longer exists, as both duties will now be considered and examined based on two criteria. Firstly, whether a general principle of good faith is observed, and secondly, whether there is a detriment that the party will suffer if avoidance is granted. It provides a unification for the legal requirements for the pre-contractual and post-contractual duty of the insurer, and it also ensures that the insurer's duty will be examined under the same set of requirements, which helps to ensure certainty and accessibility of this area of law.

This reformed section 17 also provides flexibilities for the judges in Hong Kong to revisit the scope of the insurer's duty in the future. In addition, there may be further development of this area of law in English law in the future, and the flexible scope and remedies in this area of law ensure that Hong Kong judges may follow the English law approach in the future. Alternatively, the Hong Kong judges can examine the duty based on Steyn J's approach and the Misrepresentation Ordinance to ensure that the assured is able to recover losses from the insurer under the duty of utmost good faith. This approach, of course, is not perfect, as at this stage the operation still lacks certainty, therefore the operation of the duty should not be expressly stated in the legislation. Nevertheless, this reform ensures that adequate remedies can be provided to the assured, which is more preferable than either following the approach of MIA 1906 or IA 2015. Without an adequate remedy, there is no necessity for the judges to develop the scope of the insurer's duty, and true fairness between the parties will never be achieved.

The suggested reform ensures that Hong Kong judges, with or without the assistance from the English law, must develop a comprehensive system to examine the insurer's duty of utmost good faith in the future. It is submitted that to achieve true fairness between the parties to an insurance contract, it is necessary to impose an operable duty of utmost good faith to the insurer, and this reform has provided an accessible way to achieve this purpose.

## **II. The second problem of the remedies - the problem of disproportionality to the assured**

The second problem, in relation to the remedies of utmost good faith/fair presentation, regards the problem of disproportionality under the MIO, the MIA 1906 and IA 2015. Firstly, it is submitted that under the MIO, the remedy of avoidance is the only remedy that is available to the assured. This single remedy approach disregards the matter of the seriousness of the breach and degree of loss that the insurer suffers from the breach, and therefore is disproportionate to the assured. Secondly, although the IA 2015 has imposed a set of remedies which is more proportionate to the assured, it is submitted that the problem of disproportionality still exists. To examine these problems the first part of this section will analyse the problem of disproportionality under the MIO, the MIA 1906 and the IA 2015, and in the second part, a reform proposal will be provided to solve the problem of disproportionality in Hong Kong.

### **A. The problem of disproportionality in relation to the remedies of utmost good faith/fair presentation**

#### **i. The problem of the single remedy approach under the MIO – the remedy is disproportionate to the seriousness of the breach and the loss that is caused by the breach**

The problem of disproportionality of the remedy can be analysed from two perspectives. The first is that the single remedy approach disregards the seriousness of the breach of duty, the result of which is that those who have committed a serious breach of duty (i.e. fraudulent misrepresentation) will be treated in the same way as those who have committed a minor or careless breach of duty (i.e. innocent or negligent non-disclosure/misrepresentation). The remedy, in this regard, is disproportionate to the degree of wrong that is committed by the wrongdoer.

Many judges have criticised the unsatisfactory status of the remedy. For example, in *Kausar v Eagle Star Insurance Co Ltd*,<sup>447</sup> Lord Justice Staughton expressed his view that the doctrine allows the insurer to deny liability when the assured acted dishonestly to conceal material

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<sup>447</sup> [2002] 1 Lloyd's Rep IR 154

information, but the doctrine should be applied with restraint as it is severe for the honest assured.<sup>448</sup>

This proposition is explained in detail by Lord Justice Rix in *Drake Insurance plc v Provident Insurance plc*.<sup>449</sup> Given the severe nature of the remedy, the learned judge explained that the original purpose of such a harsh remedy was to protect the insurer from the unfair presentation of the assured. However, the recent case law has suggested that the judges in England and Wales had realised that the remedy was draconian and therefore, restriction such as an inducement test had been imposed to limit the application of the doctrine.<sup>450</sup> Nevertheless, the learned judge also suggested that the spirit of English commercial law, which included the doctrine of utmost good faith that originated from marine insurance, was not about proportionality. The law was about simplicity and certainty, and the parties in commerce were encouraged to protect their business interest by their own means.<sup>451</sup> Nevertheless, he acknowledged that the nature of insurance contracts had changed in recent times, as the use of an insurance contract is no longer only limited to commercial activities, but has also spread to other areas, which are privately or socially driven. The learned judge concluded that the law should therefore consider addressing the problem of proportionality,<sup>452</sup> which was ignored under the MIA 1906.

The second problem, in relation to the matter of disproportionality, is that the remedy of avoidance has not preserved a balance between the loss of the insurer, which is caused by the breach of duty, and the loss of the assured, which is caused by the remedy of avoidance. With the exception of the situation in which the insurer will refuse to underwrite the risk, it is submitted that the loss of the insurer, which is caused by a breach of duty of utmost good faith, is no more than a loss of charging an additional premium, which is normally lower than the indemnity. It is therefore disproportionate to allow the insurer to avoid the contract in the case that the loss of the insurer is insignificant in comparison to the loss that the assured has suffered from the remedy.

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<sup>448</sup> *ibid* 157

<sup>449</sup> *Drake Insurance* (n181)

<sup>450</sup> *ibid* [87]

<sup>451</sup> *ibid* [88]

<sup>452</sup> *ibid* [89]

One may argue that the loss of the insurer is not only about the additional premium, but in a case where the breach is not discovered by the insurer, the loss of the insurer will include the payment of indemnity that the assured is not entitled to claim. Nevertheless, this proposition has disregarded the fact that disputes in relation to utmost good faith only occur when the insured risks are materialised. By the time that the dispute has arisen, and the parties bring the case to the court, there is no chance that the insurer will pay the indemnity, unless the judgment is held against the insurer. In other words, the said loss of the indemnity payment will never be an actual loss, therefore it is unfair to take this loss into consideration when deciding whether the remedy is proportionate.

This problem is illustrated in *Wise Ltd v Grupo Nacional Provincial SA*,<sup>453</sup> where the reinsurer pleaded for non-disclosure for a careless translation mistake for the insured goods. The goods were luxury watches, but the mistaken translation induced the reinsurer to believe that the goods were simply clocks. The judges accepted the fact that the non-disclosure was not fraudulent, but only a careless mistake.<sup>454</sup> As this case concerned a reinsurance contract, it was highly unlikely that the reinsurer would have denied taking the risk merely because the value of the goods was high, as the reserve budget for a reinsurance contract is normally higher than the one in the insurance contract. Besides, it was likely that in commercial practice, the reinsurer, had they known of the mistake before the conclusion of the reinsurance contract, would simply have charged a higher premium instead of refusing to enter into an insurance contract. There was also no evidence indicating that the reinsured risk was too high to be underwritten, as the risk assessment should have already been made by the reinsured during the formation of the insurance contract, and the apparent fact that the reinsured had decided to underwrite the risk suggested that this risk was capable of being underwritten by the reinsurer.

Nevertheless, the aspect of unfairness of the remedy is that, after the loss happens, and the insurer discovers the non-disclosure, the insurer can avoid the contract instead of charging an additional premium. This remedy provides a means for the insurer to escape from the liability to indemnify the assured, but the actual loss of the insurer is no more than the additional premium.

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<sup>453</sup> *Wise Ltd* (n40)

<sup>454</sup> *ibid* [9]

It is therefore submitted that the current remedy of avoidance cannot provide a proportionate measure to the assured.

In any event, it is submitted that the Law Commission is aware of the problem, and the IA 2015 has imposed new proportionate remedies to solve the unfair situation. The author is of the view that the new remedies have improved the situation, but they have not solved all the problems. In particular, it is the new remedy of reduction of claim that is not as proportionate as it appears to be. The details of the new remedies and the problems behind them will be examined in the next section.

**ii. The problem of the proportionate remedies under the IA 2015 – the disproportionality between the increase of a premium and the reduction of a claim**

Under the IA 2015, the remedy of avoidance is no longer the only remedy that is available for breaching the duty of utmost good faith/fair presentation. All sections that are related to the remedy of avoidance are now omitted from the MIA 1906. Instead, for the assured's duty of disclosure and misrepresentation, the new duty of fair presentation is imposed with a new set of remedies, which includes the remedy of avoidance, alteration of contractual terms and proportionate reduction of a premium. Section 8 of the IA 2015 provides that:

- (1) The insurer has a remedy against the insured for a breach of the duty of fair presentation only if the insurer shows that, but for the breach, the insurer—
  - (a) would not have entered into the contract of insurance at all, or
  - (b) would have done so only on different terms.
- (2) The remedies are set out in Schedule 1.
- (3) A breach for which the insurer has a remedy against the insured is referred to in this Act as a “qualifying breach”.
- (4) A qualifying breach is either—
  - (a) deliberate or reckless, or
  - (b) neither deliberate nor reckless.
- (5) A qualifying breach is deliberate or reckless if the insured —
  - (a) knew that it was in breach of the duty of fair presentation, or
  - (b) did not care whether or not it was in breach of that duty.

(6) It is for the insurer to show that a qualifying breach was deliberate or reckless.

In contrast to the MIA 1906, the IA 2015 states that there are two levels of breach of the duty of fair presentation. The first level regards a breach that is either deliberate or reckless. The second level regards a breach that is neither deliberate nor reckless. Under the IA 2015, there are now three different remedies that depend on the seriousness of the breach of the duty of fair presentation.

The first remedy is that the insurer is entitled to avoid the contract in two different situations. In the first situation where the breach is deliberate or reckless, the insurer is entitled to avoid the insurance contract and need not return any obtained premium to the assured.<sup>455</sup> This approach is proportionate, and it has not addressed any criticism as a deliberate or reckless breach of the duty is always a sufficient ground to seek a total avoidance of contract.<sup>456</sup>

In the second situation, where the breach is neither deliberate nor reckless, the insurer is entitled to avoid the contract if the insurer would not have entered into the insurance contract, but for the breach that was committed by the assured, although the obtained premium would have been returned to the assured. This approach restricts the application of the remedy of avoidance in the situations where the breaches have induced the insurers to enter into contracts which he or she would not have entered into. It is submitted that this approach is fair and proportionate to both parties to an insurance contract.

The second remedy for the insurer is an alteration of the contractual terms of a non-deliberate or reckless breach of the duty. In the situation where, but for the breach, the insurer would have entered into the insurance contract on different terms, the court could grant this second remedy, the effect of which would be that the altered terms would be treated as if they had been written into the contract in the first place. It is noteworthy that this remedy is applicable to terms such as insurance warranties, terms that are relevant to exemption and insurance excess.<sup>457</sup> Since the operation of this remedy is still unknown, the author does not recommend that legislators in

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<sup>455</sup> The Insurance Act 2015, schedule one, paragraph two

<sup>456</sup> It includes fraudulent behaviour, see Explanatory notes to the Insurance Bill 2015 (n29) para 82

<sup>457</sup> Law Commission (n4) para 11.67

Hong Kong impose this new remedy, until there is future case law in England and Wales that clarifies the application of this new remedy.

The third remedy is that if the insurer had entered into the insurance contract with a higher premium, then the insurer would be entitled to reduce the claim proportionately. There are two formulas for the proportionate remedies. The first formula applies to cases where variations of terms are not involved. The formula is as follows:

$$X = \frac{\text{Premium actually charged}}{\text{Higher premium}} \times 100$$

In this formula, X is the percentage that the claim shall be reduced after the breach of duty.

The second formula is slightly more complex. It applies to cases which involve a variation of terms and the formula is as follows:

$$Y = \frac{\text{Total premium actually charged}}{P} \times 100$$

In this formula, Y is the percentage that the claim shall be reduced after the breach of the duty. P is a variance. In the case, where the insurer increases the premium, P is the total premium that would be charged.<sup>458</sup> In the case where the insurer would has not agreed to the variation on any terms, the insurer may treat the contract as if the variation had never been made. In this regard, P is the original premium.<sup>459</sup> P represents the original premium, no matter whether the insurer increases, decreases or maintains it at its current level.<sup>460</sup>

The new remedy of proportionate reduction of claim has apparently improved the unfair situation that existed before the enactment of the IA 2015, where the remedy of avoidance was the only result of utmost good faith cases. Nevertheless, it is submitted that this new remedy still fails to address the problem of disproportionality. There are two reasons to support this proposition.

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<sup>458</sup> The Insurance Act 2015, sschedule 1, para 11(3)(a)

<sup>459</sup> The Insurance Act 2015, schedule 1 para 11(3)(b)

<sup>460</sup> *ibid* schedule 1 para 11(3)(c)



The first reason is that it is logically unsound to reduce the claim amount of the assured while the loss of the insurer, in an utmost good faith case, is actually the loss of charging an additional premium. The other two remedies, namely avoidance of contract and alteration of contractual term(s), are logical in order to take retrospective effect to the loss of the insurer if the presentation was fairly made. In the situation where the insurer should not have underwritten the risk, the remedy of avoidance allows the insurer to avoid the contract. In the situation where, but for the breach, “the insurer would have entered into the contract on different terms”, the proportionate remedy provides that “the contract is to be treated as if it had been entered into on those different terms.”<sup>461</sup> The illogical part is, in the situation where the insurer should have charged a higher premium, the remedy becomes a reduction of claim rather than compensation for an additional premium that the insurer would have charged. This illogical approach is unfair to the assured. Indeed, the leading scholar of Hong Kong insurance law, Dr Poomintr Sooksripaisarnkit, has illustrated the problem with the example below:

Assuming the premium charged was HK\$1,000. The higher premium which should have been charged is HK\$2,000. Therefore, according to the formula, the reduced claim ratio is 50%. Suppose the claim is in the amount of HK\$20,000, due to the careless breach of the duty, the insurer will only pay HK\$10,000. So, the assured’s net loss is HK\$10,000. The point is the actual loss of the insurer was the loss of obtaining a higher premium, which is HK\$1,000 in this case. But, for the loss of this HK\$1,000, the assured has to suffer HK\$10,000 loss.<sup>462</sup>

Dr Sooksripaisarnkit concluded that the new remedy serves to punish the assured, rather than compensating the loss of the insurer.<sup>463</sup> The question is whether there is a justifiable reason to punish the assured in the situation where the breach is committed unintentionally. It is understandable that by imposing a remedy with an element of punishment, it can achieve the purpose of discouraging an intentional wrongdoer to present the risk unfairly. Nevertheless, there are two reasons to support the notion that this approach does not work for the duty of utmost good faith/fair presentation. Firstly, it is submitted that in accordance with the recent

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<sup>461</sup> *ibid* schedule 1 para 5

<sup>462</sup> Poomintr Sooksripaisarnkit and Felix Chin Kiu Cheung, ‘The Consumer Insurance (Disclosure and Representations) Act 2012: Not a Model for Hong Kong!’, *The Asian Business Lawyer*, vol.18:131, p. 152. This passage regards the consumer insurance act 2012 but the proportionate remedy is identical to the one in Insurance Act 2015.

<sup>463</sup> *ibid*

trends in case law, the most draconian approach, namely the single remedy of avoidance, has failed to discourage wrongdoers. After 1996, according to the Lloyd's Insurance and Reinsurance Law Reports, there have been 97 insurance law cases that have mentioned the term "utmost good faith".<sup>464</sup> Among these 97 cases, there were 37 cases in which the intention of the alleged breach was not examined.<sup>465</sup> In the remaining 60 cases, there are 34 cases that documented that the alleged breach involved intentional conduct to conceal information or present false information to the insurer. In other words, under the MIA 1906, which advocated the most draconian remedy, over half of the cases involved an intentional breach of the duty, which suggests that the method of discouraging wrongdoers by imposing punishment may not be as effective as hoped.

The other problem of imposing a punishment on the wrongdoer in utmost good faith/fair presentation cases lies in the remaining 26 cases, the alleged breach of which was unintentional. Since the alleged breach was unintentional, the punishment clearly did not discourage the wrongdoer, because that was not the innocent assured's intention to commit the breach. The idea of discouraging the wrongdoer by imposing a measure of punishment is only useful for discouraging those who intentionally present the risk unfairly. In this regard, it is submitted that the punishment element in the new remedy, which is the proportionate reduction of claim under the IA 2015, has little significance, and worse still, it causes a disproportionate result for the innocent wrongdoer, which is unfavourable for ensuring fairness for the parties to an insurance contract.

In addition, the other reason why the new remedy fails to address proportionality is that even if the formula is logically sound, it is still mathematically illogical. The formula, by drawing a simple ratio equation between the premium and the claim, has presumed that there is a positive and linear correlation between the premium and the loss. However, in most cases, there is no evidence to suggest that there such a correlation exists. Indeed, there is no one-size-fits-all formula to calculate the amount of premium, as the art of underwriting is subject to the experience of the underwriter, and the approach of which is apparently subjective. On the other

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<sup>464</sup> Please refer to annex 2 for the table of summary of the cases.

<sup>465</sup> The reason is that the breach of utmost good faith is a matter of conduct rather than mentality, therefore in most cases it does not require the judge to examine the intention of the wrongdoer.

hand, the claim amount is also a factor that can be calculated differently by different loss adjusters. It is simply mathematically illogical to link two variants when there is no established correlation that can be proved between the two variants.

Furthermore, under an insurance policy, it is not only the premium and the claim amount that can indicate the correlation between the two variants, but also other factors can be quantified and act as indicators of the correlation between the premium and the claim, namely the excess of the insurance and the claim limit of the policy. Without considering all the quantified factors of an insurance policy, it is highly unlikely that the formula can achieve proportionality. Thus, it is submitted that this formula has undermined the art of underwriting, or have made it illogical to follow. Therefore, it is submitted that the reform of the remedies in Hong Kong should not strictly follow the IA 2015, and the formulation of the reform will be suggested in the next section.

## **B. Formulating a reform to solve the problem of disproportionality**

### **i. The problem of disproportionality in relation to the remedy**

It is submitted that to solve the problem of the remedies of utmost good faith/fair presentation, it is necessary to observe how proportionality can be achieved in utmost good faith/fair presentation cases. The old approach, which is the single remedy approach under the MIA 1906, is draconian. The approach disregards the matter of proportionality, and therefore has resulted in the innocent assured suffering from this unfair approach ever since the enactment of the duty. In addition to the trend of case law in England and Wales, the author also gathered 23 cases from Hong Kong which mentioned the term “utmost good faith” in order to analyse the case trend in Hong Kong.<sup>466</sup> Among the 23 cases, there are 14 cases in which the intention of the alleged breach was not identified. In the remaining 9 cases, there are 8 cases that indicate that the alleged breach was unintentional, which suggests that the problem of disproportionality affects the majority of Hong Kong cases, and therefore, there is a higher demand for Hong Kong law to address the problem of disproportionality.

The other approach, which is the new remedies under the IA 2015, is a better option that can be partly followed for Hong Kong law reform. In particular, the limitation of the application of the

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<sup>466</sup> Please refer to Annex 3 for the table of case summary for the 23 Hong Kong cases.

remedy of avoidance in the specified situations can be strictly followed in Hong Kong. Nevertheless, the other two remedies are problematic, and it is suggested that they should be examined with extra caution before adopting these remedies in Hong Kong law.

For the remedy of the alteration of terms, it is submitted that the operation of this remedy is still unknown, and it may provide a new alternative for the insurer to escape from the liability of paying a claim. Among the new remedies, the remedy of avoidance is about the decision as to whether the risk is worth underwriting or not, and the proportionate reduction of claim is about the calculation of the premium. These matters are less variable, and it is unlikely that the assured would be able to have any influence on these matters. The contractual term, however, is another matter. It is more likely that the agreement of contractual terms may involve frequent interaction between the insurer and the assured, and whether a term is added to the policy is not the sole decision of the insurer, but must also be agreed by the assured. If the assured insists on not adding the term into the contract, the insurer may not insist on proposing the term based on other factors, for instance, the commercial relationship between the parties. Alternatively, if the insurer insists on a contractual term, but the assured does not agree, then the assured is free to leave the bargain and contract with another insurer. There are too many variables that can be involved in the process of terms negotiation, and the potential problem of the operation of this remedy is that the court will only consider the evidence from the insurer's point of view, which means that it would be another one-sided remedy in favour of the insurer. Therefore, it is suggested that unless future cases provide a clearer explanation of this remedy, it is submitted that at this stage, there is no positive reason for Hong Kong to impose this remedy in the legislation.

The most problematic part regards the remedy of proportionate reduction of claim. As identified in section II(A) of this chapter, the purposes of imposing a new remedy should aim to maintain accessibility and proportionality. The new remedy for the reduction of claim is more complicated than the original single remedy approach. Thus, it is submitted that there is no reason to follow the new remedy, which has failed to achieve any one of the purposes of the legal reform.

Alternatively, it is submitted that the purposes of legal reform can be achieved by formulating a new remedy, which compensates the insurer in the form of charging an additional premium. The

benefits are that there is no complicated calculation involved for an additional charge of premium, and it would ensure the proportionality between the parties. However, it is noteworthy that this approach was rejected by the Law Commission for the following reason:

Insureds are not given a right to pay the extra premium that the insurer would have charged in order to retain cover. This would under-compensate the insurer, who would thereby be forced to cover the risk after it had materialised, despite not having been given sufficient information to gauge accurately the degree of likelihood of it materialising or its extent. It would be open to insurers to decide to accept the higher premium as part of a commercial settlement.<sup>467</sup>

The logic of this reasoning is unsound. The purpose of the remedies is to take retrospective effect to what should have been done if the presentation had been fairly made. If the insurer considers that the risk is too high after the disclosure and presentation has been fairly made, he can certainly choose to refuse to underwrite the risk, the result of which is the same as an avoidance of contract. By charging an additional premium, the insurer itself has already been provided with another chance to make a fair assessment of the risk. There is no issue of under-compensation, and it is therefore logical to propose a remedy of reimbursing the additional premium to achieve proportionality in the case of a breach of the duty.

It may be argued that since the element of punishment has been removed from this additional premium remedy, it may encourage the assured to present the risk unfairly, as the worst-case scenario for the wrongdoer is providing an additional premium to the insurer. In other words, the said additional premium remedy encourages the assured to present the risk unfairly. Nevertheless, under the suggested reform proposal, the insurer is always entitled to avoid the contract in the situation where the assured commits the breach deliberately. The remedy of charging an additional premium is only available to those who innocently misrepresent the risk, and therefore it will not encourage the assured in the market to present the risk unfairly, as the remedy of avoidance is still a very powerful measure to discourage the intentional wrongdoer.

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<sup>467</sup> Law Commission (n4) para 11.72

Another potential problem of the proposed reform is that the new remedy of charging an additional premium may encourage the assured to present the risk carelessly, but without a fraudulent or reckless mind or conduct, and the insurer may have to make an extra effort to ensure the accuracy of the information that is submitted by the assured. This approach would add a heavy burden to the insurer. However, this approach may be reasonable for two reasons. Firstly, the insurer is more familiar with the procedures of underwriting. Secondly, and most importantly, the insurer is well paid for their job. Indeed, cross checking the information that is submitted by client or customer is normal practice in a customer driven industry, and there is no reason that the insurance industry, especially the case in Hong Kong, can be exempted from this basic practice of the commercial world.

## **ii. The solution**

Based on the above analysis, it is submitted that the reform should not only include measures that discourage the fraudulent wrongdoer, but also measures that protect the innocent wrongdoer. The remedy of avoidance has always served the purpose of discouraging the fraudulent wrongdoer, but there is no remedy to protect the innocent wrongdoers, and the remedy of charging an additional premium is adequate to serve this purpose. It is therefore suggested that the reform proposal be as follows. For section 18 of the MIO, section 18(1) should be amended as follows:

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 be entitled to seek one of the following remedies:

- (a) The remedy of avoidance if, but for the breach, the insurer would not have entered into the contract of insurance at all, or
- (b) Additional premium if, but for the breach, the insurer would have entered into the contract with a higher premium.

Similarly, for section 20 of the MIO, section 20(1) will be amended as follows:

Every material representation made by the assured or his agent to the insurer during the negotiations for the contract, and before the contract is concluded, must be true. If it be untrue, the insurer may be entitled to seek one of the following remedies:

- (a) The remedy of avoidance if, but for the breach, the insurer would not have entered into the contract of insurance at all, or
- (b) An additional premium if, but for the breach, the insurer would have entered into the contract with a higher premium.

This proposal addresses the two problems that were identified in section II(A). Firstly, by dividing the remedies into two different categories, it is suggested that the problem of disproportionality among the wrongdoers no longer exists. The proposal ensures that the most appropriate remedy is granted in accordance with the seriousness of the breach by the assured. Secondly, by replacing the remedy of proportionate reduction of claim with the remedy of an additional premium, the proposal ensures that the problem of disproportionality between the insurer and the assured no longer exists. The premium, in any case, should be the only form of benefit that the insurer is entitled to claim under an insurance contract, and there is no reason to allow the insurer to reduce the amount of claim when the loss of the insurer is no more than the additional premium.

### **III. Conclusion**

The current law in relation to the duty of utmost good faith is problematic, because section 17 has not clearly identified the scope of the duty of utmost good faith. Sir Mackenzie Chalmers referred to section 17 as a section of general principle, and section 18, 19, 20 as not being “exhaustive”. In addition, although the IA 2015 has reformed the assured’s duty of utmost good faith by imposing the new duty of fair presentation, the insurer’s duty of utmost good faith has not been clearly identified by both the judiciary and legislature, and therefore Hong Kong should not follow the English law approach.

In relation to the problem of disproportionality, it is submitted that the three new remedies for the duty of fair presentation, under the IA 2015, have made the situation fairer. The remedy of avoidance is only applicable to cases where, but for the breach, the insurer should not have entered into the contract, and this remedy should be followed by the legislators in Hong Kong.

For the second remedy of alteration of terms, although the practical application of such a remedy remains in doubt, the legislators in Hong Kong may still consider introducing this remedy to the MIO. Nevertheless, since this remedy may operate as another one-sided remedy in favour of the insurer, it is submitted that this remedy should not be included in the current reform proposal, unless there is a clarification from the English law on the operation and legal requirement of this remedy in the future.

The proportionate reduction of the claim is the most problematic remedy. Although the said remedy may be a better option in comparison to the remedy of avoidance under the MIA 1906, it is still disproportionate and unfair to the assured. For this remedy, the author suggests that the legislators in Hong Kong should consider introducing a completely new remedy of charging an additional premium to achieve proportionality.

To conclude, it is submitted under English law, the duty of utmost good faith, although closely related to the duty of fair presentation, can now be viewed as a separate duty from the duty of fair presentation. It is suggested that Hong Kong could follow this approach to separate the two duties, but the legislators in Hong Kong should go further to rectify any unfair situations, as the IA 2015 has failed to do so. In any event, the author submits that the remedies of breaching the duty of utmost good faith are in need of reform, and the detailed reform proposal will be provided in chapter 6 of this thesis.



## **Chapter 5 The Agent's Duty Of Disclosure Under Utmost Good Faith/Fair Presentation**

This chapter regards the agent's duty of utmost good faith/fair presentation. In the past, as far as utmost good faith is concerned, the agent owed a duty not to misrepresent and a duty of disclosure under the MIA 1906. The agent's duty not to misrepresent was governed by section 20 of the MIA 1906, which was the same as the assured's duty not to misrepresent, and thus both duties were highly identical to each other. The analysis in chapter 3 of this thesis, which is about the assured's duty not to misrepresent, is applicable to the agent's duty not to misrepresent, and therefore, this chapter will not analyse the said duty again from the agent's perspective.

The problematic aspect of the agent's duty of utmost good faith/fair presentation lies in the agent's duty of disclosure. Under the MIO, section 18(1) stipulates that the assured is obligated to disclose what he or she deems to know in the ordinary course of business, which includes the knowledge that the agent is imputed or attributed to the assured. In addition, section 19 stipulates that the agent owes an independent duty to disclose material knowledge, which he knows or ought to know, to the insurer. If the agent fails to comply with the duty, the insurer is entitled to avoid the insurance contract against the assured. Nevertheless, the legislation does not provide clear answers to the questions of who is subject to the duty, and what is disclosable under the duty. Recent cases have also revealed that these unanswered questions have caused inconsistencies in judgments and have affected the certainty and accessibility of this area of law.

In England and Wales, the IA 2015 is enacted to solve the problems under the agent's duty of disclosure. Section 19 of the MIA 1906 is repealed, and the agent no longer owes an independent duty of disclosure. The assured is now required to conduct a reasonable search for the material knowledge that is possessed by the agent at the pre-contractual stage. New provisions are also imposed to address problems that are related to the Hampshire Land principle and confidentiality. However, it is arguable that the IA 2015 widens the scope of the agent's duty of disclosure. The new duty of reasonable search may add an extra burden on the assured to search for information that is out of his or her reach. Furthermore, the new exclusion

of confidential information is not clearly defined in the IA 2015, and it may further complicate the new duty of fair presentation. In this regard, it is submitted that the IA 2015 may not be a good model for Hong Kong law reform, and thus it may be necessary to formulate a new agent's duty of disclosure.

This chapter will be divided into two parts. The first part regards the identification of the problems related to the agent's duty of disclosure under the MIO, MIA 1906 and the IA 2015. To identify the problems, a thorough analysis of the modern cases and the relevant sections of the IA 2015 will be provided. The second part regards the reform proposal of the agent's duty of disclosure in Hong Kong. The reform will introduce a legislative change in relation to section 18 and 19 of the MIO.

#### **I. The agent's duty of disclosure: controversies**

This section regards the problems related to the agent's duty of disclosure. The problems of the MIO and the MIA 1906 will be identified through a case trend analysis of modern cases. However, the same approach cannot be adopted for the identification of the problems of the IA 2015, as there is currently no case law available. Therefore, the potential problems of the IA 2015 will be examined based on the language of the relevant sections and the commentaries that are provided by the Law Commission, scholars, practitioners and judges.

##### **A. The MIO does not clearly define which agent is subject to the duty, and the Hampshire Land principle is absent from the Legislation**

Under the MIO, the only section that expressly mentions the term "agent" is section 19. Section 19 requires the agent, who effects the insurance contract, to disclose material knowledge to the insurer. However, the said agent is not the only type of agent that is subject to the duty of disclosure. According to the *Chitty on Contract*, there were three types of agent that were subject to the duty of disclosure under the MIA 1906.<sup>468</sup> The first type was the agent who effected the insurance contract, and was referred to as the "agent to insure". The second type was the "agent to know", and the knowledge of the said agent was imputed to the assured, because the assured relied on the said agent's knowledge to manage the insured risk. The third

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<sup>468</sup> Beale (n300) para 42-035

type was the agent who was in a predominant position, and the knowledge of the said agent can be regarded as the knowledge of the assured. It is noteworthy that the duty of the “agent to insure”, which was governed by section 19, was different from the duties of the “agent to know” and the “agent in a predominant position”, which were governed by section 18. The difference was that section 18 applied to the agent whose knowledge was imputed to the assured, but section 19 applied to the agent whose knowledge was independent of the assured.<sup>469</sup> While the language of section 19 clearly revealed the existence of the “agent to insure”, one may not be able to observe the existence of the “agent to know” or the “agent in a predominant position” by reading section 18, which suggested that the language of section 18 did not fully reflect the actual scope of the agent’s duty of disclosure. It is arguable that the scope could be observed through case law, nevertheless, it is submitted that case law also created some confusion with regard to the agent’s duty of disclosure. In *PCW Syndicates v. PCW Reinsurers*,<sup>470</sup> the case concerned a reinsurance contract, and the agent in dispute was the managing agent of the reassured. The agent was responsible for the arrangement of the insurance contract of the reassured, but the agent was not responsible for the arrangement of the reinsurance, and the agent never directly communicated with the reinsurers. The reinsurers contended that the agent failed to disclose the material knowledge, namely a moral hazard that involved the agent fraudulently diverting the premium income of the reassured to the agent’s own account, and thus, the reinsurers pleaded that they were entitled to avoid the contract. Saville L.J. held that section 19 was only applicable to the “agent to insure”, who directly communicated and arranged the insurance with the insurer. Accordingly, the intermediate agent, who merely acted as a messenger and had no direct communication with the insurer, was not subject to the duty of disclosure.<sup>471</sup>

This judgment, however, was seemingly contradictory to *Blackburn, Low & Co v Vigors*<sup>472</sup> and *Blackburn, Low & Co. v. Haslam*,<sup>473</sup> which were referred to as model cases of section 19 of the MIA 1906.<sup>474</sup> *Blackburn, Low & Co v Vigors*<sup>475</sup> involved three agents and two reinsurance

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<sup>469</sup> *PCW Syndicates* (n71) 379

<sup>470</sup> *ibid*

<sup>471</sup> *ibid* 380-381

<sup>472</sup> (1887) 12 App Cas 531

<sup>473</sup> (1888) 21 Q.B.D.144

<sup>474</sup> Chalmers and Ivamy (n393) page 32-33

<sup>475</sup> *Blackburn, Low & Co v Vigors* (n477)

policies for a steamship. The first agent, normally responsible for arranging the reinsurance for the reassured, was Rose, Murison & Thomson, and was the Glasgow broker of the reassured. The second agent was Roxburgh, Curry & Co, and the London broker of the reassured. Before the arrangement of the first reinsurance contract, the reassured tried to arrange a reinsurance through the second agent, but the attempt failed, as the terms were not agreed between the parties.

The third agent was Rose, Thomson, Young & Co, who was the London agent of the first agent. It was the third agent who was responsible for the arrangement of the first reinsurance. Before the arrangement of the first reinsurance, the first agent, who had not directly dealt with the reinsurer, was aware that the insured ship was lost, but this material information was not communicated to the reassured or other agents.<sup>476</sup> Later, the reassured went back to the second agent, and the second agent effected the second reinsurance for the ship. The issue, in this case, was whether the reinsurer was entitled to avoid the second reinsurance contract. The House of Lords held that the second agent did not possess the material information. The second reinsurance contract was arranged by the second agent, but the said agent was not in the position to manage the steamship, and therefore the said agent was not in the position to know that the insured ship was lost. As a result, the reinsurer was not entitled to avoid the contract based on non-disclosure.<sup>477</sup> The House of Lords also held that, first, the operation of the agent's duty of disclosure was not an imputation of knowledge from the agent to the principal. Second, there was no legal obligation for the first agent to communicate the material information to the reassured.<sup>478</sup>

Later, in *Blackburn, Low & Co. v. Haslam*,<sup>479</sup> it was held that the first reinsurance could be avoided, due to the concealment of fact by the first agent. It is noteworthy that in this case, the third agent, who was the party that affected the first reinsurance, was considered to be a separate legal entity which was independent from the first agent.<sup>480</sup> The reason was that:

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<sup>476</sup> For the purpose of clarification, the third agent was the placing broker of the first reinsurance contract and the second agent was the placing broker of the second reinsurance contract.

<sup>477</sup> *Blackburn, Low & Co v Vigors* (n477) 540

<sup>478</sup> *ibid* 543

<sup>479</sup> *Blackburn Low& Co. v. Haslam* (n478)

<sup>480</sup> *ibid* 153

...because in almost all cases where a policy has been held to be avoided by reasons of concealment, the concealment occurs some time before the actual policy is signed. It is the negotiation that is tainted, and the contract is void because it is founded upon the negotiation, and through however many hands the offer of an insurance may pass, if there be a concealment by the assured or his agent, the policy is avoided.<sup>481</sup>

The court, in this case, held that this judgment was not contradictory to the House of Lords judgment in *Blackburn, Low & Co v Vigors*,<sup>482</sup> because the focus of the latter case was on the second reinsurance contract. Moreover, the information that was obtained for the arrangement of the first reinsurance was ceased, as the said information was not intended to be known for the arrangement of the second reinsurance. In other words, the duty of disclosure under the first reinsurance contract was examined independently from the duty of disclosure under the second reinsurance contract, and therefore the knowledge of the first agent was not deemed to be known by the second agent.

In the *PCW Syndicates* case,<sup>483</sup> Saville L.J. further explained that in *Blackburn, Low & Co. v. Haslam*,<sup>484</sup> the “agent to insure”, namely the third agent, was deemed to know every circumstance that ought to be communicated to him or her. In this regard, the agent, who was not the placing broker but possessed the material information, should have communicated the material information to the “agent to insure”. Saville L.J. concluded that the reinsurance contract in *Blackburn, Low & Co. v. Haslam*<sup>485</sup> was avoided regardless of whether the agent, who possessed the material information, was the “agent to insure” or “agent to know”.<sup>486</sup>

However, if Saville L.J.’s judgment that the “agent to insure” should have known any information that ought to have been communicated to him or her by all the agents in a chain of insurance was correct, then it is difficult to understand why the second agent, as the “agent to insure” of the second reinsurance, was not deemed to know the material information which was held by

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<sup>481</sup> *ibid* 152 - 153

<sup>482</sup> *Blackburn, Low & Co v Vigors* (n477)

<sup>483</sup> *PCW Syndicates* (n71)

<sup>484</sup> *Blackburn Low & Co. v. Haslam* (n478)

<sup>485</sup> *ibid*

<sup>486</sup> *PCW Syndicates* (n71) 383. It is noteworthy that since the counsel in this *PCW Syndicates* case did not seek to avoid the contract based on section 18, the issue of whether the managing agent of the reassured could be regarded as an “agent to know” or an “agent in predominant position” was not examined.

the first agent. The surrounding factors of the two reinsurance contracts, namely the reassured, the risk, the periods of reinsurance and the premiums, were almost identical to each other, and there was no reason to exclude the first agent from the chain of insurance under the second reinsurance contract in *Blackburn, Low & Co v Vigors*.<sup>487</sup> It may be argued that in *Blackburn, Low & Co. v. Haslam*,<sup>488</sup> the third agent effected the first reinsurance contract based on the negotiation that was initiated by the first agent, and therefore the first agent was obliged to communicate the material information to the third agent. Nevertheless, the above-mentioned judgments illustrated that the agent's duty of disclosure could be particularly complicated when there were multiple agents involved in a chain of insurance. Apparently, section 19 of the MIA 1906 did not provide detailed guidance about which agent should have been included in the chain of insurance, and what knowledge should have been communicated to the "agent to insure". Thus, it caused hardships for the reader of the legislation to understand and comply with the duty.

The said problem can be further elaborated on by a case trend analysis of the modern cases. In the Lloyd's Insurance and Reinsurance Law Report, there were nine English cases that mentioned the terms "section 19" and "good faith" between 1995 to 2017.<sup>489</sup> There were three cases, namely *Henderson v Merrett Syndicates Ltd*,<sup>490</sup> *International Lottery Management Ltd v Dumas and Others*<sup>491</sup> and *Dalecroft Properties Ltd v Underwriter*<sup>492</sup> that did not examine the issue of the agent's duty of disclosure in relation to utmost good faith. Apart from these three cases, *Manifest Shipping Co Ltd v Uni-Polaris Shipping Co Ltd and Ors (the Star Sea)*<sup>493</sup> was a case that mainly focused on the analysis of the post-contractual duty of utmost good faith. In that judgment, the agent's duty of disclosure was only mentioned to support Lord Scott's

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<sup>487</sup> *Blackburn, Low & Co v Vigors* (n477)

<sup>488</sup> *Blackburn Low & Co. v. Haslam* (n478)

<sup>489</sup> The period was set based on two reasons. Firstly, the position of agent's duty of disclosure, before the *PCW Syndicates* case, was summarised in the *PCW Syndicates* case already and thus, there was no necessity to provide another analysis of the cases before the decision of the *PCW Syndicates* case. Secondly, the landmark case *Pan Atlantic* was reported in 1995, where the inducement test was formally introduced in addition to the materiality test in utmost good faith cases, and these tests were also applicable to cases of agent's duty of disclosure. In this regard, it is submitted that case authorities after 1995 were more significant to reflect the modern development of the agent's duty of disclosure. Nevertheless, the case trend analysis will also examine case authorities before 1995, but on a selective basis. It is noteworthy that the case trend analysis only aims to indicate a general trend among significant cases on a selective basis, and it is not an analyse of all agent's duty of disclosure cases in England and Wales, as there were cases that were settled out of court, and there were also cases that were not reported in the Lloyd's Insurance and Reinsurance Law Report.

<sup>490</sup> [1996] 5 Lloyd's Rep IR 279

<sup>491</sup> [2002] 1 Lloyd's Rep IR 237

<sup>492</sup> [2017] 1 Lloyd's Rep IR 511

<sup>493</sup> *The Star Sea* (n450)

decision that the pre-contractual and post-contractual duties of utmost good faith were different from each other, and both of the duties could have been breached by the assured or the agent with an honest belief.<sup>494</sup>

For the remaining four cases, the first case, *Group Josi v Walbrook Insurance Co. Ltd. and Others*,<sup>495</sup> concerned a reinsurance contract. The reinsurer sought to avoid the contract on the grounds of fraudulent non-disclosure by the agent.<sup>496</sup> The reinsurer argued that the knowledge that was deemed to be known by the reassured should not have been limited to the knowledge that was obtained by the reassured in the ordinary course of business. Nevertheless, Saville L.J. rejected this argument because section 18 clearly stated that the reassured only deemed to know information that was obtained in the ordinary course of business. The reinsurer's argument, therefore, was simply contradictory to section 18 of the MIA 1906, and there was no case authority supporting the reinsurer's argument.<sup>497</sup> Saville L.J. also held that since the reinsurance contract was effected by the agent and the reassured was not aware of the concealed knowledge, the breach would have certainly fallen within the jurisdiction of section 19, and there was no valid ground to support the argument of the reinsurer.<sup>498</sup> As a result, the judgment of *PCW Syndicates*<sup>499</sup> was strictly followed in this case.<sup>500</sup>

The authoritative textbook, *Arnould: Law of Marine Insurance and Average*, suggested that Saville L.J.'s judgment in the *Group Josi* case<sup>501</sup> implied that there were only two types of agent, namely the "agent to know" and the "agent to insure", that were subject to the duty of disclosure, and the "agent in a predominant position" did not exist after the judgment of the *Group Josi*.<sup>502</sup> This observation was noted in another authoritative textbook *MacGillivray on Insurance Law*,<sup>503</sup> but the said observation was not further elaborated on. Clearly, the language of sections 18 and 19 caused confusion as to which agent was subject to the duty of disclosure and presented potential difficulties for the reader of the legislation to understand and comply with the duty.

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<sup>494</sup> *ibid* [94]

<sup>495</sup> *Group Josi* (n57)

<sup>496</sup> *ibid* 94

<sup>497</sup> *ibid* 100

<sup>498</sup> *ibid* 100

<sup>499</sup> *PCW Syndicates* (n71)

<sup>500</sup> *Group Josi* (n57) 101

<sup>501</sup> *ibid*

<sup>502</sup> Gilman, Templeman, Blanchard, Hopkins and Hart (n38) Para 16-10

<sup>503</sup> Birds, Lynch and Paul (n39) Para 17-015 footnote 50

The second case, *HIH Casualty and General Ins Ltd v Chase Manhattan Bank*,<sup>504</sup> concerned an insurance contract of time variable contingency for the repayment of financing to produce five movies. The insurer pleaded that the assured had breached the duty of utmost good faith through his broker who had concealed and misrepresented the terms and claims records of the previous insurance contract. The insurer sought to avoid the contract against the assured or alternatively, claim damages against both the assured and the insurance broker. With respect to the agent's duty of disclosure, the *PCW Syndicate* case<sup>505</sup> was followed; Saville L.J.'s judgment was referred to as the explanation of the said duty.<sup>506</sup> This case emphasised that the section 19 duty was independent from the assured's duty of disclosure, and as a result, an exclusion clause in relation to the assured's duty was not applicable to the agent's duty.<sup>507</sup> It was also held that the insurer was not entitled to seek damages against the agent, because such a remedy was not available for breach of the duty of utmost good faith.<sup>508</sup> This case was a clear-cut case that fell within the ambit of section 19, and it did not examine the agent's duty from the perspective of section 18. Nevertheless, it identified the problem that the independent duty of disclosure under section 19 could be confusing. On the one hand, the *HIH Casualty* case<sup>509</sup> suggested that an exclusion of the assured's duty of disclosure did not amount to an exclusion of the agent's duty of disclosure. On the other hand, the *HIH Casualty* case<sup>510</sup> also suggested that although the agent's duty of disclosure was held to be an independent duty, there was no remedy for the insurer to seek against the agent. The judgment raised the issue as to whether it was appropriate to treat the agent's duty of disclosure as an independent duty, as the remedy of the said independent duty was still dependent on the remedy against the assured, but not the agent.

The third case in this case trend analysis is *ERC Frankona Reinsurance v American National Insurance*.<sup>511</sup> In this case, the reinsurer sought to avoid the reinsurance contract based on the

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<sup>504</sup> *HIH Casualty* (n346)

<sup>505</sup> *PCW Syndicates* (n71)

<sup>506</sup> *HIH Casualty* (n346) [8], [50], [53] and [54]

<sup>507</sup> *ibid* [54]

<sup>508</sup> *ibid* [75]. The agent, however, may have been liable for damages under the Misrepresentation Act 1967, but it was a problem of a different statutory, and this chapter only considers the agent's duty of disclosure under the MIA 1906.

<sup>509</sup> *ibid*

<sup>510</sup> *ibid*

<sup>511</sup> *ERC Frankona Reinsurance* (n65)



non-disclosure of conviction records of the chairman and chief operating officer of the underwriting agent. The underwriting agent, however, was not the placing broker of the reinsurance. Mr Justice Andrew Smith held that the reassured was aware of the conviction records of its agent, and therefore the reinsurer was entitled to avoid the contract.<sup>512</sup> Since it was a matter of fact that the reassured did possess the material knowledge, it was evident that the reassured had breached the duty of utmost good faith.

The *ERC Frankona Reinsurance* case<sup>513</sup> examined the three types of agent who were subject to the duty of disclosure in detail. For the “agent to insure”, Mr Justice Andrew Smith noticed that the approach of the *PCW Syndicate* case<sup>514</sup> was subject to criticism, but he had to follow the decision of this case, which suggested that in respect of section 19, the *PCW Syndicate case*<sup>515</sup> was followed one more time.<sup>516</sup>

For the “agent in a predominant position”, Mr Justice Andrew Smith also considered whether the agent in the *ERC Frankona Reinsurance case*<sup>517</sup> fell within this category. It is noteworthy that the judgment of the *Group Josi case*<sup>518</sup> was referred to in the *ERC Frankona Reinsurance case*,<sup>519</sup> but Mr Justice Andrew Smith did not address the question of whether the “agent in a predominant position” was subject to the duty of disclosure. This question was left unanswered after the *Group Josi case*.<sup>520</sup>

For the “agent to know”, Mr Justice Andrew Smith held that the relevant principle was formulated in the case *Proudfoot v Montefiore*.<sup>521</sup> In that case, the assured was a merchant who insured a cargo of madder. The agent was appointed by the assured “for a year to make purchases of madder on his account, and to ship and consign the cargoes to him.”<sup>522</sup> Prior to the effect of the insurance contract, the agent knew that there had already been a total loss of

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<sup>512</sup> *ibid* [110]- [112]

<sup>513</sup> *ibid*

<sup>514</sup> *PCW Syndicates* (n71)

<sup>515</sup> *PCW Syndicates* (n71)

<sup>516</sup> *ibid* [124]

<sup>517</sup> *ERC Frankona Reinsurance* (n65)

<sup>518</sup> *Group Josi* (n57)

<sup>519</sup> *ibid* [199]

<sup>520</sup> *ibid*

<sup>521</sup> (1867) 1 LR 2 QB 511

<sup>522</sup> *ibid* 518

cargo, but the agent did not communicate this information to the assured. The court held that the insurer was entitled to avoid the contract because the agent was bound to communicate the concealed information to his principal. It was held that:

...if an agent, whose duty it is, in the ordinary course of business, to communicate information to his principal as to the state of a ship and cargo, omits to discharge such duty, and the owner, in the absence of information as to any fact material to be communicated to the underwriter, effects an insurance, such insurance will be void, on the ground of concealment or misrepresentation.<sup>523</sup>

In the *ERC Frankona Reinsurance* case,<sup>524</sup> Mr Justice Andrew Smith relied on the above-cited judgment and held that it was not a case in which the reassured had to rely on the underwriting agent to manage the risk, and therefore the underwriting agent was not the “agent to know”.<sup>525</sup> The *ERC Frankona Reinsurance* case<sup>526</sup> summarised the judicial decisions in relation to the agent’s duty of disclosure. Nevertheless, it had not answered the key question, which had previously been raised since the *Group Josi* case,<sup>527</sup> of whether the “agent in a predominant position” was still subject to the duty of disclosure. Since Mr Justice Andrew Smith had examined the case under the category of the “agent in a predominant position”, it may be arguable that the judgment implied that this type of agent still existed under the duty of disclosure. However, the *ERC Frankona Reinsurance* case<sup>528</sup> suggested that there was no agreement on this matter, and it reflected the lack of certainty in the scope of the agent’s duty of disclosure.

The last modern authority for the case trend analysis is *Crane v Hannover*,<sup>529</sup> which concerned a reinsurance contract. In this case, the reinsurer pleaded that the duty of utmost good faith was breached by the reassured, due to non-disclosure and misrepresentation of the underwriting practice. Although this case did not concern the agent’s duty of disclosure, Mr Justice Walker summarised the current law of utmost good faith in this case, and with respect to section 19, the

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<sup>523</sup> *ibid* 521 - 522

<sup>524</sup> *ERC Frankona Reinsurance* (n65)

<sup>525</sup> *ibid* [132]

<sup>526</sup> *ibid*

<sup>527</sup> *Group Josi* (n57)

<sup>528</sup> *ERC Frankona Reinsurance* (n65)

<sup>529</sup> [2010] 1 Lloyd’s Rep IR 93

judgment highlighted the approach of the *PCW Syndicates* case<sup>530</sup>, specifically that only the agent who had effected the contract was subject to the duty of disclosure. The matters, that were known by the intermediate agent, may have been the knowledge that was deemed to be known by the agent to insure, and therefore may have had to have been disclosed under section 19.<sup>531</sup>

After examining all the relevant modern authorities, there are three common features of the agent's duty of disclosure that can be identified from the case trend analysis. The first feature is that the language of the legislation did not fully reflect the scope of the agent's duty. As suggested, it was section 18 and 19 of the MIA 1906 that regulated the agent's duty of disclosure. The problem with section 19, as identified in the *HIH Casualty* case,<sup>532</sup> was that the said independent agent's duty of disclosure did not provide an independent remedy for the insurer to seek against the agent. The issue of the remedy raised the question as to whether the agent's duty of disclosure should be treated as an independent duty under the legislation.

Furthermore, the language of section 18 appeared to be confusing, in the sense that the reader of the legislation was highly unlikely to be able to aware of the existence of the "agent to know" and the "agent in a predominant position". The modern case authorities have also suggested that there was a conflict of interpretations regarding whether the "agent in a predominant position" still existed after the *Group Josi* case.<sup>533</sup> The textbook *Arnould: Law of Marine Insurance and Average* was correct, and therefore it is reasonable to suggest that the said type of agent was no longer subject to the duty of disclosure, nevertheless, since there was no judicial decision that expressly excluded the said type of agent from the duty of disclosure, it is suggested that there was no definitive answer to this issue. The law reform of Hong Kong legislation should carefully consider this issue and provide a definitive answer for the scope of the duty in the reformed legislation.<sup>534</sup>

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<sup>530</sup> *PCW Syndicates* (n71)

<sup>531</sup> *Crane* (n534) Annex 1 [17]

<sup>532</sup> *HIH Casualty* (n346)

<sup>533</sup> *Group Josi* (n57)

<sup>534</sup> The suggested scope of the duty for the reform of Hong Kong law will be provided in section II(B) of this chapter.

It is noteworthy that under the general agency law, the assured, as a principal, can sue the agent if the agent breaches the duty of care. In general, the agent is required, with reasonable skill and care, to effect insurance policy, to advise the client any matter that is related to the policy, and to assist the assured to claim against the insurer under the insurance policy.<sup>535</sup> An insurance broker also owes a duty to advise its principal and client a wide range of issues including but not limited to types and coverages of insurance policy, issues that may affect the validity of insurance policy, onerous clauses of insurance policy and any matter that may affect the interests of the client.<sup>536</sup>

As far as the duty of disclosure is concerned, the broker owes an independent duty of care to explain the requirement of the duty of disclosure to the assured, and the broker also needs to carefully consider the knowledge that may be material to the risk in order to advise the assured to comply with the duty of disclosure.<sup>537</sup> In *Aiken v Stewart Wrightson*,<sup>538</sup> the concerned reinsurance contract was avoided by the reinsurer on the ground that several material information was not disclosed by the agent for the purpose of risk assessment, and hence, the reassured sued the agent for breach of contract and negligence. As alleged by the reassured, the broker was in breach of the duty of care, under both contract law and tort law, by making the wrong description of claims as well as non-disclosure of two major claims data. When considering the duty of care that the agent should have exercised, the court held that the agent should have disclosed everything that was material, maybe material or arguably material to the reinsurer.<sup>539</sup> Apparently, the scope of such a duty of care is wider than the one under section 19, where it only requires the agent to disclose material fact to the insurer.

In *O&R Jewellers Ltd v Terry*,<sup>540</sup> this case concerned a jewellers block policy, and there was a robbery happened in the insured shop. The assured tried to claim under the policy from the insurers, but the insurers rejected the claim on two grounds, one of which was that the assured did not disclose the criminal record of its director to the insurer. The assured therefore sued the

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<sup>535</sup> Christopher Walton; Stephen Todd; Philip Kramer; Daniel Edwards; Roger Cooper, *Charlesworth & Percy on Negligence* (14th Ed. Sweet & Maxwell, 2018) para 10-194

<sup>536</sup> Michael Jones; Anthony Dugdale; Mark Simpson, *Clerk & Lindsell on Torts* (22nd Ed. Sweet & Maxwell, 2018) para 10-246

<sup>537</sup> Eggers, Picken and Foss (n56) para 13.77

<sup>538</sup> *Aiken v Stewart Wrightson* [1995] 2 Lloyd's Rep. 618

<sup>539</sup> *ibid* 643

<sup>540</sup> *O&R Jewellers Ltd v Terry* [1999] Lloyd's Rep. I.R. 436

agent for the breach of duty to advise the assured to comply with the duty of disclosure. The court held that, since it was evident that the broker knew the conviction of the director of the assured company, the broker was obligated to disclose the conviction of the director to the insurer, or to advise the assured to disclose the said conviction to the insurer.<sup>541</sup> Since the broker failed to do so, it was held by the court that the assured was entitled to claim damages against the broker.<sup>542</sup>

The standard of care, in relation to the duty of utmost good faith, was examined in *Jones v Environcom*.<sup>543</sup> The assured sued the agent for a breach of duty of care on the ground that the agent failed to advise the assured to comply with the duty of disclosure, in particular, to disclose the use of plasma guns during the process of de-manufacturing fridges. The court held that in relation to the duty of disclosure, the broker had to fulfil four types of responsibility as follows:-

- (i) must advise his client of the duty to disclose all material circumstances;
- (ii) must explain the consequences of failing to do so;
- (iii) must indicate the sort of matters which ought to be disclosed as being material (or at least arguably material); and
- (iv) must take reasonable care to elicit matters which ought to be disclosed but which the client might not think it necessary to mention.<sup>544</sup>

The court held that the agent, in this case, had failed to warn the assured to comply with the duty, but the agent was not liable to pay for the loss that the assured had suffered from the avoidance of insurance contract. The reason was that even the agent had complied with the duty of care and advised the assured to comply with the duty of disclosure, the court found that it was still unlikely for the assured to disclose the use of plasma guns during the recycle work, as the assured did not realise that the use of plasmas guns was a material fact to the risk.<sup>545</sup>

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<sup>541</sup> Ibid 447-448

<sup>542</sup> Ibid 451

<sup>543</sup> *Jones v Environcom* [2010] 1 Lloyd's Rep IR 676

<sup>544</sup> Ibid [54]

<sup>545</sup> Ibid [73]

The *Jones* case<sup>546</sup> was followed by subsequent cases.<sup>547</sup> In *Synergy Health (UK) Ltd v CGU Insurance Plc (t/a Norwich Union)*,<sup>548</sup> the assured failed to inform the insurer, that the fire alarms were not installed in the insured premises and thus, the insurance contract was avoided on the ground of non-disclosure. The assured argued that the broker was in breach of the duty of care to advise the assured to comply with the duty of disclosure. The court considered the judgment of the *Jones* case<sup>549</sup> and held that it was evident that the broker had no knowledge about the fire alarms. There was also no indication that a competent broker would have doubted that the assured did not install the fire alarms in the premise and therefore, the broker was not liable for the breach of the duty of care.<sup>550</sup>

The above case authorities illustrated that the broker's duty of care was independent from the jurisdiction of section 19. Apparently, the scope of the duty of care is wider than the scope that is identified by section 19 of the MAI 1906/MIO, and the result of the breach of the duty of care is also different from the breach of the duty of disclosure under section 19. Thus, it is suggested that such a duty of care would exist regardless of whether the agent's duty of disclosure is an independent duty or not.

The second feature of the agent's duty of disclosure is that disputes of these cases often arose in the situations where there were multiple agents involved in a chain of insurance. This phenomenon could have been revealed by the fact that most of the agent's duty of disclosure cases concerned reinsurance contracts, where there would be at least two agents involved in a chain of insurance, namely, the placing broker of the reinsurance contract, and the underwriting agent of the insurance contract, the risk of which was covered by the reinsurance contract in dispute. In this kind of situation, the duty was confusing because the legislation had not provided clear guidance on how the agent, who was not the placing broker, was subject to the duty of disclosure. In particular, section 18 was unclear as to how the agent's knowledge was deemed to be imputed to the assured, and section 19 was also unclear as to how the agent's knowledge should have been communicated to the placing broker. Without clear guidance from

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<sup>546</sup> *ibid*

<sup>547</sup> See, for example, *Eurokey Recycling Ltd v Giles Insurance Brokers Ltd* [2015] Lloyd's Rep. I.R. 225 and *Involnert Management Inc v Aprilgrange Ltd* [2015] Lloyd's Rep. I.R. 661

<sup>548</sup> *Synergy Health (UK) Ltd v CGU Insurance Plc (t/a Norwich Union)* [2011] Lloyd's Rep. I.R. 500

<sup>549</sup> *Jones* (n548)

<sup>550</sup> *Synergy* (n553) [206], [229]

the legislation, it may be difficult to understand how the agent, who was not the placing broker, was subject to duty, and thus to comply with the duty. In this regard, it is submitted that the reform of Hong Kong legislation should provide clearer guidance on how an agent, who is not the placing broker, is subject to the duty of disclosure.

The last feature, regarding the agent's duty of disclosure, is that most of the cases involved a pleading of non-disclosure in relation to the fraud of the agent. This feature leads to another problem with the MIA 1906, which was the absence of the Hampshire Land principle from the legislation. In the *PCW Syndicates* case,<sup>551</sup> Saville L.J. held that section 19 required the agent to disclose material information to the insurer unless the information fell within the Hampshire Land principle, which was illustrated in the case of *Re Hampshire Land Company*.<sup>552</sup> In that case, the company directors incurred a debt on behalf of the company without obtaining ratification from the shareholders. The issue, in this case, was whether the company would have been deemed to know the director's fraud when the company was itself the victim of the fraud. The court held that the knowledge was not imputed to the company, and this principle was applied to the duty of the common agent and "...it would be impossible to infer that the duty, either of giving or receiving notice, will be fulfilled where the common agent is himself guilty of fraud."<sup>553</sup>

Thus, in the *PCW Syndicates* case,<sup>554</sup> Staughton L.J. held that for the ambit of section 19, the reinsurer could not have avoided the contract on the basis that the agent did not disclose anything that was related to its fraud or unlawful conduct.<sup>555</sup> As suggested by Staughton L.J., the principle extended to any case "where the principal's rights are affected if the agent does not make disclosure to a third party."<sup>556</sup>

According to the Lloyd's Insurance and Reinsurance Law Report, there were four cases that cited both the *Re Hampshire Land* case<sup>557</sup> and the *PCW Syndicates* case,<sup>558</sup> namely *Group Josi*

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<sup>551</sup> *PCW Syndicates* (n71)

<sup>552</sup> *ibid* 259

<sup>553</sup> *Re Hampshire Land* (n79) 749

<sup>554</sup> *PCW Syndicates* (n71)

<sup>555</sup> *ibid* 378

<sup>556</sup> *ibid* 379

<sup>557</sup> *Re Hampshire Land* (n79)

*Re v Walbrook Insurance Co. Ltd. and Others*,<sup>559</sup> *Kingscroft and Ors v Nissan Fire & Marine Insurance*,<sup>560</sup> *Sphere Drake Insurance v Euro International Underwriting Ltd*<sup>561</sup> and *ERC Frankona Reinsurance v American National Insurance*,<sup>562</sup> and none of these cases sought to challenge the decision of the *PCW Syndicates* case<sup>563</sup> in relation to the application of the Hampshire Land principle.<sup>564</sup> Among the four cases, the case *Sphere Drake Insurance v Euro International Underwriting Ltd*<sup>565</sup> cited both the *PCW Syndicates* case<sup>566</sup> and the *Re Hampshire Land* case,<sup>567</sup> but it did not analyse the Hampshire Land principle in detail. For the remaining three cases, the case fact of the *Group Josi* case<sup>568</sup> was examined in the previous case trend analysis. In that case, Saville L.J. held that both section 18 and 19 did not require the agent to disclose its own fraud to the insurer, and the assured was not deemed to know of the agent's fraud,<sup>569</sup> and the said judgment did not deviate from the *PCW Syndicates* case.<sup>570</sup>

In *Kingscroft and Ors v Nissan Fire & Marine Insurance*,<sup>571</sup> the reinsurer alleged that the underwriting agent had breached the duty of disclosure by concealing the fact that the paid premium was diverted by the agent for illegitimate purposes. There were seven directors of the agent's company in total, and the fraudulent act was committed by three of the directors. It was argued by the reinsurer that the knowledge of the remaining four directors, who were not involved in the fraudulent act, but must have been aware of the fraud, should have been imputed to the company and hence, the Hampshire Land principle was not applicable. Brooke L.J. held that such an allegation was too "ingenious and much too remote from reality" and the

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<sup>558</sup> *PCW Syndicates* (n71)

<sup>559</sup> *Group Josi* (n57)

<sup>560</sup> [1999] Lloyd's Rep IR 371

<sup>561</sup> [2003] Lloyd's Rep IR 525

<sup>562</sup> *ERC Frankona Reinsurance* (n65)

<sup>563</sup> *PCW Syndicates* (n71)

<sup>564</sup> Similar to the previous case trend analysis, this case trend analysis only concerns cases between the period of 1995 to 2017, and it is not an analysis of all the cases in England and Wales related to the agent's duty of disclosure and the Hampshire Land principle.

<sup>565</sup> *Sphere Drake Insurance* (n568)

<sup>566</sup> *PCW Syndicates* (n71)

<sup>567</sup> *Re Hampshire Land* (n79)

<sup>568</sup> *Group Josi* (n57)

<sup>569</sup> *ibid* [100]-[101]

<sup>570</sup> *PCW Syndicates* (n71)

<sup>571</sup> *Kingscroft and Ors* (n567)



reinsurer was not entitled to avoid the contract.<sup>572</sup> The judgments of the *PCW Syndicates* case<sup>573</sup> and *Group Josi* case<sup>574</sup> were followed without criticism.<sup>575</sup>

In *ERC Frankona Reinsurance v American National Insurance*,<sup>576</sup> the reassured argued that the non-disclosure of the previous conviction of the agent's director was not disclosable, due to the application of the Hampshire Land principle, but the argument was rejected by Mr. Justice Andrew Smith. He held that judging from the evidence before him, he saw no reason that the agent's company would have declined to disclose the previous conviction records of its director, and hence the Hampshire Land principle was not applicable.<sup>577</sup> Mr. Justice Andrew Smith also distinguished the current case from the *Kingscroft and Ors* case,<sup>578</sup> and the learned judge did not seek to deviate from the judgment of the *PCW Syndicates* case<sup>579</sup> as far as the Hampshire Land principle was concerned.

The above case trend analysis has revealed that with respect to the agent's duty of disclosure, no judges have sought to challenge the principle that was established in the *PCW Syndicates* case,<sup>580</sup> and hence, the Hampshire Land principle was a settled rule in utmost good faith cases. The only problem was that since the Hampshire Land principle was not expressly stated in the MIA 1906, it is likely that the reader may not have been aware of the existence of the said principle. Therefore, the reform of Hong Kong law should consider including the Hampshire Land principle into the legislation for the sake of clarity. It is noteworthy that contrary to the above founding through the case trend analysis, there are considerable criticisms about the scope of the Hampshire Land principle, and therefore these criticisms will be addressed in the next sub-section.

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<sup>572</sup> *ibid* 375

<sup>573</sup> *PCW Syndicates* (n71)

<sup>574</sup> *Group Josi* (n57)

<sup>575</sup> *Kingscroft and Ors* (n567) 374

<sup>576</sup> *ERC Frankona Reinsurance* (n65)

<sup>577</sup> *ibid* [135] – [136]

<sup>578</sup> *ibid* [200]

<sup>579</sup> *PCW Syndicates* (n71)

<sup>580</sup> *PCW Syndicates* (n71)

## **B. The IA 2015 has caused new problems for the agent's duty of disclosure**

As identified in the previous section, there are three problems for the agent's duty of disclosure. Firstly, the MIA 1906 did not provide a definitive scope for the agent's duty of disclosure. Secondly, the MIA 1906 was unclear as to how the agent, who was not a placing broker, was subject to the duty. Thirdly, the Hampshire Land principle was absent from the legislation. It is submitted, to some extent, that the IA 2015 has solved these problems, but the IA 2015 has also caused new uncertainties that are undesirable for Hong Kong law reform. Consequently, the problems of the IA 2015 will be examined in the following sub-sections.

### **i. The new duty of reasonable search is not clearly defined and causes new uncertainties for the future practice**

Under the IA 2015, section 19 of the MIA 1906 has now been repealed and there is no section that is identical to section 19. In other words, there is no longer an independent duty of disclosure for the agent under the duty of utmost good faith/fair presentation.<sup>581</sup> It is submitted that this change of law is reasonable and should be welcomed as a way of reforming Hong Kong legislation. The reason is that section 17 of the MIO, as a general section that governs the duty of utmost good faith, suggests that this duty is to be observed by either party to an insurance contract. The term "either party", which means either the assured or the insurer, suggests that the agent is not a party to an insurance contract, and thus the agent should not owe a duty of utmost good faith. In this regard, it is submitted that section 19 should not be independent from the assured's duty of disclosure, as the duty that is owed by the "agent to insure", who has the actual authority to act on behalf of the assured, is another aspect of the assured's duty. Therefore, it is submitted that the adoption of the IA 2015 approach, which merges the agent's duty of disclosure with the assured's duty, is preferable for reforming Hong Kong legislation, as it helps to clarify the position of law in relation to the agent's duty of disclosure.

The other factor that supports the IA 2015 approach is that section 19 itself has a very limited application in practice. In England and Wales, the Law Commission found that there have only

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<sup>581</sup> Explanatory notes to the Insurance Bill 2015 (n29), para 59.

been 20 reported cases in the last 100 years that have involved the application of section 19.<sup>582</sup> In Hong Kong, there has been only 1 reported case, namely, *Success Insurance v George Kallis (Manufacturers) Ltd.*,<sup>583</sup> that has involved a discussion as to whether the assured could rely on the agent's knowledge about a shipping line that was rarely used by the assured. The judgment, however, focused on the application of section 18 of the MIO in relation to the deemed knowledge of the assured, which was irrelevant to section 19.<sup>584</sup>

While the above analyses mainly concern the application of section 19(a) of the MIO, it is submitted that section 19(b) is also outdated and has little importance in the modern era.<sup>585</sup> Section 19(b) provides that the agent needs to disclose every material knowledge from the assured to the insurer unless "it comes to his knowledge too late to communicate it to the agent." With the advanced technology available to all in the modern era, it is highly unlikely that the assured would be unable to communicate with the agent in time.<sup>586</sup> In this regard, it is submitted that the whole of section 19 of the MIO has little significance in practice, and to avoid the confusion about the agent's duty of disclosure, section 19 should be repealed for Hong Kong law reform.

The repeal of section 19 of the MIA 1906, however, does not mean that the material knowledge that is possessed by the agent will no longer be disclosable under the IA 2015. Section 3(4) of the IA 2015 provides that the assured has a duty to disclose "every material circumstance which the insured knows or ought to know." Under section 4(3)(b), the knowledge requirement now includes the knowledge of "one or more of the individuals who are responsible for the insured's insurance."

Section 4(8)(b) stipulates that the disclosable information includes the knowledge of the agent. In the explanatory notes, it is suggested that these measures are intended to treat the knowledge of the agents as imputed to the assured, but the scope of it is intended to be set up

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<sup>582</sup> Law Commission (n37) para 7.4

<sup>583</sup> *Success Insurance* (n136)

<sup>584</sup> *ibid* 14

<sup>585</sup> See, 'Reform of the pre-contractual duty of disclosure of the agent to insure: evolution or revolution?', Claire Blanchard, [2013] L.M.C.L.Q. 325, 337

<sup>586</sup> See Gilman, Templeman, Blanchard, Hopkins and Hart (n38) Para 16-38

with flexibility.<sup>587</sup> Judging from the language of these sections, it is arguable that the wording “who are responsible for the insured’s insurance” enhances the scope of the duty because section 19 of the MIA 1906 only required the “agent to insure” to disclose material knowledge.<sup>588</sup> Lord Mance commented that under the IA 2015, there is no longer the category of “agent to know” under the duty of disclosure,<sup>589</sup> the view of which is supported by the authoritative textbooks.<sup>590</sup> However, the matter as to whether the “agent to know” is still subject to the duty of disclosure under the IA 2015 is further complicated by the new duty of reasonable search. Section 4(6) of the IA 2015 requires the assured to conduct a reasonable search, and section 4(7) provides that the search should include the knowledge that is possessed by the agent. In the explanatory notes, it is suggested that the knowledge of the “agent to know” may still be required to be disclosed under the new duty of fair presentation.<sup>591</sup> In this regard, it appears that the scope of the agent’s duty of disclosure, under the new duty of fair presentation, is identical to the original agent’s duty under the MIA 1906. Nevertheless, there is no definitive answer to this issue. According to the Law Commission, the scope of the duty is expected to be framed by the insurance market and the parties to an insurance contract.<sup>592</sup> However, the conflicting views from different stakeholders have further complicated the matter. The insurers in the market express their concerns that the scope of the duty can be narrower than expected subject to the judicial interpretation of the duty.<sup>593</sup> On the contrary, Peter Macdonald Eggers QC suggests that the new duty of disclosure under the IA 2015 is a wider one than the old one under the MIA 1906.<sup>594</sup> These views reflect the current situation that, with respect to the agent’s duty of disclosure, the duty of reasonable search has no definitive scope and causes new uncertainties to this area of law,<sup>595</sup> and hence, the new duty is undesirable for Hong Kong law reform, unless the scope of the duty can be clearly defined in the legislation.

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<sup>587</sup> Explanatory notes to Insurance Bill 2015 (n29) para 56. The scope, as suggested, shall be “expected to be construed relatively narrowly, but are capable of being applied flexibly”, which did not add meaning on the section.

<sup>588</sup> Similar view is expressed by the City of London Law Society, see House of Lords (n83) page 87, para 4. It is submitted that, however, the difference between the old section 19 and the new section 4(3)(b) is minimal, as the old section 19, as defined in the previous sub-section, also includes knowledge that ought to be communicated to the placing agent.

<sup>589</sup> *ibid* page 56, Q30.

<sup>590</sup> See, for example, Merkin (n42) para A-0731 and MacGillivray (n195) para. 20-033.

<sup>591</sup> Explanatory notes (n29) para 58

<sup>592</sup> House of Lords (n83), page 15, para 10 and 11

<sup>593</sup> *ibid*, page 32, para17

<sup>594</sup> Peter MacDonald Eggers QC, ‘The fair presentation of commercial risks under the Insurance Act 2015’ in Malcolm Clarke and Baris Soyer (Eds.), *The Insurance Act 2015: A New Regime for Commercial and Marine Insurance Law* (Informa 2016), page 32-33

<sup>595</sup> The author’s view is that the category of “agent to know” will still exist after the enactment of the IA 2015. Lord Mance commented that the possible operation of the duty of reasonable search is as follows: “...the postulate of

The problem of the duty of reasonable search is also criticised in chapter 1 of this thesis. It is unreasonable to expect the actual person, who is responsible for arranging the insurance for the company, to search for information that is possessed by senior management or other companies. Similar logic applies to the duty of reasonable search in relation to the knowledge that is possessed by the agent. The actual person that is responsible for the arrangement of the insurance for the assured is highly unlikely to be able to access the knowledge of the agent, who is likely to be a separate legal entity. In fact, the duty can be problematic when the agent is the party who effects the insurance contract. Graham Terrell, the Deputy Chair of the Liability & Accident Committee of the British Insurance Brokers' Association, has criticised this, saying that it is impractical to expect an international insurance broker firm, with 70 branches across the world, to comply with the duty of reasonable search by searching all the databases of all branches.<sup>596</sup> Again, it reveals that there is a need to provide a definite scope for the duty of reasonable search. It is noteworthy that the duty of reasonable search is not contradictory to the common law principle that the assured is not allowed to turn a blind eye to the information that he or she is supposed to know if a reasonable enquiry is made during the underwriting process.<sup>597</sup> In this regard, it is suggested that the duty of reasonable search is still adaptable for preserving the interests between the parties to the contract in Hong Kong, but the scope of it should be accurately defined.<sup>598</sup>

## **ii. The Hampshire Land principle is codified in the IA 2015**

The IA 2015 has imposed a new section to address the problem that the Hampshire Land principle was absent from the MIA 1906. Section 6(2) of the IA 2015 clarifies the common law position of the Hampshire Land principle, specifically that the party, who is subject to the knowledge requirement of the fair presentation, is not deemed to know the fraud that is

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“reasonable search” seems to be that anything that ought reasonably to have been revealed by a reasonable search is then imputed, so that, unless the fraud exception applies, the agent’s silence, even in the face of a question, would not matter; it would still be something which he ought reasonably to have revealed to the principal and therefore something of which the principal was taken to be aware so that the insurance would fail.” See House of Lords (n83) page 57, q30. Judging from the explanation of Lord Mance, it seems to the author that the old “agent to know” requirement has now been recategorised into a new duty of reasonable search. Be that as it may, it does not affect the conclusion that the duty of reasonable search is lack of certainty and it does not solve the problem that is identified in the previous subsection.

<sup>596</sup> *ibid* page 67, Q41 and page 69, para 10

<sup>597</sup> See, for example, *Wise Ltd* (n40)

<sup>598</sup> The suggested solution of this problem will be discussed in section III of this chapter.

perpetrated against the assured.<sup>599</sup> Nevertheless, one may observe that the said section does not provide guidance on the application of the Hampshire Land principle. According to the Law Commission, section 6(2) should remain flexible because the scope of the Hampshire Land principle is still uncertain,<sup>600</sup> and the uncertainty lies in the question of whether the Hampshire Land principle can be applied beyond cases of actual fraud.<sup>601</sup> In the context of utmost good faith, the possibility that the principle can be applied beyond cases of actual fraud was mentioned in the *Kingscroft Insurance Co Ltd* case<sup>602</sup> and the *ERC Frankona Reinsurance* case,<sup>603</sup> but none of the authorities had confirmed this application of the Hampshire Land principle.<sup>604</sup> Outside the context of utmost good faith, the case *Bilta (UK) Ltd (in liquidation) v Nazir*<sup>605</sup> is now considered as the leading authority of the Hampshire Land principle.<sup>606</sup> However, as Lord Neuberger and Lord Mance suggested, the application of the Hampshire Land principle is a matter of context,<sup>607</sup> and hence the *Bilta* case,<sup>608</sup> which was concerned with damages in tort and insolvency contribution, may be distinguishable from the utmost good faith/fair presentation cases.<sup>609</sup> Be that as it may, it is evident that English law does not provide a definitive answer regarding the scope of the Hampshire Land principle in utmost good faith cases, and the application of the said principle heavily depends on the surrounding factors of each case. In other words, the application of the Hampshire Land principle can only be considered on a case-by-case basis. Therefore, it is unrealistic to propose a one-size-fits-all rule to regulate the Hampshire Land principle. As further judicial development is expected, it is submitted that the IA 2015 approach of codifying Hampshire Land principle is already the best solution at the moment, and therefore should be followed by Hong Kong law reform.

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<sup>599</sup> See Insurance Act 2015, section 4(2)(3) and 5(1)

<sup>600</sup> Law Commission (n4) para 8.75 – 8.76

<sup>601</sup> See Gilman, Templeman, Blanchard, Hopkins and Hart (n38) para 16-48

<sup>602</sup> *Kingscroft and Ors* (n567)

<sup>603</sup> *ERC Frankona Reinsurance* (n65)

<sup>604</sup> Gilman, Templeman, Blanchard, Hopkins and Hart (n38) para 16-48 and 16-49

<sup>605</sup> [2015] UKSC 23; [2015] All ER 1083; [2016] A.C. 1

<sup>606</sup> See Gilman, Templeman, Blanchard, Hopkins and Hart (n38) para 16-48 about the analysis of how *Bilta (UK) Ltd (in liquidation) v Nazir* is applicable to utmost good faith/fair presentation cases.

<sup>607</sup> *Bilta* (n612) [9] and [41]

<sup>608</sup> *ibid*

<sup>609</sup> There is also concern in the case about the title of the “fraud” exception rule, as Lord Neuberger put it, the Hampshire Land principle extends beyond fraud. Again, judging from the case fact of the Hampshire Land case itself as well as its appliance in utmost good faith cases, it is submitted that the use of term “fraud exception rule” shall be retained until further case law development on this issue.

It is noteworthy that the Hampshire Land principle is criticised for encouraging the assured to turn a blind eye to the fraud of the agent.<sup>610</sup> Nevertheless, as far as the duty of utmost good faith is concerned, such a criticism is not supported by any modern case authority. It is also illogical to suggest that the assured is deemed to know the fraud of the agent, as common sense suggests that the agent is likely to hide the fraud from the assured. In this regard, the said criticism is invalid, and it should not be an obstacle for codifying the Hampshire Land principle in Hong Kong.

**iii. Further uncertainties are caused by the new exclusion of confidential information**

In addition to the codification of the Hampshire land principle, the IA 2015 excludes confidential information from the agent' duty of disclosure. Section 4(4)(a) of the IA 2015 provides that the assured, who is subject to the duty of fair presentation, is not obliged to disclose confidential information that is known by an agent or an employee of an agent. Furthermore, section 4(4)(b) restricts the agent's disclosure of confidential information that is obtained through a party who is not connected to the insurance contract. It is suggested that section 4(4) aims to clarify the question of whether the insurance broker is required to disclose information that is obtained from other client who is not connected to the insurance contract.<sup>611</sup> Section 4(5)(b) further clarifies that the reassured/agent is obliged to disclose information that is obtained from a person who is connected to the insurance contract, the risk of which is covered by the reinsurance contract of the reassured.

At first sight, these new sections seem sensible. However, as pointed out by Lord Mance, the new exclusion is "an unusual concept" in this area of law, which may be contradictory to the judgments since the two *Blackburn* cases in the 19<sup>th</sup> century, and Lord Mance considered it as an undesirable change of law.<sup>612</sup> The British Insurance Law Association has offered an example of the potential problem that will be caused by this new requirement:

.....the issue of whether the information in question was actually confidential (as well as whether such confidentiality as might formerly have attached to it has been lost) could be argued in open court between the insured and the insurer, with the broker

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<sup>610</sup> House of Lords (n83), page 101

<sup>611</sup> Explanatory notes to Insurance Bill 2015 (n29) para 60. The parties, that are connected to the contracts, specifically mean the parties that are covered by the insurance contract, see The Insurance Act 2015, section 4(5)(1).

<sup>612</sup> House of Lords (n83), page 59, q34

being no more than an embarrassed and reluctant witness, and the party who had originally asserted (and might want to continue to assert) the confidentiality of the information in question playing no part at all in the proceedings.<sup>613</sup>

The British Insurance Law Association concluded that the change may cause a new problem rather than solving the old problem.<sup>614</sup> For the operation of the said exclusion, the most common scenario is that a broker obtains information from the assured A, but there is no agency contract between the parties. Later, the broker arranges an insurance contract for the assured B for a similar risk. In this situation, is the material information, that has been obtained from the assured A, disclosable to the insurer of the assured B? Under the IA 2015, the answer is that the information from the assured A is disclosable if the information is not confidential. The problem is how the matter of confidentiality can be determined when there is no agency contract between the broker and the assured A. In other words, the new exclusion of confidential information may create uncertainty as to whether certain information can be considered confidential outside an agency contract.

Another potential problem of the said exclusion is illustrated in *Quinn Direct Insurance v Law Society*.<sup>615</sup> This case concerned a professional indemnity insurance. The insurer sought a court order to access the information, which was possessed by the Law Society, in relation to the books and accounts of the assured. The judgment was mainly about the public function of the Law Society, as well as the contractual terms in relation to the disclosure of information, nonetheless, the court commented on the relationship between the duty of disclosure and confidentiality as follows:

He [the assured] cannot justify any concealment of a material matter on the ground that he, personally, is privileged from disclosing it nor, perhaps, on the ground that the information he failed to disclose was confidential. Nevertheless, the privilege is that of his client and cannot be broken or waived without the client's consent.<sup>616</sup>

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<sup>613</sup> *ibid*, page 76, para 21

<sup>614</sup> *ibid*

<sup>615</sup> [2010] 1 Lloyd's Rep IR 655

<sup>616</sup> *ibid* [24]



This judgment suggested that the assured could not rely on the ground of confidentiality to conceal material knowledge that he or she was required to submit under the duty of disclosure unless his or her client had waived the confidentiality of the disputed knowledge. Although the judgment may not be directly relevant to the agent's duty of disclosure, it raises the issue of whether the confidentiality can be waived by the assured and if so, under what circumstances such waiver can be applied. Again, the IA 2015 has not provided a clear answer to this issue, and it may add another uncertainty to the agent's duty of disclosure.

To summarise, the core problem of the exclusion of confidential information by the agent is that it is an unprecedented doctrine. There is no case law that has suggested there is a conflict between non-disclosure and the requirement of confidentiality. Considering the uncertainties that will be caused by the said exclusion, it is submitted that this change of law is not desirable for Hong Kong law reform.

## **II. Reforming the agent's duty of disclosure in Hong Kong**

### **A. The reform strategy – the actual assured approach**

In respect to the agent's duty of disclosure, both the MIA 1906 and the IA 2015 are problematic. The MIA 1906 did not provide a detailed guidance about the operation of the agent's duty of disclosure. The IA 2015 has imposed new provisions to solve the problems under the MIA 1906, but the new provisions are also likely to cause further new problems for the agent's duty of disclosure, which may defeat the purposes of reforming the law. In this regard, it is submitted that both the MIA 1906 and the IA 2015 should not be strictly followed for Hong Kong law reform.

Despite the legal problems that have been identified in the previous sub-sections, there is another problem that is yet to be examined in relation to the agent's duty of disclosure. This problem regards whether the duty of utmost good faith/fair presentation forms a justifiable basis for the imputation of knowledge between the agent and the assured. In section I(A) of this chapter, nine cases in England and Wales, which were reported in the Lloyd's Insurance and Reinsurance Law Report between 1995 to 2017, were analysed, and it was found that none of the assured in these cases was liable for breaching the duty of disclosure, because of an

imputation of knowledge from the agent to the assured.<sup>617</sup> While the doctrine has rarely been used over the past twenty years, the detriment of the imputation approach was demonstrated in the *Blackburn* cases. The detriment is that the assured is liable for breaching the duty of disclosure in the situation where he or she has no awareness of the material knowledge that is concealed by the agent. Both the MIA 1906 and the IA 2015 provide measures to ensure that the insurer will not suffer from the information asymmetry. However, the legislation never considers the detriment that the assured has suffered. In the situation where the agent conceals the material information without informing the assured, there are no means for the assured to discover the concealed facts, and thus to comply with the duty. In this regard, it is submitted that the imputation approach is no longer fit for the purpose of ensuring fairness between the assured and the insurer, and the author suggests reforming the agent's duty of disclosure by introducing a new "actual assured" approach for the knowledge requirement of the duty of disclosure, which was introduced and analysed in chapter 1 of this thesis. The detailed proposal of this "actual assured" approach will be made in the next sub-section.

The other question to be considered is about how the reform of the agent's duty of disclosure should be effected. The repeal of section 19, as suggested in section I(B)(i), requires a deletion of the existing legislative provision. Therefore, this part of reform can only be effected by a legislative change, and it does not require further judicial development.<sup>618</sup>

The reform of the "actual assured" approach is more complicated. To draw the attention of the reader of the legislation about the change of law, the most efficient way is to impose new provisions to the MIO. Nevertheless, since the "actual assured" approach requires the judges to examine the new duty on a case-by-case basis, the reform also requires a certain degree of judicial development. The same approach is applicable to the codification of the Hampshire Land principle, which requires an additional provision. In addition, it also requires further judicial development, as the scope of it is uncertain at the moment. That is to say, pure judicial development of the reform is undesirable, as it may adversely affect the accessibility of the

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<sup>617</sup> For the purpose of clarification, in the *ERC* case, although the reassured was liable for breaching the duty of utmost good faith, the judgment was based on the fact that the reassured was evidently aware of the previous conviction of the underwriting agent of the insurance contract that was covered by the disputed reinsurance contract. It did not involve the imputation of knowledge from the agent to the reassured.

<sup>618</sup> For the purpose of clarification, section 19 will be simply deleted from the Marine Insurance Ordinance as a reform suggestion; therefore, it will not be examined in the next sub-section.

reform. The detailed reform and the operation of the new duty will be explained in the next subsection.

### **B. The solution – Imposing new provisions to the MIO and further judicial development**

In chapter 1 of this thesis, the author submits that section 18(1) should be amended as follows to reform the knowledge requirement of the assured:

(a) 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 person who is responsible for the assured's insurance (the actual assured), and the assured is deemed to know every circumstance which, in the ordinary course of business, ought to be known by the actual assured, unless it is a knowledge of fraud perpetrated against the assured. If the assured fails to make such disclosure, the insurer may avoid the contract.

(b) The assured is deemed to know what should reasonably have been revealed by a reasonable search of information accessible to the actual assured.

Section 18(1)(c) should be added as follows:

(c) If the person who is responsible for the assured's insurance is an agent of the assured, the knowledge of fraud, which is perpetrated by the agent against the assured, is not imputed to the assured.

It is submitted that the new section 18(1)(a) is applicable to the situation where the agent is the party that is responsible for arranging the insurance contract. Under the new section 18(1)(a) and section 18(1)(b), the term "actual assured" does not mean "the assured", but the actual person who is responsible for the arrangement of the insurance. In other words, if the arrangement is made by an agent, the said agent (or an actual person in the said agent company) is the "actual assured", and he or she is subject to the duties under section 18(1)(a) and section 18(1)(b). Section 18(1)(c) is added to address the application of the Hampshire Land principle.

The reform has solved the three problems that are stated in section I(A) of this chapter. Firstly, the reform ensures that there will not be any further dispute about the scope of the duty. The three types of agent, namely the “agent to insure”, the “agent to know” and the “agent in a predominant position” will no longer exist under the new duty of disclosure. The actual assured, under the new duty of disclosure, who can be any individual person of the assured or the agent company, will only be required to disclose information that is within his or her reach. The reasonable search requirement also ensures that the actual assured will not be allowed to turn a blind eye to the information that is accessible to him or her. The possession of knowledge and the question of whether the information is accessible by the actual assured, as discussed in chapter 1, is a matter of fact, which avoids the problem that the assured is deemed to know any information that is in fact not possessed by or accessible to him or her.

The Hampshire Land principle is also codified to draw the reader’s attention to the legislation. As examined in section I(B)(ii) of this chapter, the IA 2015’s approach is currently the best option for codifying the Hampshire Land principle, and therefore it should be strictly followed for Hong Kong law reform. It may be arguable that the suggested reform is contradictory to the judgment of the *Bilta* case.<sup>619</sup> The said judgment suggested that the Hampshire Land principle could be applied beyond actual fraud, and thus the suggested legislative change shall not limit the application of the Hampshire Land principle to actual fraud cases only. Nevertheless, the *Re Hampshire Land* case<sup>620</sup> was a case concerned with the actual fraud of the agent. The question of whether the Hampshire Land principle could be applied beyond actual fraud was not examined in the *Re Hampshire Land* case.<sup>621</sup> Furthermore, there were not any utmost good faith cases suggesting that the Hampshire land principle can be applied beyond actual fraud. In this regard, it is submitted that the legislative change shall limit the application of the Hampshire Land principle to cases of actual fraud only.<sup>622</sup>

The reform also imposes a more definitive duty of reasonable search to avoid the uncertainties that were identified in section I(B) of this chapter. The scope of the new duty of reasonable

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<sup>619</sup> *Bilta* (n612)

<sup>620</sup> *Re Hampshire Land* (n79)

<sup>621</sup> *ibid*

<sup>622</sup> *ibid*. For the situation that beyond actual fraud, the “actual assured” approach shall be sufficient to ensure fairness, and the detailed operation of it shall be examined in the following passages.

search will be determined by whether or not the knowledge is accessible by the actual assured. The actual operation of the new duty is demonstrated in the following hypothetical situation. An agent, who acts as an actual assured, is accused of being in breach of the duty of disclosure, because he or she did not disclose material information, which is held by the agent's subsidiary company. The said subsidiary company is based in another country, and its information technology system is different from the agent's system. In this case, the determination of whether the agent has complied with the duty of reasonable search involves several issues. The first issue is whether the agent was aware of the existence of the material knowledge. In a case where the agent was aware of the existence of the information, but turned a blind eye to it, the agent is liable for breaching the duty of reasonable search. However, in a case where the agent was not aware of the existence of the material information, then the next issue to be determined is whether the agent was able to access the information. To determine the matter of accessibility, one of the questions to be examined is whether it is a normal practice for the agent to communicate with the subsidiary company in the ordinary course of business. If it is evident that the agent has a regular exchange of information with the subsidiary company, then it is more likely than not that the agent failed to comply with the duty of reasonable search, unless the agent can prove that the exchange of information could not have brought to his or her awareness the existence of the material information. On the contrary, if the actual assured can prove that in the ordinary course of business there is rarely or no communication between the two companies and that the agent cannot access the IT system of the subsidiary company, then the actual assured is not liable for the breach of the duty of reasonable search.<sup>623</sup>

It may be arguable that the "actual assured" approach, which abolishes the imputation of knowledge between the assured and the agent, may increase the burden of risk underwriting on the insurer. Nevertheless, the new agent's duty of disclosure is imposed to ensure that the matter of liability is determined by a matter of fact, and not a matter of presumption. The effect of "actual assured" approach can be illustrated by applying the new duty to the case fact of *Blackburn, Low & Co. v. Haslam*.<sup>624</sup> The third agent, in that case, would no longer be treated as knowing the fact that was concealed by the first agent. Under the new duty of reasonable

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<sup>623</sup> This chapter only analysed the reasonable search approach that is imposed on the agent when the agent is the actual assured, for the reasonable search approach of the assured and the insurer, please refer to chapter 1 of this thesis.

<sup>624</sup> *Blackburn Low & Co. v. Haslam* (n478)

search, the third agent would have to prove that, firstly, the third agent was not aware of the existence of the material knowledge. Secondly, the third agent had no regular exchange of information with the first agent. Thirdly, the third agent had no means to access the information of the first agent. Hypothetically, the third agent, in that case, would still be liable for breaching the duty of disclosure, because the case fact suggests that there was an exchange of information between the first agent and the third agent, and therefore the third agent should have at least enquired about the status of the vessel with the first agent. Since the third agent had not done so, the third agent would still liable for the breach of the duty. Although the result of applying the new duty is the same as the outcome of *Blackburn, Low & Co. v. Haslam*,<sup>625</sup> the new duty ensures that the issue of liability is determined by a matter of fact, without any presumption or imputation of knowledge, and hence, fairness can be ensured.

### **III. Conclusion**

The agent's duty of disclosure is a doctrine that is rarely used, but involves a sophisticated understanding of the matter, which can cause substantial confusion to the reader of the legislation. The scope of the duty was not fully reflected by section 18 and 19 of the MIA 1906, and it was almost impossible for the reader of the legislation to be aware of the existence of the "agent to know" and the "agent in a predominant position". In a situation where the chain of insurance involved multiple agents, it was also difficult for the assured to identify which agent was subject to the duty of disclosure. The absence of the Hampshire Land principle from the MIA 1906 was also detrimental, as it was an important indication of the scope of the duty. Consequently, it is evident that the MIA 1906 and the MIO in Hong Kong are in need of reform.

The IA 2015 has no doubt provided clearer guidance regarding the agent's duty of disclosure. However, although it has solved the old problems, the IA 2015 has also caused new problems that are certainly unfavourable for the parties to an insurance contract. Indeed, there is no clear guidance on how the new duty of reasonable search operates and the scope of it is indefinite. The new exclusion of confidential information is unprecedented and considering the uncertainties that are caused, this new exclusion is certainly unwelcomed for reforming the agent's duty of disclosure in Hong Kong. One of the purposes of imposing the IA 2015 is to

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<sup>625</sup> *Blackburn Low & Co. v. Haslam* (n478)

preserve the balance of interests between the insurer and the assured, and it seems that the IA 2015 has failed to achieve this purpose. In this regard, it is submitted that for the reform of Hong Kong law, the IA 2015 should not be strictly followed.

The suggested reform proposal for the agent's duty of disclosure in Hong Kong aims to preserve the advantages of both the MIA 1906 and the IA 2015. The reform also aims to provide a simpler but more effective way to regulate the agent's duty of disclosure. Firstly, the language of the new provisions is simple and easy to read, which ensures that the law is understandable and accessible by the reader. In addition, it also clarifies the questions that remain unanswered in case law and the IA 2015. The reform provides a precise definition of the scope of the agent's duty of disclosure, which is more reasonable for the assured in comparison with both the MIA 1906 and the IA 2015. In any event, it is submitted that the current agent's duty of disclosure in Hong Kong is in need of reform, and therefore a detailed reform proposal will be provided in chapter 6 of this thesis.

## **Chapter 6 The Reform Proposal For The Duty Of Utmost Good Faith/Fair Presentation In Hong Kong**

This chapter details the reform proposal for the duty of utmost good faith/fair presentation in Hong Kong. It will be divided into three sections. The first section examines the issue of whether the reform should be introduced as a default regime. While the legislative changes for reforming the duty of utmost good faith/fair presentation were formulated in the previous 5 chapters, the question of whether the reform should be introduced as a default regime is yet to be examined. The idea of imposing the reform as a default regime can be seen in the Insurance Act 2015, where section 15 and 16 are introduced as “contracting out” provisions. It is noteworthy that the main concern is not about how the “contracting out” provisions operate, but about whether Hong Kong law reform should adopt the “default regime” approach. Therefore, in the first section of this chapter, the author will analyse some potential examples of situations that could occur under the default regime. These include cases where the parties would either wholly or partly contract out of the duty of utmost good faith/fair presentation. The author concludes that these options may defeat the purposes of reforming the duties in Hong Kong, and thus Hong Kong should carefully consider and perhaps avoid “contracting out” provisions for reforming the duty of utmost good faith/fair presentation.

The second section proposes some draft provisions of the new Marine Insurance Ordinance for the reform of the duty of utmost good faith/fair presentation in Hong Kong. To clarify some of the key issues of the reform, explanatory notes will be provided to describe the rationale and operation of the suggested new provisions. The author also conducted an anonymous survey (the Hong Kong survey) to collect views about the duty of utmost good faith in Hong Kong. The anonymous survey ensures that all the views from the participants are equally weighted, and it helps to prevent bias in analysing the results of the survey. It is also more likely that the participants are willing to provide honest responses under an anonymous survey, as the identities of the participants are not traceable. The 19 participants of the Hong Kong survey include academics, lawyers, insurance agents/brokers and insurers who used to work/has been



working within Hong Kong insurance industry. The survey results will be analysed and considered as a reference for the reform proposal in the following sections.<sup>626</sup>

The last section offers guidance about the application of the new duty of utmost good faith/fair presentation. A hypothetical case analysis will be provided to demonstrate how the reform proposal would work in practice.

**I. Reforming the duty of utmost good faith/fair presentation in Hong Kong: should it be introduced as a default regime?**

The issue that is yet to be determined for the reform of the duty of utmost good faith/fair presentation in Hong Kong is whether the reform should be introduced as a default regime. The default regime approach can be seen in the IA 2015. Section 16(2) of the IA 2015 states that any term, which will put the assured in a disadvantageous position, shall be treated as a term with no legal effect unless the transparency requirement of section 17 is met by the insurer. Section 17(2) requires the insurer to “take sufficient steps to draw the disadvantageous term to the insured’s attention before the contract is entered into or the variation agreed.” Section 17(3) requires that “The disadvantageous term must be clear and unambiguous as to its effect.” In other words, the parties to an insurance contract are free to contract out of the duty of fair presentation and its remedies under the IA 2015. The Law Commission commented that the “contracting out” clauses will help to maintain flexibility of the UK insurance market and provide considerable freedom for the parties to tailor-made their own contract.<sup>627</sup>

The question, therefore, is whether this approach is desirable for reforming the duty of utmost good faith/fair presentation in Hong Kong. According to the Hong Kong survey, 10 respondents thought that the default regime was desirable for the Hong Kong law reform, 4 respondents believed that the default regime was undesirable, and 5 respondents had no comment on this issue. One respondent expressed their concern that the default regime will create much uncertainty. The flexibility of the default regime is no doubt attractive to the insurers, as they are free to contract out of any terms that are unfavourable to them, provided that the “transparency requirement” is met. Nevertheless, the main purpose of the reform is to ensure fairness

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<sup>626</sup> The questionnaire of the survey is attached in Annex 4 of this thesis.

<sup>627</sup> Law Commission (n4) para 29.25

between the parties to an insurance contract, and whether the “contracting out” clauses can achieve this purpose is a matter that is yet to be examined. In the following sub-section, the author will assess the impact of the “contracting out” clauses in two scenarios. The first scenario regards the contracting out of the whole duty of utmost good faith/fair presentation, and the second scenario regards the contracting out of the remedies of the duty of utmost good faith/fair presentation.

#### **A. The first scenario: contracting out of the whole duty of utmost good faith/fair presentation**

The first scenario is that the parties agree to contract out of the duty of utmost good faith/fair presentation, although the Law Commission expressed the view that the contracting out of the duty of fair presentation is unlikely to happen in practice.<sup>628</sup> However, the “contracting out” clauses open up the possibility for contracting out of the duty of fair presentation, and the said clauses should be examined to assess the impact of introducing the “contracting out” clauses into the reform proposal of Hong Kong legislation.

One of the possible consequences is that the parties to an insurance contract will establish their own rules to govern the assured’s conduct in relation to disclosure and presentation of the risk at the underwriting stage. This consequence, however, is likely to complicate the market practice. One of the examples is provided by the British Insurance Brokers’ Association as follows:

We do not agree with insurers being able to contract out of the new regime in all circumstances. For example, in subscription placement, it could cause problems if some insurers contract out and others do not, e.g. by leaving the insured with a gap in cover in the event of a claim.<sup>629</sup>

Similar views are also supported by London & International Insurance Brokers’ Association<sup>630</sup> and Marsh Limited.<sup>631</sup> Although the said concern can be solved by a pre-contractual arrangement between the insurers, the said concern also reflects that for this kind of multi-lines

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<sup>628</sup> House of Lords (n83) page 20

<sup>629</sup> *ibid*, page 69, para 14

<sup>630</sup> *ibid*, page 97, para 9

<sup>631</sup> *ibid*, page 106, para 10

arrangement of insurance, the “contracting out” clauses may impose an extra administrative burden on the insurer, which may be unfavourable for the insurance industry.

One may also need to consider that without the interference of the law, it would be likely that the insurer would have better knowledge to impose terms that are more favourable for the insurer, which could be unfair to the assured.<sup>632</sup> Indeed, a similar concern has been expressed by Aon UK Limited as follows:

The only time we can see insurers contracting out of their new duties is when the insured: (1) does not understand the impact; or (2) is in a weak bargaining position. We believe this would mean that the most financially vulnerable insureds (i.e. the ones who need this protection the most) will be the ones who are left exposed where contracting out is allowed.<sup>633</sup>

Aon UK Limited’s concern is relevant to another argument in favour of the default regime, which is the assured can benefit from the default regime by negotiating terms that help to reduce the premium. For instance, the assured could agree to contract out of the whole duty of fair presentation and adopt terms that are similar to the duty of utmost good faith under the MIA 1906, and in return, the insurer may offer a discount for the premium. The remedy of the avoidance is harsher for the assured, and the insurer is in a more favourable position to avoid the contract based on non-disclosure and misrepresentation. Nevertheless, as suggested by the Aon UK Limited, the assured (particularly in the case of the assured being a small business) may lack the knowledge required for the negotiation of insurance terms in most of the situations. It would be too idealistic to assume that the assured would fully understand the pros and cons of contracting out of the duty of utmost good faith/fair presentation. Furthermore, from a risk management perspective, contracting out of the duty of fair presentation and the adoption of the duty of utmost good faith would simply lead to exposure to the risk of avoiding the contract by the insurer based on non-disclosure and misrepresentation. In this regard, it is submitted that this consequence would not help to ensure fairness between the parties to an insurance contract and therefore, it is unfavourable for Hong Kong law reform.

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<sup>632</sup> See, Gerald Swaby 'Insurance law: fit for purpose in the twenty-first century?' 2010 Int. J.L.M. 21, page 32

<sup>633</sup> *ibid*, page 80, para 9.

The other possible consequence is that the “contracting out” clauses may eliminate the precontractual duties of disclosure and presentation of the risk. In other words, it may be possible that the parties are free from the duty of utmost good faith/fair presentation. It is noteworthy that Lloyd’s Market Association warned that waiving the duty of fair presentation may lead to “the most egregious types of non-disclosure or misrepresentation”<sup>634</sup> and thus, it may be unlikely that the insurer will accept such an arrangement in normal circumstances. In theory, the elimination of the duty of fair presentation may happen in a soft market where there are more insurers than assureds. For example, the current London insurance market is often described as a soft market.<sup>635</sup> Evidence of this is provided in the Airmic report, which indicates that brokers and the assured seek to “sign-off” the duty of fair presentation in the London insurance market.<sup>636</sup> In addition, the Lloyd’s Market Association suggests that there are eight types of contracting out clauses in the market.<sup>637</sup> One of the examples is that an express waiver is included in the insurance contract to waive all rights arising from the duty of fair presentation.<sup>638</sup>

At first sight, this consequence seems to be favourable to the assured. The question, however, is whether the same situation would occur in Hong Kong. According to statistics from the Insurance Authority, the Hong Kong general insurance market recorded an annual gain of HKD\$1.8 billion in 2016, which suggests that Hong Kong may be a hard market, and thus, contracting out of the duty of utmost good faith/fair presentation may not happen in Hong Kong. Moreover, the duty of utmost good faith/fair presentation is imposed to ensure that the exchange of information between the parties at the pre-contractual stage can be fairly regulated. By allowing the parties to contract out of the duty of utmost good faith/fair presentation, the exchange of information at the pre-contractual stage is no longer regulated by a fixed legal duty. Instead, it becomes a constant factor that depends on the market dynamics, which creates a new kind of uncertainty in the commercial insurance practice. The new

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<sup>634</sup> Lloyd’s Market Association, ‘Insurance Act 2015 – Duty of Fair Presentation – Clauses’, Lloyd’s Market Association Bulletin 2016 <[http://www.lmalloyds.com/LMA/News/LMA\\_bulletins/xLMA\\_bulletins/LMA16\\_047\\_KvdK.aspx](http://www.lmalloyds.com/LMA/News/LMA_bulletins/xLMA_bulletins/LMA16_047_KvdK.aspx)> accessed 8 March 2019

<sup>635</sup> The Lloyd’s market recorded over 2 billion pounds annual loss for both 2016 and 2017. Lloyd’s Market Association, ‘Lloyd’s demonstrates strength following 2017 major loss activity’ <<https://www.lloyds.com/news-and-risk-insight/press-releases/2018/03/2017-annual-results-gbp>> accessed 10 August 2018

<sup>636</sup> Airmic, ‘The Insurance Act 2015 – 10 months on guide 2017’, page 6, para 3.1.

<sup>637</sup> Lloyd’s Market Association, ‘Insurance Act 2015 – Duty of Fair Presentation – Clauses’, Lloyd’s Market Association Bulletin 2016 <[http://www.lmalloyds.com/LMA/News/LMA\\_bulletins/xLMA\\_bulletins/LMA16\\_047\\_KvdK.aspx](http://www.lmalloyds.com/LMA/News/LMA_bulletins/xLMA_bulletins/LMA16_047_KvdK.aspx)> accessed 6 September 2018

<sup>638</sup> *ibid*

approach also fails to ensure fairness and protect the weaker party from the information asymmetry. Given this, it is submitted that this consequence is undesirable for the Hong Kong law reform.

**B. The second scenario: contracting out of the remedy for the breach of the duty of utmost good faith/fair presentation**

The alternative method for contracting out of the duty of utmost good faith/fair presentation is to ensure that the duty is only partly contracted out by the parties to an insurance contract. In this case, it may result in a contracting out of the remedy of the duty of utmost good faith/fair presentation. One of the possible consequences would be that the new remedy would be more favourable for the insurer. The example of this kind of contracting out can be seen from the draft model clause of the Lloyd's Market Association:

Section 8(2) and Schedule 1 of the Insurance Act 2015 are excluded in their entirety. If the Insured breaches the duty of fair presentation, and the Insurer shows that but for the Insured's breach it would not have entered into the insurance contract at all, or would have done so only on different terms, then the Insurer may avoid the insurance contract and refuse all claims. If the breach was deliberate or reckless, the Insurer need not return any of the premiums paid. If the breach was not deliberate or reckless, the Insurer must return the premiums paid.<sup>639</sup>

The draft clause aims to contract out of the proportionate remedy that is imposed by the IA 2015. In a case where there is a breach of the duty of fair presentation, the only remedy for the insurer to seek against the assured is the remedy of avoidance. It is noteworthy that the effect of the draft clause remains in doubt, as the transparency requirement is yet to be tested by the court. Nevertheless, the draft model clause of the Lloyd's Market Association indicates the fact that it is entirely possible for the insurer to replace the proportionate remedy of the IA 2015 with the single remedy of avoidance of the MIA 1906. Therefore, this consequence is unfavourable, as it wholly defeats the purpose of the reform by allowing the insurer to adopt the single remedy approach, which is detrimental to the assured.

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<sup>639</sup> Lloyd's Market Association, 'Model clauses for use in connection with the Insurance Act 2015 - LMA9121' <<http://www.lmalloyds.com/actclauses>> accessed 14 March 2019

The other possible consequence is that after contracting out of the remedies of the duty of utmost good faith/fair presentation, the new remedy is in favour of the assured. However, similar to the first scenario, this situation would only happen when the assured fully understands how the remedies operate to negotiate for such a favourable remedy. The assured company may employ its own insurance department with lawyers who are experienced in dealing with commercial risks. In the case that the assured are small businesses, this situation is highly unlikely to happen. In this regard, it is submitted that the default regime approach will only be beneficial to larger companies but detrimental to the smaller companies, and thus, fairness cannot be ensured between the parties to an insurance contract.

**C. Conclusion: should it be possible to contract out of the duty of utmost good faith/fair presentation?**

The two scenarios above indicate the fact that the contracting out of the duty of utmost good faith/fair presentation can be problematic. The “contracting out” clauses are imposed in the IA 2015 to uphold freedom of contract. Nevertheless, freedom of contract is well protected by the general contract law, and there is no need to impose new protection of the commercial insurance law. In theory, despite the imbalance of bargaining power between the parties, the parties are always free to negotiate a contractual term that excludes the duty of utmost good faith/fair presentation, and the effect of such a contract term is determined by the general contract law. Indeed, by introducing new “contracting out” clauses into the legislation, it certainly creates new uncertainties for the interpretation of contractual terms in relation to the commercial insurance contract.

Worse still, the incorporation of the “contracting out” clauses in the reform proposal can also be treated as an invitation to contract out of the duty of utmost good faith/fair presentation. For example, apart from the Lloyd’s standard clauses, the Shipowners’ Limited also decided to contract out of the proportionate remedies under the IA 2015 and adopted the remedy of avoidance in the case where there is a breach of the duty of fair presentation.<sup>640</sup> The most detrimental part of contracting out of the duty of utmost good faith/fair presentation is that it allows the insurer to adopt the single remedy of avoidance for the breach of the duty of utmost

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<sup>640</sup> The Shipowners’ Limited, ‘Club Rules 2018’, Rule 1 section 1(B)(i)  
<<https://www.shipownersclub.com/publications/club-rules-2018/?>> accessed 9 August 2018

good faith/fair presentation. This approach is criticised in chapter 4 of the thesis, and it is one of the major reasons why reform is needed for this area of law. The reform of the duty of utmost good faith/fair presentation in Hong Kong aims to correct the one-sided situation that has lasted for over 250 years, ever since the judgment of *Carter v Boehm*,<sup>641</sup> and the default regime approach simply defeats the whole purpose of the reform. It is noteworthy that this thesis only examines the problems of the “contracting out” clauses in relation to the duty of utmost good faith/fair presentation, and that the default regime approach may be feasible for other areas of law in relation to the reform of the commercial insurance law. Nevertheless, based on the above analysis, it is submitted that the default regime is not feasible for the duty of utmost good faith/fair presentation and thus, it should not be adopted as part of the reform proposal in Hong Kong. In the next section, the author will outline the detailed reform proposal for reforming the duty of utmost good faith/fair presentation in Hong Kong and provide explanatory notes for the major change in law.

## **II. The reform proposal for section 17, 18, 19 and 20 of the Marine Insurance Ordinance**

### **A. New section 17 of the MIO in Hong Kong**

#### **i. The draft provisions of new section 17 of the MIO**

##### Section 17(1)

A contract of insurance is a contract based on 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. The court or arbitrator may declare the contract subsisting and award damages in lieu of avoidance, if of opinion that it would be equitable to do so, having regard to the nature of the breach of utmost good faith and the loss that would be caused by it if the contract were upheld, as well as to the loss that avoidance would cause to the other party.

##### section 17(2)

This section does not apply to matters arising under or in relation to the duty of fair presentation, which is provided in section 18, 19 and 20 of this ordinance. The Misrepresentation Ordinance is not applicable to the cases which involved the disputes of utmost good faith/fair presentation.

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<sup>641</sup> *Carter* (n1)

## ii. The explanatory note of new section 17 of the MIO

The new section 17(1) is analysed and formulated in chapter 4 of this thesis. The new section imposes a new discretionary remedy of damages for the party who suffers from a breach of the duty of utmost good faith. The reform of section 17(1) is in line with the Hong Kong survey, in which 11 respondents agreed that a new remedy should be provided for the breach of the duty of utmost good faith. Only 2 respondents did not agree that there is a need to impose an alternative remedy for the breach of the duty of utmost good faith, with 6 respondents having no comment on this issue.

The new section 17 aims to regulate issues that are not covered by section 18, 19 and 20 of the MIO. For this reason, section 17 is now referred to as the duty of utmost good faith, and section 18, 19 and 20 are referred as the duty of fair presentation. The new section 17(1) introduces new discretionary remedies for the breach of the duty of utmost good faith. These discretionary remedies are different from the proportionate remedies of the duty of fair presentation, which are regulated by the new section 18, 19 and 20. The new discretionary remedies of the duty of utmost good faith ensure that the assured can seek damages against the insurer when the breach is committed by the insurer. As discussed in chapter 4 of this thesis, the scope of the insurer's duty of utmost good faith is still under development, and the new discretionary remedies are imposed to encourage judges to make further developments and establish the scope of the insurer's duty in Hong Kong.<sup>642</sup>

The new section 17(1) is also applicable to the case where the breach of the post-contractual duty of utmost good faith is committed by the assured. Similar to the insurer's duty of utmost good faith, the post-contractual duty of utmost good faith of the assured is still under development.<sup>643</sup> The said duty has no definite scope, and it heavily relies on the judges to examine the surrounding factors of each case to determine whether the assured has breached

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<sup>642</sup> For a detailed discussion about the scope of the insurer's duty of utmost good faith in England and Wales, see John Butler and Robert Merkin, *Butler & Merkin's Reinsurance Law, Volume 1*, (Sweet & Maxwell 2018) para A-0526 – A-0544. For a detailed discussion about the insurer's duty of utmost good faith from a global perspective, see Leander D. Loacker, *Informed insurance choice? The insurer's pre-contractual information duties in general consumer insurance*, (Edward Elgar Publishing 2015) page 149 – 185. It is noteworthy that there is no relevant discussion about the scope of the insurer's duty of utmost good faith in Hong Kong.

<sup>643</sup> For a detailed analysis about the post-contractual duty of utmost good faith, see Howard Bennett, 'Mapping the doctrine of utmost good faith in insurance contract law' [1999] LMCLQ 165, Baris Soyer, 'Continuing duty of utmost good faith in insurance contracts: still alive?' [2003] LMCLQ 39, Richard Aikens 'The post-contract duty of good faith in insurance contracts: is there a problem that needs a solution?' [2010] J.B.L. 379 and B Soyer, A.M. Tettenborn, 'Mapping (utmost) good faith in insurance law - future conditional?' [2016] L.Q.R. 618



the post-contractual duty of utmost good faith. Furthermore, among the 21 cases that were reported in the Lloyd's Insurance and Reinsurance Law Report between 1995 and 2017 with the term "post-contractual duty of utmost good faith", none of the insurers could successfully claim against the assured on the ground of breaching the post-contractual duty of utmost good faith. It appears that the post-contractual duty of utmost good faith has little practical significance. Nevertheless, under the new section 17(1), which governs the general scope of the duty of utmost good faith, the post-contractual duty of utmost good faith of the assured from the MIO cannot be eliminated because it may be revealed in future cases. Therefore, the new discretionary remedies are imposed for the judges to exercise discretions on the future matters in relation to the post-contractual duty.

The new section 17(2) is analysed and formulated in chapter 3 and chapter 4 of this thesis. The current legislation in Hong Kong has not clearly distinguished between the duty not to misrepresent under the MIO and the same duty under the Misrepresentation Ordinance. As a result, the insurer can plead for both types of misrepresentation on the same issue, which may result in an unfair outcome for the assured, as the same issue will be trialled twice. In this regard, it is suggested that the duty not to misrepresent under the MIO should be separated from the duty not to misrepresent under the Misrepresentation Ordinance. It is noteworthy that the Hong Kong survey found that 9 respondents had never handled any misrepresentation case under the Misrepresentation Ordinance. In addition, 3 respondents had only handled this kind of case less than once a year, and another 3 respondents had handled this kind of case a few times a year. The survey results suggest that the new section 17(2) may have little adverse impact on the practitioners in Hong Kong, but it ensures that the insurer is not allowed to plead misrepresentations under both the MIO and the Misrepresentation Ordinance. This measure helps to clarify the position of Misrepresentation Ordinance in utmost good faith cases.

## **B. New section 18 of the MIO in Hong Kong**

### **i. The draft provisions of new section 18 of the MIO**

Section 18(1)(a)

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 person who is responsible for the assured's insurance (the actual assured), and the assured is deemed to

know every circumstance which, in the ordinary course of business, ought to be known by the actual assured, unless it is a knowledge of fraud perpetrated by the assured. If the assured fails to make such disclosure in the absence of a valid defence, the insurer may be entitled to seek one of the following remedies:

- (i) The remedy of avoidance if, but for the breach, the insurer would not have entered into the contract of insurance at all, or
- (ii) Additional premium if but for the breach, the insurer would have entered into the contract with a higher premium.

#### Section 18(1)(b)

The assured is deemed to know what should reasonably have been revealed by a reasonable search of information accessible to the actual assured. Information that can be found on the internet is not deemed to be known by the assured.<sup>644</sup>

#### Section 18(1)(c)

If the person who is responsible for the assured's insurance is an agent of the assured, the knowledge of fraud, which is perpetrated by the agent against the assured, is not imputed to the assured.

#### Section 18(1)(d)

For the purpose of section 18(1)(a), the assured is entitled to raise a defence on the ground that the a reasonable assured would not have expected that the material circumstance is disclosable to the insurer.

#### Section 18(2)(a)

Every circumstance is material which a reasonable assured in the circumstances would have appreciated that the fact in question would be one that a prudent insurer would want to know about in fixing the premium or determining whether he will take the risk and on what terms.

#### Section 18(2)(b)

For the purpose of section 18(1), whether the insurer is induced by the assured's non-disclosure or misrepresentation of the risk, in each case, is a question of fact, and there should not be a presumption of inducement unless there is a justifiable ground for such a presumption.

#### Section 18(3)

In the absence of inquiry the following circumstances need not be disclosed, namely—

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<sup>644</sup> Deemed knowledge was analysed in Chapter 1(II) of the thesis so here it suffices to say that the deemed knowledge should not be extended to the information that can be found on the internet.

- (a) any circumstance which diminishes 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 his business, as such, ought to know. The insurer is also deemed to know what should reasonably have been revealed by a reasonable search of information accessible to the insurer.
- (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.<sup>645</sup>

#### Section 18(4)

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

#### Section 18(5)

The term "circumstance" includes any communication made to, or information received by, the assured.

#### section 18(6)

For a claim of non-disclosure, the insurer/underwriter needs to prove that had the material circumstance been disclosed, the insurer/underwriter would not have entered into the insurance contract, or would have entered into the insurance contract with additional premium.

### **ii. The explanatory note of new section 18 of the MIO**

The new section 18 introduces "the actual assured" approach to reform the duty of utmost good faith/fair presentation in Hong Kong, which is applicable to both the assured and the agent to insure. "The actual assured" approach ensures that under the new duty of disclosure, the person, who is responsible for the arrangement of the insurance, is subject to the new duty of disclosure. The new approach is in line with section 18(3) that only a single underwriter is subject to the knowledge. As a result, both parties to an insurance contract are equally treated under the duty.

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<sup>645</sup> Section 18(3)(d) concerns the law on insurance warranty in relation to the exemption of disclosure. IA 2015 has proposed a significant reform on the breach of warranty in commercial insurance contract. Nevertheless, the discussion of the reform of the breach of warranty is outside the scope of this thesis, and thus section 18(3)(d) remains in the MIO under the reform proposal.

The new approach is easy for the assured to understand and comply with the duty of disclosure. In the past, the MIO was ambiguous as to what constituted the knowledge that is deemed to be known by the assured. The new section 18(1)(b) avoids the ambiguity by stating that the assured is only deemed to know any information that is reachable by him or her through a reasonable search. The duty of reasonable search does not extend to the information that can be found on the Internet, as the information on the internet can be almost unlimited and the scope of the reasonable search can be indeterminable. For the information that is possessed by the assured's colleague, the actual assured, who is subject to the reasonable search requirement, still needs to disclose this information to the insurer, unless he or she can prove that a reasonable man in his or her position would not be able to access the information. If the actual assured cannot prove that he or she has no authority to access the concealed information, then he or she is still liable for the non-disclosure. The Hong Kong survey also found that 10 respondents agreed that the duty of reasonable search should be imposed in Hong Kong, with 4 respondents disagreeing and 5 respondents having no comment. Nevertheless, as a matter of fairness, the suggested new duty should be imposed on both parties to an insurance contract.

The operation of the "actual assured" approach is analysed in chapter 1 and chapter 5 of this thesis. It is a two-limb test to examine whether the assured/agent breaches the duty of disclosure. The first limb of the test is regarding whether the actual person, who is responsible for the arrangement of the insurance, possesses the material knowledge that is obliged to be disclosed to the insurer. The insurer needs to provide factual evidence to prove that the actual assured has, in fact, possessed the material information. The second limb of the test is related to whether the actual assured is deemed to know the concealed knowledge under the duty of reasonable search. Again, no presumption shall be imposed on the actual assured that he or she is deemed to know the concealed knowledge unless there is sufficient factual evidence proving the case. One of the examples is that the actual assured is well informed that the risk is managed by his colleague in the same office, but he or she has not inquired about the concealed knowledge. In this situation, the actual assured breaches the duty of reasonable search. The other example is that the agent breaches the duty of reasonable search if he or she knows that the concealed knowledge is possessed by the assured but chooses not to inquire about the concealed knowledge.

The next major change to the new section 18 regards the new materiality and inducement tests. With respect to the materiality test, a third-way approach is imposed, which is a hybrid of the prudent insurer test and the reasonable insured test. The examination of materiality involves a two-limb test. Firstly, the insurer has to prove that the concealed knowledge is something a reasonable assured would expect the insurer to know for the purpose of underwriting. Secondly, the insurer has to prove that he or she has acted as a prudent insurer to request the concealed knowledge. This new materiality test encourages an active exchange of information between the parties to an insurance contract. The first limb of the test ensures that the assured will not suffer from the detriment of the prudent insurer test, which even practitioners have failed to understand correctly at times. The second limb of the test ensures that the insurer cannot sit back and do nothing during the underwriting process. If the insurer wants to assess the risk fairly, he or she must identify what the information that he or she wishes to obtain is before the formation of the contract.

With respect to the new inducement test, the reform encourages the use of systematic criteria for the underwriting process. The example of a systematic underwriting system can be seen in *Drake Insurance v. Provident Insurance*,<sup>646</sup> where the motor insurance premium was calculated using a points system. This kind of system ensures that the insurer can only testify objectively for the degree of inducement that he has suffered from the non-disclosure. The insurer is also encouraged to keep a good record of the insurances that he has underwritten so that when he is required to prove inducement, he can rely on the record to prove the degree of inducement.

The use of the presumption of inducement is also limited to justifiable grounds under the new section 18(2)(b). One of the justifiable grounds is that the presumption is applicable to the following underwriters when the leading underwriter has proved actual inducement under a subscription policy. The other example is that the presumption is applicable when the actual underwriter is absent from the trial for a good reason, for instance, the actual underwriter refuses to testify because he or she is now working at another insurance company and there is a conflict of interest. Apart from the above two examples, the judge should apply the

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<sup>646</sup> *Drake Insurance* (n181)

presumption of inducement on a case-by-case basis, with the caution that the presumption will cause detriment to the assured if it is leniently granted.

The other major change observed in the proposed new section 18 is that the remedies of the breach are now different. In addition to the original remedy of avoidance, it imposes a new remedy to compensate the insurer by paying an additional premium, should the risk be fairly presented at the underwriting stage. The Hong Kong survey found that 10 respondents agreed that the proportionate remedies should be introduced in Hong Kong, although 3 respondents disagreed with the introduction of the proportionate remedies and 6 respondents had no comment on this issue.

It should be highlighted here that the “proportionate remedies” that are imposed in the new section 18 are significantly different from the ‘proportionate remedies’ that are imposed by the IA 2015. The new remedies raise the question of how proportionality should be defined in relation to utmost good faith/fair presentation cases. The Law Commission has not explained why a reduction of claim payments is proportionate to the loss of the insurer. The said proportionate remedy is now used by the Financial Ombudsman Service and is a default remedy for careless misrepresentation under the Consumer Insurance (Disclosure and Representation) Act 2012. Again, there is no discussion as to how such a reduction of claim payment is proportionate to the loss of the insurer.

The case law in England and Wales did not also offer an explanation of proportionality in relation to utmost good faith/fair presentation cases. In the Lloyd’s Insurance and Reinsurance Law Reports, there are 15 case reports that mentioned the terms “proportionality” and “good faith”. Nevertheless, none of the cases provided a detailed analysis of the proportionality principle. The typical use of the term was illustrated in the *Pan Atlantic v. Pine Top* case,<sup>647</sup> in which the term “proportionality” was mentioned as an opposite concept of the “all or nothing” remedy under section 17 of the MIA 1906, yet there was no discussion of what amounts to a proportionate remedy.<sup>648</sup> In *Drake Insurance plc v Provident Insurance plc*,<sup>649</sup> Rix L.J.

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<sup>647</sup> *Pan Atlantic* (n46)

<sup>648</sup> *ibid* 112

<sup>649</sup> *Drake Insurance* (n181)

suggested that the doctrine of proportionality involved “the process of balancing rights and wrongs”, but the said doctrine was not further elaborated on.<sup>650</sup> In *Sharon's Bakery (Europe) v AXA Insurance UK*,<sup>651</sup> Blair J suggested that the test of proportionality was relevant when determining the materiality of the concealed information in relation to the moral hazard of the assured.<sup>652</sup> The rest of the cases were not directly relevant to either the proportionality principle or utmost good faith.<sup>653</sup>

It is therefore submitted that the meaning of proportionality (in the context of insurance law) in relation to utmost good faith/fair presentation cases is not well-defined under English Law, but rather a matter of common sense that requires careful considerations and examination. Based on the analysis in chapter 4 of this thesis, it is submitted that the reduction in claim approaches over-compensates for the loss of the insurer in a case of the breach of the duty of fair presentation. The new section 18 introduces a new remedy for the insurer to seek an additional premium that the insurer should have charged if the risk was fairly presented. This appears to be more appropriately proportional to the loss of the insurer, and fairer to the assured. It is noteworthy that a similar remedy of charging an additional premium is also proposed by Airmic,<sup>654</sup> the International Underwriting Association of London<sup>655</sup>, and RSA Insurance plc<sup>656</sup> as an alternative remedy to the remedy of claim payment reduction under the IA 2015. These proposals suggest that the remedy of charging an additional premium is technically feasible in practice.

Furthermore, the new proportionate remedies do not under-compensate the insurer, because the insurer is still entitled to avoid the contract if, but for the breach, the insurer would not have entered into the insurance contract with the assured. The remedy of avoidance is still an

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<sup>650</sup> *ibid* [88]

<sup>651</sup> [2012] 1 Lloyd's Rep IR 164

<sup>652</sup> *Ibid* [62]

<sup>653</sup> These cases are: *Aldrich and Ors v Norwich Union* [2000] 1 Lloyd's Rep IR 1, *Barings Plc (n295)*, *Bonner v Cox Dedicated Corporate Member Ltd* [2005] 1 Lloyd's Rep IR 569, *Delaney v Pickett* [2013] 1 Lloyd's Rep IR 24, *Galloway v Guardian Royal Exchange (UK) Ltd* [1999] 1 Lloyd's Rep IR 209, *Greene Wood McLean v Templeton* [2011] 1 Lloyd's Rep IR 557, *Rogers v Merthyr Tydfil County Borough Council* [2006] 1 Lloyd's Rep IR 759, *Society of Lloyd's v Clementson* [1996] 5 Lloyd's Law Rep IR 215, *Travelers Casualty Surety v Sun Life Assurance* [2007] 1 Lloyd's Rep IR 619, *The "DC Merwestone"* [2015] Lloyd's Rep. IR 115 and *The "DC Merwestone"* [2016] Lloyd's Rep. IR 468

<sup>654</sup> Airmac, 'Insurance Act Clause', <<https://www.airmic.com/news/insurance-act-clause>> accessed 10 August 2018

<sup>655</sup> The International Underwriting Association of London, 'IUA09-066 Alternative Remedy for Breach of the Duty of Fair Presentation', <[iuclauses.co.uk/site/cms/contentDocumentView.asp?chapter=5](http://iuclauses.co.uk/site/cms/contentDocumentView.asp?chapter=5)> accessed 10 August 2018

<sup>656</sup> Policyfast, 'Business Car policy Booklet', <[https://www.bewiser.co.uk/sites/default/files/Policyfast%20Business%20Car%20RSA%20Policy%20Booklet%20March%202017\\_0.pdf](https://www.bewiser.co.uk/sites/default/files/Policyfast%20Business%20Car%20RSA%20Policy%20Booklet%20March%202017_0.pdf)> accessed 10 August 2018

effective way of protecting the insurer from an intentional breach the duty. The said remedy is also appropriate for the cases where the concealed fact is so important that it justifies the use of the remedy.

It is arguable that a harsher remedy may encourage the assured to take extra care to comply with the duty, and thus, the single remedy approach should not be abolished. Nevertheless, the duty of utmost good faith is already detrimental in the sense that it is too difficult for the assured to understand and comply with it. The main issue of the duty of utmost good faith is not about the degree of care that the assured needs to comply with the duty. Even if the assured wishes to comply with the duty, the scope of the duty is too wide, and the burden is too high for a reasonable assured to bear. It is argued that the harsh remedy can protect the insurer from the information asymmetry at the underwriting stage. Nevertheless, it is suggested that a fair presentation of the risk can only be achieved by complete cooperation between both parties to the insurance contract. The harsh remedy has the adverse effect of encouraging the insurer to sit back and do nothing. Therefore, a lenient remedy should be imposed, so that the insurer will take a more active role in exchanging information with the assured at the underwriting stage.

Another argument against the new section 18 is that since the “actual assured” approach will increase the administrative burden on the insurer, it may lead to an increase in the premium in general, which would be unfavourable to the assured. According to the Hong Kong survey, 1 respondent thought that the change in law will/would be very likely to affect the premium charged by the insurer and 9 respondents agreed that the change in law will/would be likely to affect the premium charged by the insurer. Furthermore, 6 respondents had no comment to make on this issue and 3 respondents thought that the change in law would be unlikely to affect the premium charged. Nevertheless, the main purpose of the reform is to ensure fairness between the parties to an insurance contract under the duty of utmost good faith/fair presentation. If money can buy fairness, it is certainly a fair cost that both parties are willing to accept. From a risk management perspective, the additional premium could also ensure that it is less likely for the insurer to avoid the insurance contract based on the single remedy approach of the old duty of utmost good faith under the MIO. In this regard, it is submitted that although the change of law may lead to an increase in the premium by the insurer, it may be a necessary cost that both parties need to bear for the sake of fairness.



### **C. New section 19 of the MIO in Hong Kong**

#### **i. The draft provisions of new section 19 of the MIO**

Section 19 is now omitted/repealed.

#### **ii. The explanatory note of new section 19 of the MIO**

The problem regarding section 19 of the MIO is examined in chapter 5 of this thesis. Section 19 is confusing because the agent's duty of disclosure appears to be an independent duty, but the insurer is not entitled to seek any independent remedy against the agent under the said duty. The so-called independent duty only authorises the insurer to seek a remedy against the assured. Furthermore, the agent's duty of disclosure has a very limited application in practice. In England and Wales, there were less than 20 cases that were concerned with the said duty during the past 100 years. In Hong Kong, there has been no case law that has been concerned with the said duty. According to the Hong Kong survey, 10 respondents had never dealt with a case that was related to the breach of the agent's duty of utmost good faith and just 5 respondents stated they had dealt with the case less than once a year. The survey indicated that most of the respondents had not dealt with cases in relation to section 19, and thus the adverse impact of repealing section 19 should be minimal.

### **D. New section 20 of the MIO in Hong Kong**

#### **i. The draft provisions of new section 20 of the MIO**

Section 20(1)

Every material representation made by the assured or his agent to the insurer during the negotiations for the contract, and before the contract is concluded, must be true. If it be untrue the insurer may be entitled to seek one of the following remedies:

- (a) The remedy of avoidance if, but for the breach, the insurer would not have entered into the contract of insurance at all, or
- (b) Additional premium if, but for the breach, the insurer would have entered into the contract with a higher premium.

Section 20(2)

A representation is material which a reasonable actual assured in the circumstances would have appreciated that the fact in question would be one that a prudent insurer would want to know about in fixing the premium, or determining whether he will take the risk.

Section 20(3)

A representation may be either a representation as to a matter of fact, or as to a matter of expectation or belief.

Section 20(4)

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.

Section 20(5)

A representation as to a matter of expectation or belief is true if it be made in good faith.

Section 20(6)

A representation may be withdrawn or corrected before the contract is concluded.

Section 20(7)

Whether a particular representation be material or not is, in each case, a question of fact.

Section 20(8)

For a claim of misrepresentation, the insurer/underwriter needs to prove that should the material misrepresentation not have been made, the insurer/underwriter would not have entered into the insurance contract, or would have entered into the insurance contract with additional premium.

**ii. The explanatory note of new section 20 of the MIO**

The new section 20 is almost identical to the new section 18, and thus most of the major issues have been examined in the previous sub-section. The only issue remaining is whether the materiality and inducement tests of non-disclosure are the same as the tests of misrepresentation under the new duty of fair presentation. In chapter 3 of this thesis, the author has already concluded that the materiality test and inducement test of non-disclosure and misrepresentation are the same, and these shall be followed under the new duty of fair presentation of this reform proposal. The new section 18(6) and the new section 20(8) are imposed to clarify that both duties share the same inducement tests.

### **III. The procedural guidance about the application of the new duty of utmost good faith/fair presentation**

The last section of this chapter provides guidance on the application of the new duty of utmost good faith/fair presentation in Hong Kong under the suggested reform proposal. Following this, the author will provide an overview of what the issues that need to be determined are, and on what basis these issues under the reform proposal are determined. It is noteworthy that the pros and cons of the reform proposal have already been examined in the previous 5 chapters and the previous sections of this chapter, and thus will not be repeated in the following sub-sections. The following sub-sections only provide procedural guidance about the application of the new duty under the reform proposal.

#### **A. The starting point: whether it is a case of utmost good faith or fair presentation?**

Under the reform proposal, the first issue that needs to be determined by the court is whether the dispute falls within the category of utmost good faith or fair presentation. The easiest way to determine this issue is to identify if the case is about a breach of the pre-contractual duty of disclosure or presentation by the assured, in which case it falls within the duty of fair presentation. The duty of fair presentation is governed by the new section 18 and 20 of the MIO. If the dispute is not about a breach of the pre-contractual duty of disclosure or presentation of the risk by the assured, then it falls within the duty of utmost good faith. The duty of utmost good faith is governed by the new section 17 of the MIO.

##### **i. When it is a case of fair presentation: is it a case of non-disclosure or misrepresentation?**

When the dispute is about the duty of fair presentation, the first thing that needs to be determined by the court is whether the dispute is related to non-disclosure or misrepresentation, since a non-disclosure case is governed by the new section 18 and a misrepresentation case is governed by the new section 20. It is noteworthy that non-disclosure and misrepresentation are always pleaded as an alternative pleading of each other, therefore it may make little practical significance to distinguish between these two duties. Nevertheless, these two duties are different in nature, thus there are two separate sections that govern these duties. It should be noted that the requirements for proving the breach of these two duties are identical to each other.

**a. When it is a case of non-disclosure: what are the issues that need to be determined?**

The first issue to be determined under the duty of disclosure is who is the actual person that is subject to the duty, and hence the knowledge of this person will be examined by the court to determine whether the assured is in breach of the duty. The identification of the responsible person is governed by the new section 18(1) of the MIO. In most of the cases, the responsible person will either be an employee of the assured company or an employee of the company of the agent to insure.

The second issue to be determined is whether the concealed knowledge is known or deemed to be known by the actual assured (or their agent). The court will examine the state of mind of the actual assured, and the insurer will need to factually prove that the assured possessed the concealed information but did not disclose it to the insurer. Alternatively, the insurer can argue that the assured did not comply with the duty of reasonable search, that is, according to the new section 18(1)(b), did not conduct a search or enquiry to the relevant parties inside and outside of the assured's company.

As a defence, the assured can argue that the insurer had failed to comply with the duty of reasonable search in accordance with the new section 18(3)(b). The insurer needed to have searched within its company to ensure that he or she had not missed any information about the assured that was possessed by the other underwriters within the same insurance company unless he or she could prove that such information was not accessible to him or her. The insurer also needs to ask the assured for any information that is missing, if the insurer becomes aware that this is the case during the underwriting process.

After it is determined that the knowledge was possessed by the actual assured, the next issues to be determined would be regarding the materiality and inducement tests. Under the reform proposal, to prove the materiality of non-disclosure, the insurer would need to satisfy a two-limb test under the new section 18(2)(a) and 18(4). The first limb of the test is regarding whether the concealed knowledge was something that a prudent insurer would want to know during the

underwriting process. The second limb of the test is regarding whether a reasonable assured is expected to know that the concealed information is material to the risk.

If the materiality is proved by the insurer under the prudent insurer test and the assured failed to raise a defence under the reasonable assured test, then the next issue to be determined is whether the insurer was induced by the concealed knowledge. The inducement test is governed by the new section 18(2)(b), which requires the insurer to prove the inducement with factual evidence, for example, the point system that was used in *Drake Insurance v. Provident Insurance*<sup>657</sup> or previous case records that demonstrated the insurers' practices. The presumption of inducement could only be granted with acceptable reasons; for example, the underwriter had resigned from the insurance company and refused to testify for the insurance company due to the conflict of interest.

After all the above issues are determined by the court and it has been confirmed that the assured is in breach of the duty of disclosure, the last issue to be determined would be the appropriate remedy for the insurer. The options of remedy are governed by the new section 18(1)(a). In a case where, but for the breach, the insurer would not have entered into the insurance contract, the insurer is entitled to avoid the contract. In a case where, but for the breach, the insurer would have accepted the risk but charged for a higher premium, the insurer is entitled to charge the additional premium that he would deem fair to charge if the risk had been assessed properly. It is noteworthy that the decision regarding an appropriate remedy is linked to the inducement test under the new section 18(2)(b). The insurer would need to provide factual evidence to prove the seriousness of the breach. If the insurer can only submit opinion evidence about the breach, then the court should consider the weight of the evidence and decide which remedy should be granted to the insurer.

**b. When it is a case of misrepresentation: what are the issues that need to be determined?**

The procedure of examining misrepresentation cases is the same as the procedure of examining non-disclosure cases. All the issues that are listed in the previous sub-section,

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<sup>657</sup> *Drake Insurance* (n181)

namely, the identification of the responsible person, the materiality and inducement tests, and the remedies are the same in both the new section 18 and 20. Therefore, examining the non-disclosure of a particular matter should lead to the same result as examining misrepresentation of the same matter. Furthermore, under the new section 17(2), the insurer is not entitled to seek a remedy against the assured for misrepresentation under both the MIO and the Misrepresentation Ordinance. The insurer is required to decide which route to take to sue against the assured, as the insurer is not allowed to benefit from the unjust privilege of trialling the same issue twice.

The application of the new duties of disclosure and misrepresentation can be further elaborated on by the below hypothetical case analysis. The assured, Company A, held a marine insurance policy for its vessel *Regent Water*. When Company A arranged the policy, the person responsible for Company A, Mr. B, failed to disclose that the master of the *Regent Water* (the shipmaster) had a criminal record for dangerous driving. *Regent Water* then suffered from a total loss due to perils of the sea. If the insurer had known about the criminal record of the shipmaster, he or she would merely have charged a slightly higher premium for the risk. Nevertheless, under the duty of utmost good faith of the MIO, the insurer was entitled to avoid the contract on the grounds of non-disclosure and misrepresentation. This case was detrimental to the assured because the non-disclosed fact was arguably irrelevant to the risk, but it could pass the materiality and inducement tests, as the criminal record of the shipmaster was certainly essential to the risk assessment. In addition, both Mr. B and the shipmaster might not have known that the driving conviction was disclosable to the insurer. As a result, the original duty of utmost good faith under the MIO could not ensure that the assured could be fairly treated.

The above detrimental situation could be remedied if the new duty of fair presentation of the reform proposal is adopted. First, the new materiality test requires the insurer to act prudently to request the information that is needed for the risk assessment. Since the criminal record of the shipmaster is important for the insurer, the insurer would certainly need to request that Mr. B provide the relevant information. Assuming that Mr. B knows about the shipmaster's driving conviction, Mr. B may have no idea about whether it is disclosable or not, therefore Mr. B can discuss this issue with the insurer. If Mr. B knows nothing about the conviction, then he must fulfil the duty of reasonable search and check the shipmaster's criminal record. In any case, the

new duty of fair presentation encourages more extensive and open communication between the parties to an insurance contract, which helps to prevent disputes arising from the exchange of information at the pre-contractual stage.

Furthermore, even if the insurer successfully proved that Mr. B had breached the new duty of fair presentation, the insurer would not be allowed to avoid the contract automatically. The insurer would need to prove that he would not have entered into the contract but for the breach of the duty. From the case fact, the insurer would only have charged a higher premium if he had learnt about the shipmaster's driving conviction. Under the new duty of fair presentation, the insurer would only be entitled to charge the additional premium that he or she had missed if the risk had been fairly presented. In this regard, it is submitted that the insurer would be properly compensated for what he or she deserved, the result of which is truly proportionate to both the assured and the insurer.

**ii. When it is a case of utmost good faith: what are the issues that need to be determined?**

The new duty of utmost good faith is now separated from the new duty of fair presentation. The new duty of fair presentation covers the pre-contractual disclosure and misrepresentation of the assured. The new duty of utmost good faith covers all the conducts of the parties to an insurance contract other than the pre-contractual non-disclosure and misrepresentation of the assured.

The new duty of utmost good faith has no fixed scope and is intended to be imposed with flexibility, as it is the court's responsibility to develop the scope and to apply such a duty when the court deems it to be fit. One example of this kind of duty is when the assured purchases marine insurance from the insurer, the insurer knows that the insured ship has already arrived at the destination but chooses not to disclose this information to the assured. The other possible application is the post-contractual conduct of the assured. The new section 17 is imposed as a measure to cope with the future development in this area of law, and thus, further judicial development is expected for the application of this section. The application of it, therefore, can only be examined on a case-by-case basis, and no fixed procedural guidance can be provided.

#### **IV. Conclusion**

To conclude, the most controversial aspect regarding the reform approach lies in the default regime approach, but the debate behind this approach is a struggle between the freedom of contract and a Parliamentary intervention. This, however, is an endless debate. It is evident that freedom of contract cannot ensure fairness between the parties, and that is the reason why legislations such as the Unfair Contract Terms Act 1977 and the Consumer Rights Act 2015 were enacted to regulate the use of contractual terms in a reasonable and fair sense. Legislative intervention, on the other hand, should only be made cautiously. The author suggests that the reform proposal for the Hong Kong legislation shall not impose the “contracting out” clauses that may encourage the parties to contract out of the duty of utmost good faith/fair presentation, but the parties are always entitled to exclude the duty of utmost good faith/fair presentation by imposing relevant terms to the insurance contract.<sup>658</sup>

Further, the “contracting out” approach is strongly against the purpose of the reform that is proposed by the author. The proposed reform contemplates the law from the assured’s perspective and aims to change the law that has been insurer-friendly for the last 100 years. In this regard, it is submitted that the default regime approach itself has no problem, but it is not desirable for the reform proposal, which aims to achieve true fairness between the parties to an insurance contract by reforming the duty of utmost good faith/fair presentation.

The draft provisions of the reform are analysed in the above sections. These new provisions aim to preserve the advantages of both the MIA 1906 and the IA 2015. The draft provisions take reference from the IA 2015, but most of the changes are tailor-made for the Hong Kong context, as it is evident that the IA 2015 fails to address the problems of the MIA 1906 and the MIO. In fact, the question of whether the IA 2015 should be followed as part of Hong Kong law reform is a controversial issue. According to the Hong Kong survey, 6 respondents thought that the Hong Kong law reform should follow the IA 2015, whereas 6 respondents thought that the reform should be independent from the IA 2015, and 7 respondents had no comment on this issue. The survey result shows that there is no agreed view on this issue. Nevertheless, in answer to the question of “to what extent the change of law in England and Wales affected your daily

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<sup>658</sup> See, for example, Baris Soyer, ‘Reforming pre-contractual information duties in business insurance contracts - one reform too many?’ [2009] J.B.L. 15, page 31



practice”, most of the respondents (13 respondents) answered neither agree nor disagree. It is suggested that to some extent, the Hong Kong market is already detached from the UK insurance market, and the approach of adopting the IA 2015 in Hong Kong may not be as desirable as expected. In this regard, it may now be a suitable time for Hong Kong to develop its own law reform for the duty of utmost good faith/fair presentation and deviate from English Law.

## Conclusion

Insurance is *uberrimæ fidei*. The duty of utmost good faith was introduced by Lord Mansfield in *Carter v Boehm* over 250 years ago.<sup>659</sup> Nowadays, the duty still survives in many jurisdictions, but in most of the jurisdictions the forms of the duty are different from their origin in English law. Hong Kong is one of the rare cases in which the duty of utmost good faith remains the same as its origin in English law before the enactment of the IA 2015. This thesis heavily criticised the duty of utmost good faith, as well as the MIA 1906/MIO. However, this thesis does not intend to undermine the significance of the duty of utmost good faith. Lord Mansfield offered the best way to protect the insurer from information asymmetry with a harsh but clear legal duty. Sir Mackenzie Chalmers codified the duty of utmost good faith in the MIA 1906, which radically improved the accessibility of the said duty. Even until recently, there have been those that believe the MIA 1906 works well and that reform is unnecessary. For example, the Commercial Bar believed that the MIA 1906 developed a high degree of certainty for commercial insurance law, and that the common law system has proved to be capable of coping with future changes. Therefore, a reform is unnecessary, but the adverse effect of the reform is obvious. It will destroy the certainty that has been developed for over 250 years and it may take a considerably long time to recover from the damage that is caused a change in the reform.<sup>660</sup> In fact, it is totally reasonable to argue that the MIA 1906/MIO and the duty of utmost good faith are still feasible for the modern insurance market. Nevertheless, it is also equally true that the duty of utmost good faith is not as feasible as when it was first introduced by Lord Mansfield in the 18<sup>th</sup> century. With the use of the internet, the transfer of information is now much faster and more complicated. The exchange of information between the insurer and the assured is no longer the same as it used to be in the 18<sup>th</sup> century, and society and people are changing. As a result, the utmost good faith, of course, also needs to be changed.

The question is, therefore, what people want to achieve in the name of utmost good faith in the 21<sup>st</sup> century. The Law Commission has given its own answer in the IA 2015, which has seen a number of changes. Firstly, the IA 2015 has imposed a new duty of fair presentation to replace the duty of utmost good faith. This new duty of fair presentation has introduced new protections

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<sup>659</sup> *Carter* (n1)

<sup>660</sup> House of Lords (n83) page 91, para 29

for the insurer; for example, “Data dumping” from the assured is banned and a vague “reasonably clear and accessible” manner is imposed on the assured’s presentation of risk. Furthermore, a new duty of reasonable search has been imposed on the assured, as the scope of pre-contractual disclosure by the assured is arguably wider than before. In the author’s view, the enactment of the IA 2015 has not solved the major problems that existed under the duty of utmost good faith under the MIA 1906. It is suggested that the duty of fair presentation is still insurer-friendly and inaccessible to the assured. For example, the Federation of Small Businesses highlighted that under the IA 2015, some of the new sections related to the duty of fair presentation were simply not understandable by the assured.<sup>661</sup> In fact, one may reasonably point out that the new provisions under the IA 2015 are no easier to understand than the old provisions under the MIA 1906. The accessibility of the duty has been a matter of dispute for the last 250 years, and, unfortunately, the IA 2015 has failed to improve the situation. This insurer-friendly approach of the IA 2015 certainly discourages companies from all over the world to purchase commercial insurances in a country where the law is arguably unfair to the assured. This thesis, therefore, aims to change the unfair situation and provide an alternative reform proposal that is more assured friendly. The author believes that the reform proposal is more suitable for the global market, which is more customer-driven, and Hong Kong is a good example that fits with the reform proposal.

Chapter 1 of this thesis considered the knowledge requirement of the duty of disclosure, and chapter 2 considered the materiality and inducement tests of the duty of disclosure. The duty of disclosure is imposed to protect the insurer from the information asymmetry. The rationale behind the measure is that the assured is in a better position to obtain information that is material to the risk, and thus, as a matter of fairness, the material information should be disclosed to the insurer fairly for the purpose of risk assessment. Ironically, it is suggested that the current law has created a new type of information asymmetry. Under the duty of disclosure, the insurer is in a better position to judge the scope of knowledge that is disclosable for the purpose of risk assessment. The materiality and inducement tests only consider the evidence from the insurer’s perspective, and the view of the assured is irrelevant to the tests. In other words, the insurer is in a privileged position with respect to its professional knowledge that

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<sup>661</sup> *ibid* page 93, para 1 and 2.

concerns the insurance practice, which is suggested to be another form of information asymmetry. While the insurer is well-protected under the duty of disclosure, the current law has not considered the detriment that the assured has suffered from the “new information asymmetry”. In the author’s view, the duty is simply incomprehensible to a reasonable assured.

In chapter 1, the author suggested to reform the knowledge requirement of the duty of disclosure by adopting the actual assured approach and imposing a new duty of reasonable search, which aimed to redefine the scope of knowledge that is disclosable by the assured under the law. In chapter 2, the author suggested to reform the materiality test by imposing a third-way test, which is a hybrid of the prudent insurer test and the reasonable insured test. The author also suggested to reform the inducement test by imposing new provisions that govern the operation of the inducement test. It is suggested that an effective communication is the only solution to the problem of information asymmetry, and the reform proposal encourages the insurer to communicate with the assured proactively to prevent non-disclosure at the pre-contractual stage.

Chapter 3 considered the problems of the duty not to misrepresent. The problems in this chapter were straightforward. The inducement tests of non-disclosure and misrepresentation are missing from the MIO, and thus there is a risk that the inducement tests can be misinterpreted. The solution of this problem, as suggested in chapter 3, was that a written inducement test should be imposed in the MIO to clarify the operation of the test. Furthermore, several cases in England and Wales suggested that the insurer could take unjust privilege to plead misrepresentation under the Misrepresentation Act 1967 as an alternative pleading of misrepresentation under the MIA 1906. To prevent the same problem happening in Hong Kong, the author suggested to impose a new provision in the legislation to forbid the application of the Misrepresentation Ordinance in the utmost good faith/fair presentation cases.

Chapter 4 considered the problems of the remedies for the breach of the duty of utmost good faith/fair presentation. The first section of chapter 4 identified the problem that the remedy of avoidance is inadequate for the assured in the case where the breach is committed by the insurer. To solve this problem, it is suggested that the remedy of damages should be imposed in section 17 of the MIO as an alternative of the remedy of avoidance. Nevertheless, in the

author's view, the core problem of this chapter lies in the principle of proportionality. Proportionality has different meanings in different contexts, and this thesis only examined the principle in the context of utmost good faith/fair presentation cases. The fundamental principle of proportionality, which the author tried to establish in this thesis, is that the remedy should be proportionate to the loss. The author suggested that this principle should be adopted as a guiding principle of reforming the duty of utmost good faith/fair presentation in Hong Kong. The single remedy approach under the MIO does not comply with the principle because it disregards the seriousness of the breach of the duty. Furthermore, the proportionate remedies, which are imposed by the Law Commission in the IA 2015, also do not comply with the principle. The reason is that one of the remedies allows the insurer to reduce claim payments in proportion to the premium that he would have charged if the risk was fairly presented. This remedy, in the author's view, overcompensates the loss of the insurer. Therefore, the author suggested to impose the new proportionate remedies, which consist of the remedy of avoidance and the remedy of charging additional premium, for the breach of the pre-contractual duty regarding section 18 and 20 of the MIO. One of the new remedies allows the insurer to charge a higher premium as an alternative of the remedy of avoidance. It is suggested that this new remedy complies with the principle of proportionality, as the loss of the insurer, in the case where the breach is not serious enough to justify the use of the remedy of avoidance, is no more than the loss of additional premium.

Chapter 5 considered the agent's duty of disclosure. It is suggested that the agent's duty and the assured's duty are the two sides of the same coin. Nevertheless, the application of the agent's duty is complicated by section 19 of the MIO, which gives the impression that the agent's duty is independent from the assured's duty. This, coupled with the fact that the agent's duty is rarely used in Hong Kong, suggests that the best solution for the problem is that the agent's duty should be merged with the assured's duty, and thus, section 19 of the MIO should be abolished.

Chapter 6 formulated a reform proposal for the duty of utmost good faith/fair presentation in Hong Kong. The reform proposal may be criticised for being too assured-friendly, but the main theme of the reform is about accessibility and fairness. This thesis has criticised the duty of utmost good faith/fair presentation for being unfair and inaccessible to the assured, and the

proposed reform aims to provide a fairer and more accessible duty of utmost good faith/fair presentation. The reform proposal is made based on the situation in Hong Kong, but it could also be adopted in other jurisdictions including England and Wales,<sup>662</sup> as the parties to an insurance contract are allowed to contract out of the duty of fair presentation under the IA 2015. The author hopes that this thesis can convince the reader of the fact that utmost good faith is not and should not be a fixed concept for all time and places. In the modern era, the assured can always do “forum shopping” and choose a jurisdiction that is more customer friendly. In this regard, it is submitted that an assured friendly utmost good faith may be a more feasible choice for the 21<sup>st</sup> century insurance market.

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<sup>662</sup> The other jurisdiction that may be suitable to adopt the reform proposal of this thesis is Singapore. Singapore is also facing a situation that is similar to Hong Kong in relation to the duty of utmost good faith in commercial insurance law. For the current situation in Singapore, please see H.Y. Yeo and Yaru Chia, ‘The morphing duty of good faith and disclosure: lessons for Singapore’ [2018] JBL 425

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## Annex 1 49 Insurance Cases In Relation To The Inducement Tests After The Decision Of The *Pan Atlantic*

Case name	Different results?	Different inducement tests?	Case summary and the inducement test of the case
<p><i>St Paul Fire v McConnell</i> [1995] 4 Re LR 293</p>	No	No	<p>Construction of buildings not supported on piles (deep foundations) but on (shallow) spread foundations, and results in a subsidence damage.</p> <p>Inducement tests: What the insurer would have done if the true fact (the foundation and ground condition) was told to the insurer. (p.301)</p>
<p><i>Gate v Sun Alliance</i> [1995] LRLR 385</p>	No	No	<p>The insurer refused the claim based on non-disclosure of the existence of the owners of the vessel other than the assured, non-disclosure of fraud and dishonesty of the assured, and non-disclosure and misstatement of the purchase price of the vessel (the actual value was lower than the value that was stated in the policy). The inducement tests were not discussed in this case (p.398-400)</p>

<p><i>GMA v Storebrand</i> [1995] LRLR 333</p>	<p>No</p>	<p>No</p>	<p>Reinsurance case. Misrepresentation of the type of business that the company was running. Non-disclosure of the existence of the four stop loss contracts.</p> <p>No evidence of inducement so there was no discussion about the inducement tests. (p.350)</p>
<p><i>Hill v. Citadel Insurance</i> [1995] LRLR 218</p>	<p>No</p>	<p>No</p>	<p>Reinsurance case. Non-disclosure and misrepresentation of the amount of the excess of the loss protection policy. Inducement tests were not discussed as the plaintiff admitted inducements.</p> <p>Inducement tests: “An underwriter would have been induced if the misrepresentation or non-disclosure materially affected the decision.” (page 233)</p>
<p><i>SAIL v Farex</i> [1995] LRLR 116</p>	<p>No</p>	<p>No</p>	<p>Reinsurance case. Misrepresentation of the existence of retrocession cover. Non-disclosure of the coverage of the policy. Non-disclosure and misrepresentation of the claim history. The inducement tests were not discussed. (p.124,126)</p>

<i>Hume v AA</i> [1996] LRLR 19	No	No	The defendant applied for a stay of action and the court held that the defendant was entitled to the stay. Non-disclosure and misrepresentation were not examined in this case, and inducement tests were not discussed.
<i>Agnew v Länsförsäkringsbolagens AB</i> [1997] 6 Re LR 33	No	No	Non-disclosure and misrepresentation were discussed within the context of Article 5 of the Lugano Convention. Non-disclosure and misrepresentation were not examined in this case, and inducement tests were not discussed.
<i>Manifest Shipping v Uni-Polaris Shipping</i> [1997] 6 Re LR 175	No	No	Fire accident on <i>the Star Sea</i> . Utmost good faith ended after the commencement of the proceedings, and therefore all utmost good faith claims against the witness statement and expert report failed. Inducement tests were not examined in this case.
<i>Home Ins Co of Il v Spectrum Info Tech</i> [1997] 6 Re LR 1	No	No	Whether Directors and Officers Insurance was similar to marine insurance. Whether the insurer was entitled to a remedy under the duty of utmost good faith. The court held that the D&O was not similar to marine insurance. Inducement tests were not discussed in this case.

<i>Royal Boskalis v. Mountain</i> [1997] LRLR 523	No	No	Whether the insurer was allowed to avoid the contract on the grounds of non-disclosure and misrepresentation after the conclusion of the contract. The inducement tests discussed were beyond the scope of section 18 and 20.
<i>Mander v Commercial Union Assurance Co Plc</i> [1998] Lloyd's Rep IR 93	No	No	Validity of marine open cover reinsurance contract. Non-disclosure and misrepresentation were pleaded in relation to the prudential covers and broker's liability. The relevant judgment was obiter judgment only. No detailed discussion on inducement tests, yet the court held that non-disclosure and misrepresentation existed.
<i>Kingscroft &amp; Ors v Nissan Fire &amp; Marine (No 2)</i> [1999] Lloyd's Rep IR 603	No	No	Reinsurer pleaded non-disclosure and misrepresentation in relation to the share of the whole account quota and the pools retention. No express definition was provided for the inducement tests.
<i>KS Merc-Scandia v Certain Lloyd's Underwriters &amp; Ors</i> [2001] Lloyd's Rep IR 802	No	No	Open cover marine insurance. The insurer's pleaded a breach of the post-contractual duty of utmost good faith and the condition of notice of claim by the assured. Inducement tests were not discussed in detail.

<i>Odyssey Re (London) Ltd and Anor v OIC Run-off Ltd</i> [2001] Lloyd's Rep IR 1	No	No	Reinsurance perjury case. Irrelevant to utmost good faith in the context of insurance law.
<i>International Lottery Management Ltd v Dumas and Others</i> [2002] Lloyd's Rep IR 237	No	No	Political risk policies. Non-disclosure and misrepresentation in relation to the authorisation of running lottery business from the Azerbaijan Government. Inducement tests were not expressly stated in the judgment.
<i>Feasey v Sun Life Assurance Co of Canada</i> [2002] Lloyd's Rep IR 807	No	No	Reinsurance of life and personal injury insurance. Whether false statements were made in relation to the payments. Non-disclosure and misrepresentation were not distinguished and inducement tests were not expressly stated.
<i>Agapitos v Agnew and Others</i> [2002] Lloyd's Rep IR 573	No	No	Whether fraudulent claim fell within the jurisdiction of section 17 of MIA. Inducement test was not discussed in the context of non-disclosure or misrepresentation.
<i>Brotherton v Aseguradora Colseguros SA (No 2)</i> [2003] Lloyd's Rep IR 746	No	No	Non-disclosure of a report that was related to the misconduct and criminal allegation against the president of the assured bank.

			<p>Inducement test: "Whether a material non-disclosure induced the actual underwriter to act to his prejudice depends likewise upon whether the circumstances withheld would, if known, have caused him to act differently, either by not writing the insurance at all or by only writing it on different terms. "(para 18) Misrepresentation was not discussed in this case.</p>
<p><i>New Hampshire Insurance Co v Oil Refineries Ltd</i> [2003] Lloyd's Rep IR 386</p>	No	No	<p>Non-disclosure of a large sum of outstanding third-party liability claims. The court held that there was a non-disclosure and the insurer was entitled to avoid the contract.</p> <p>Inducement test: "I cannot say how much more Mr Higgins would have charged if he had known of the flower growers' claim, but I do know that it would have been more, and that is enough. "(para 45) Misrepresentation was not discussed in this case.</p>
<p><i>Moore Large &amp; Co Ltd v Hermes Credit &amp; Guarantee Plc</i> [2003] Lloyd's Rep IR 315</p>	No	No	<p>Non-disclosure of the level of indebtedness of the claimant. The insurer waived the right of avoidance.</p> <p>Inducement test: "In the field of non-disclosure inducement is</p>

			to be tested by ordinary principles of the law of misrepresentation.” (para 67) In other words, no distinction was made between the inducement tests.
<i>Assicurazioni Generali SpA v ARIG</i> [2003] Lloyd's Rep IR 131	No	No	Non-disclosure of abnormal reserving policy and misrepresentation of the participation of the parties to the business and also the loss statistics.  Inducement tests: “He must therefore show at least that, but for the relevant non-disclosure or misrepresentation, he would not have entered into the contract on those terms.” (para 62)
<i>Wise Ltd v Grupo Nacional Provincial SA</i> [2004] Lloyd's Rep IR 764	No	No	Rolex watch was presented as a clock due to mistranslation.  The court held that there was a non-disclosure. Misrepresentation on the issue of cancellation was rejected but it was a different issue.  Inducement test: “Mr Bennett had given evidence at trial that had he known that the risk he was being asked to cover included the carriage of watches, he would not have written the risk.” (para97)



<i>Interpart Comercio e Gestao SA v Lexington Ins Co</i> [2004] Lloyd's Rep IR 690	No	No	Falsely inserted a date in a certificate of cargo inspection. Application of summary judgment. Summary judgment rejected. Inducement tests were not discussed in this case.
<i>Frans Maas (UK) Ltd v Sun Alliance and London Insurance Plc</i> [2004] Lloyd's Rep IR 649	No	No	Pleading of non-disclosure, in relation to the goods that were delivered without bills of lading, was failed. Misrepresentation was not discussed in this case.
<i>Drake Insurance plc v Provident Insurance plc</i> [2004] Lloyd's Rep IR 277 (CA)	No	No	Non-disclosure of previous speeding conviction. Misrepresentation was not discussed in this case.
<i>International Management Group (UK) Ltd v Simmonds</i> [2004] Lloyd's Rep IR 247	No	No	Non-disclosure and misrepresentation of materials that were related to the government permission of the cricket matches between India and Pakistan.  Inducement test: "Their approach to underwriting, as set out earlier in this judgment when dealing with materiality, shows how they would have been influenced if proper information had been given to them about Government permission in particular." (para 147)

<p><i>Eagle Star Insurance Co Ltd v Games Video Co</i></p> <p>[2004] Lloyd's Rep IR 867</p>	<p>No</p>	<p>No</p>	<p>Non-disclosure and misrepresentation of the value of the vessel.</p> <p>Inducement test: "Mr Bridges (the insurer's underwriter) said that he would not have accepted the risk if he had known there was an 'extreme overvaluation'. This evidence was both credible and consistent with the expert evidence and I therefore find that the insurer relied on the representation." (para 123)</p>
<p><i>Bonner v Cox Dedicated Corporate Member Ltd</i></p> <p>[2005] Lloyd's Rep IR 569</p>	<p>No</p>	<p>No</p>	<p>Non-disclosure of the loss records, misrepresentation of the duration and nature of the risks.</p> <p>Inducement test: This issue involves asking a hypothetical question, namely what, probably, would have happened had disclosure of the Elk Point loss been made to Mr Woodgate on or soon after 8 December 1998. (para 103)</p> <p>No distinction was made for the inducement test of misrepresentation.</p>
<p><i>O'Kane v Jones</i></p> <p>[2005] Lloyd's Rep IR 174</p>	<p>No</p>	<p>No</p>	<p>Non-disclosure of the nature of the risk and default payment of the premium. Inducement test: "I was not satisfied that Mr</p>

			Kent would have declined the risk or insisted on different terms on 16 December 1999 had he been told of the premium payment problems on the 2020 Policy, or indeed of the fact that ABC were owed a substantial sum of money by Nanice.” (para 235) No distinction was made between the two inducement tests.
<i>Markel v La Republica</i> [2005] Lloyd's Rep IR 90	No	No	Application of the stay of proceedings. Misrepresentation of prior misconduct of the broker, premium skimming, market nature and the information about the assured's income and insurance history. The court held that there was a triable case and the application was denied. Inducement tests were not examined.
<i>Goshawk Dedicated Ltd v ROP Inc</i> [2006] Lloyd's Rep IR 711	No	No	Anti-suit injunction. Utmost good faith was not examined in this case.
<i>Talbot Underwriting v Nausch, Hogan &amp; Murray</i> [2006] Lloyd's Rep IR 531	No	No	Non-disclosure of the principal of the policy. Misrepresentation was not discussed in this case. Inducement tests were not discussed in this case.

<i>North Star Shipping v Sphere Drake Insurance</i> [2006] Lloyd's Rep IR 519	No	No	Non-disclosure and misrepresentation of the legal proceedings and overvaluation. Inducement tests were not distinguished by the judges.
<i>Mundi v Lincoln Assurance Ltd</i> [2006] Lloyd's Rep IR 353	No	No	Non-disclosure of the medical consultation and drinking habit of the assured. Misrepresentation was not discussed.
<i>Micro Design v Norwich Union</i> [2006] Lloyd's Rep IR 235	No	No	Non-disclosure in relation to the cancellation of the previous policy due to the default payment of the premium. Misrepresentation was not discussed.  Inducement test: "What would NU have done if the claimants had disclosed to NU that the St Paul's policy had been cancelled?" (para 101)
<i>Noblebright Ltd v Sirius International Corporation</i> [2007] Lloyd's Rep IR 584	No	No	Non-disclosure of the incidents without claims. Misrepresentation was not discussed in this case. Inducement tests were not discussed.
<i>Zeller v British Caymanian Insurance</i> [2008] Lloyd's Rep IR 545	No	No	Non-disclosure of the heart condition of the assured. Misrepresentation was not discussed. Inducement tests were not distinguished in this case.

<i>Laker Vent Engineering v Templeton Insurance</i> [2009] Lloyd's Rep IR 704	No	No	Non-disclosure of prior arbitration in relation to progress of work and payment between the assured and a third party. Misrepresentation was not discussed. The inducement tests were not distinguished. The underwriter did not give any evidence, so the inducement tests were not discussed. (para 69)
<i>Crane v Hannover</i> [2010] Lloyd's Rep IR 93	No	No	Misrepresentation and non-disclosure of the underwriting practice. Inducement test: "There is no distinction, for the purpose of establishing inducement, between the requirement of causation as it relates to misrepresentation and as it relates to non-disclosure." (Annex 1 para 19)
<i>Direct Line Insurance v Fox</i> [2010] Lloyd's Rep IR 324	No	No	A fraudulent claim case which was irrelevant to utmost good faith. Inducement test was not discussed.
<i>A C Ward v Catlin (Five)</i> [2010] Lloyd's Rep IR 695	No	No	Non-disclosure and misrepresentation of the Risky Improvement Requirement. Inducement tests: "What in my judgment would not have happened, if Mr McAndrew had been told the true position on 20 February 2007, is that he

			would simply have lifted the endorsement without imposing terms. Accordingly, I am satisfied that Mr McAndrew was induced by material misrepresentation or non-disclosure to lift the endorsement and vary the contract of insurance.” (para 232)
<i>Persimmon Homes v Great Lakes</i> [2011] Lloyd's Rep IR 101	No	No	Non-disclosure and misrepresentation of the dishonest conduct. The inducement tests were not distinguished.
<i>Stansfield v Consumers' Assoc of Singapore</i> [2012] Lloyd's Rep IR Plus 13	No	No	Post contractual duty of utmost good faith. Inducement tests were not discussed in the context of non-disclosure and misrepresentation.
<i>Bate v Aviva Insurance UK Ltd</i> [2014] Lloyd's Rep. IR 527	No	No	Misrepresentation. The insured building was not used for business purposes. Non-disclosure of on-going construction of the building. Misrepresentation of the previous loss. Inducement tests were not distinguished (para 29)
<i>Sea Glory Maritime Co and Another v AL Sagr National Insurance Co (The "MV Nancy")</i> [2014] Lloyd's Rep IR 112	No	No	Non-disclosure and misrepresentation of the manager of the vessel, previous detention and conflict of interest. Inducement tests were not distinguished.

<p><i>Versloot Dredging BV and Another v HDI Gerling Industrie Versicherung AG and Others (THE “DC Merwestone”)</i></p> <p>[2016] Lloyd's Rep. IR 468</p>	No	No	Fraudulent claim case. Inducement tests were not discussed in the context of non-disclosure and misrepresentation.
<p><i>Involnert Management Inc v Aprilgrange Ltd and Others Ais Insurance Services Ltd (First Third Party) Oamps Special Risks Ltd (Second Third Party)</i></p> <p>[2015] Lloyd's Rep. IR 661</p>	Yes	Yes	Non-disclosure and misrepresentation of the value of the vessel. The inducement tests were distinguished by the judge.
<p><i>Axa Versicherung Ag v Arab Insurance Group (BSC)</i></p> <p>[2015] Lloyd's Rep. IR Plus 31</p>	No	No	Non-disclosure and misrepresentation of the loss statistics. Inducement tests were not distinguished.
<p><i>Brit Uw Ltd v F &amp; B Trenchless Solutions Ltd</i></p> <p>[2016] Lloyd's Rep. IR 69</p>	No	No	Non-disclosure and misrepresentation of a void under the railway line. No distinction was made between the inducement tests. (para 113, para 159-163)

## Annex 2 97 Insurance Cases In Relation To Utmost Good Faith After The Decision of the *Pan Atlantic*

Case Name	Intention (Intentional/ Innocent/ Not identified)	Contract avoided?	Summary
<i>A C Ward v Catlin (Five)</i> [2010] Lloyd's Rep IR 695	Not identified	Yes	Cigarettes and tobaccos stolen from warehouse. Misrepresentation and Non-disclosure of failure to comply with security recommendations. The court held that the assured was liable due to the fault of the broker. Although the intention was not identified, the credibility of the broker was heavily criticized by the judge. (para 8,9, 10 and 226)
<i>Agapitos v Agnew and Others</i> [2002] Lloyd's Rep IR 574	Intentional	N/A	Fire accident due to hot work on deck. Vessel total loss. Insurer contended fraudulent claim and the breach of the post-contractual duty of utmost good faith for the commencement date of the hot work. The court refused the application for permission to amend the defence from the breach of warranty to the breach of utmost good faith as the lie was not material. The court held that the assured was telling a lie in relation to the commencement date of the hot work. (para 10)



<p><i>Agnew</i> v <i>Länsförsäkringsbolagens</i> [2000] Lloyd's Rep IR 318</p>	<p>Not identified</p>	<p>N/A</p>	<p>Guarantee insurance to supply underwater valves in the oilfield. Misrepresentation was made in relation to the condition of the valves. The court dismissed the action of setting aside the writ. Matters in relation to the application of the Lugano Convention and utmost good faith was not examined in detail.</p>
<p><i>Aldrich and Ors v Norwich Union</i> [2000] Lloyd's Rep IR 1</p>	<p>Innocent</p>	<p>No</p>	<p>Endowment/life policy. Non-disclosure of financial loss at Lloyd's. The court held that there was no -non-disclosure. No fraud was identified. (page 8)</p>
<p><i>Alfred McAlpine Plc v BAI (Run-Off) Ltd</i> [2000] Lloyd's Rep IR 321</p>	<p>Innocent</p>	<p>No</p>	<p>Contractor policy. Injury of worker. Fail to notify the insurers for the claim. The court held that there was no dishonesty. (para 21)</p>
<p><i>Anders &amp; Kern UK Ltd v CGU Insurance plc</i></p>	<p>Innocent</p>	<p>No</p>	<p>Retail and wholesale policy. Burglary at the warehouse. The assured contended that there was an implied term for the insurer to relax the requirement of security for the warehouse.</p>

[2007] Lloyd's Rep IR 555			The court held that there was no such an implied term and the insurer was in good faith. (para 33)
<i>Ansari v New India Assurance</i> [2009] Lloyd's Rep IR 562	Intentional	Yes	Fire insurance. Non-disclosure of the fact that the sprinkler system was not working. The court held that the assured was liable and aware of the condition of the sprinkler system. (para 50)
<i>Assicurazioni Generali SpA v ARIG</i> [2003] Lloyd's Rep IR 131	Not identified	No	Non-disclosure of abnormal reserving policy and misrepresentation of the participation of the parties to the business and also loss statistics. The court held that there was no actionable non-disclosure or misrepresentation. Judges had different opinions on the intention of the non-disclosure and misrepresentation (para 67, 70, 72, 202 and 211) For the purpose of data collection, this case is classified as "Not identified", as there is no clear cut for the intention of the breach. It is neither fraudulent nor innocent.
<i>Aviva Insurance v Brown</i> [2012] Lloyd's Rep IR 211	Intentional	N/A	Property Insurance. Fraudulent claim of accommodation cost. Post-contractual duty was involved but not examined in detail. (para 98)
<i>Axa Versicherung AG v Arab Insurance Group (BSC)</i> [2016] Lloyd's Rep IR 1	Innocent	No	Non-disclosure and misrepresentation of loss statistics. The court held that there was no non-disclosure and misrepresentation. (para 214)

<i>Baghbadrani v Commercial Union Assurance Co Plc</i> [2000] Lloyd's Rep IR 94	Intentional	No	Material damages and business interruption policy. Fire accident. The assured provided fraudulent quotation and wrong number of students. The court held that the claim was fraudulent. (page123-124) Utmost good faith was discussed at the claims stage (page 101).
<i>Bate v Aviva Insurance UK Ltd</i> [2014] Lloyd's Rep IR 527	Intentional	Yes	Property Insurance. Fire accident. Failure to disclose the use and work status of the property. Misrepresentation of the previous loss. The court held that the assured was liable for misrepresentation and non-disclosure, and the presentations were fraudulent. (para 53)
<i>Bonner v Cox Dedicated Corporate Member Ltd</i> [2005] Lloyd's Rep IR 569	Innocent	No	Reinsurance. Non-disclosure of loss records, misrepresentation of duration and nature of the risks. The court held that the reassured was not liable to the breach. (para 363)
<i>Brit UW Ltd v F &amp; B Trenchless Solutions Ltd</i> [2016] Lloyd's Rep IR 69	Intentional	Yes	Non-disclosure and misrepresentation of a void under the railway line. The court held that the assured was liable for the breach, and the assured was aware of the non-disclosed information. (para140)
<i>British-American Insurance (Kenya) Ltd v Matelec SAL</i> [2014] 1 Lloyd's Rep IR 287	Not identified	N/A	A case of whether the arbitration clause extended to the insurance contract. Utmost good faith was mentioned but not examined.

<p><i>Brotherton v Aseguradora Colseguros SA (No 2)</i> [2003] Lloyd's Rep IR 746</p>	<p>Not identified</p>	<p>N/A</p>	<p>Refer to <i>Brotherton v Aseguradora Colseguros SA (No 3)</i> for the case summary. This case challenged the validity of the allegation against the president, and the attempt was unsuccessful.</p>
<p><i>Brotherton v Aseguradora Colseguros SA (No 3)</i> [2003] Lloyd's Rep IR 762</p>	<p>Intentional</p>	<p>Yes</p>	<p>Reinsurance. Professional indemnity insurance of bank. Non-disclosure and misrepresentation of the misconduct of the bank's president. The court held that the reinsurer was entitled to avoid the contract. The court found that the reassured was aware of the misconduct. (para 18-20)</p>
<p><i>Cavell USA v Seaton Insurance</i> [2009] Lloyd's Rep IR 616</p>	<p>Intentional</p>	<p>N/A</p>	<p>This case was about whether exclusive jurisdiction clause was applicable to fraud claim and utmost good faith was mentioned as a clause of the insurance contract but not as an operation of law. (para 44)</p>

<i>Centre Reinsurance v Curzon Insurance Ltd</i> [2004] Lloyd's Rep IR 622	Not identified	N/A	A third-party claim against the insurer under a liability insurance in the situation where the assured was insolvent. Utmost good faith was examined as a matter of insurer's attitude to handle claim at the claims stage. (para 92)
<i>Crane v Hannover</i> [2010] Lloyd's Rep IR 93	Innocent	No	Misrepresentation and non-disclosure of reassured underwriting practice. The court held that the reinsurer was not entitled to avoid the contract. The presentation was not false. (para 127)
<i>Curzon Insurance Ltd v Centre Reinsurance Co</i> [2006] Lloyd's Rep IR 370	Innocent	No	Reinsurance contract. Declaration that settlement arrangements entered into by the reassured did not infringe the terms of reinsurance arrangements. The court held that the assured was entitled to the declaration. (para 74) Utmost good faith was mentioned at the post-contractual stage but the court held that there was no breach of the duty. (para 61)
<i>Dalecroft Properties Ltd v Underwriters</i> [2017] Lloyd's Rep IR 511	Intentional	Yes	Property Insurance. Fire accident. Non-disclosure and misrepresentation of the state of the property. The court held that the assured was liable for the breach, even under the standard of IA 2015. (para 201)

<i>Delaney v Pickett</i> [2013] Lloyd's Rep IR 24	Not identified	Yes	Motor Insurance. Driver and passenger in the same car. Whether the passenger can claim against the driver under tort law. The related policy was avoided by the insurer on the ground of utmost good faith, but it was not an issue in this case. (para 65)
<i>Direct Line Insurance v Fox</i> [2010] Lloyd's Rep IR 324	Intentional	N/A	Property Insurance. Fire accident. The assured made a wrong claim on the VAT of repairing cost the damaged house. The court held that there was no fraudulent claim, and the fraudulent action was not about the claim, but the VAT. Utmost good faith was not examined in detail. (para 31)
<i>Direct Line Insurance v Khan</i> [2002] Lloyd's Rep IR 384	Intentional	N/A	Fire accident in residential house. Fraudulent claim of rental fee and accommodation fee. The court held that the assured was liable for fraudulent claim. Utmost good faith was not examined in detail. (para 22)
<i>Dornoch Ltd v Mauritius Union Assurance Co Ltd</i> [2006] Lloyd's Rep IR 127	Not identified	N/A	Conflict of laws case. Utmost good faith was not examined in the context of English law. (para 77)
<i>Drake Insurance plc v Provident Insurance plc</i> [2004] Lloyd's Rep IR 277	Innocent	No	Motor Insurance. Non-disclosure of no-fault accident. The court held that the insurer was not entitled to avoid the contract. (para 129, 191)

<i>DSG v QBE International Insurance Ltd</i> [1999] Lloyd's Rep IR 283	Intentional	Yes	Insurance for promotion. Non-disclosure and misrepresentation of previous experience of handling promotion. The court held that there was non-disclosure and misrepresentation. (page 288)
<i>Eagle Star Insurance Co Ltd v Games Video Co</i> [2004] Lloyd's Rep IR 867	Intentional	Yes	Vessel total loss. Misrepresentation of the value of the vessel. The court held that the insurer was entitled to avoidance as the disclosure and misrepresentation were made in bad faith. (para 55 and 119)
<i>Economides v Commercial Union Assce Co plc</i> [1998] 7 Lloyd's Rep IR 9	Innocent	No	Household insurance. Non-disclosure and misrepresentation of the value of the goods in house. The Court held that the assured was not liable to the breach. The assured acted honestly. (page 21)
<i>European Risk Insurance Co hf v McManus</i> [2014] Lloyd's Rep IR 169	Not identified	N/A	Professional indemnity insurance of a solicitor firm. Declaration of the validity of the claim notification and the award of cost were refused by the court. Utmost good faith was not examined in detail. (para 19)

<p><i>Feasey v Sun Life Assurance Corporation of Canada</i> [2003] Lloyd's Rep IR 637</p>	<p>Not identified</p>	<p>N/A</p>	<p>P &amp; I reinsurance. Utmost good faith was mentioned but not examined. (page 667)</p>
<p><i>First Nat Commercial Bank v Barnet Devanney Ltd</i> [1999] Lloyd's Rep IR 43</p>	<p>Not identified</p>	<p>N/A</p>	<p>Composite insurance for mortgage. The breach of utmost good faith by one of the co-assured did not affect the other co-assured. (page 51)</p>
<p><i>Frans Maas (UK) Ltd v Sun Alliance and London Insurance Plc</i> [2004] Lloyd's Rep IR 649</p>	<p>Innocent</p>	<p>No</p>	<p>Non-disclosure of goods being released without bills of lading. The court held that there was no breach of utmost good faith. (para 64)</p>



<p><i>Galloway v Guardian Royal Exchange (UK) Ltd</i> [1999] Lloyd's Rep IR 209</p>	<p>Intentional</p>	<p>N/A</p>	<p>Home contents policy. Non-disclosure of conviction of fraud in obtaining property by deception. The court held that the assured was liable for fraudulent claim. Utmost good faith was examined in the context of fraudulent claim. (page 212, 213)</p>
<p><i>Gan Insurance v Tai Ping Insurance</i> [2002] Lloyd's Rep IR 612</p>	<p>Not identified</p>	<p>N/A</p>	<p>Reinsurance of the machinery to produce computer chips. Settlement was reached without the consent of the reinsurer, which was in breach of the settlement clause of the contract. Utmost good faith was not examined in detail. (page 613)</p>
<p><i>Gan v Tai Ping (Nos 2 &amp; 3)</i> [2001] Lloyd's Rep IR 667</p>	<p>Innocent</p>	<p>No</p>	<p>The same case fact as <i>Gan Insurance v Tai Ping Insurance</i>. The court held that there was no non-disclosure and misrepresentation. (page 668-669)</p>
<p><i>GE Frankona v CMM Trust No 1400</i> [2006] Lloyd's Rep IR 704</p>	<p>Not identified</p>	<p>N/A</p>	<p>Interpretation of the meaning of the warranty "Warranted fully crewed at all times". Utmost good faith was not examined in detail. (para 7)</p>

<i>Goshawk Dedicated Ltd v ROP Inc</i> [2006] Lloyd's Rep IR 711	Not identified	N/A	Seeking of anti-suit injunction. Utmost good faith was not examined in detail.
<i>Group Josi Re v Walbrook Ins Co Ltd</i> [1996] 5 Lloyd's Rep IR 91	Intentional	No	Reinsurance. Non-disclosure of the fraud of the directors of the reassured. The court held that the reassured was not liable for the non-disclosure as the fraud exception rule applied. (page 101)
<i>Henderson v Merrett Syndicates Ltd</i> [1996] 5 Lloyd's Rep IR 279	Not identified	N/A	Alleged negligence regarding the writing of run-off contracts and reinsurances to close. Utmost good faith was not examined in detail (page 366)
<i>Henderson v. Merrett Syndicate</i> [1997] Lloyd's Rep IR 265	Not identified	N/A	Auditors alleged contributory negligence. Utmost good faith was not examined in detail. (page 364)

<p><i>Herridge v Parker</i> [2014] Lloyd's Rep IR 177</p>	<p>Not identified</p>	<p>N/A</p>	<p>Avoidance of contract due to the fraud of the assured. Whether the insurer was liable to the cost under the third-party cost order. Utmost good faith was not examined in detail and the judge stressed that the finding was based on an assumption of fraud, but it was not the actual finding. (para 18)</p>
<p><i>HIH Casualty and General Ins Ltd v Chase Manhattan Bank</i> [2003] Lloyd's Rep IR 239</p>	<p>Intentional</p>	<p>Yes</p>	<p>Insurance securing repayment of financing for production of films. Non-disclosure and misrepresentation by the broker. The court held that the assured was liable to the breach. (para 23)</p>
<p><i>HIH Casualty and General Insurance v JLT</i> [2006] Lloyd's Rep IR 493</p>	<p>Intentional</p>	<p>Yes</p>	<p>HIH sued against the broker for negligence. The same case as <i>HIH v Chase</i>.</p>

<i>HIH Casualty v New Hampshire Insurance Co</i> [2001] 5 Lloyd's Rep IR 96	Not identified	N/A	Reinsurance of a film finance insurance. The issue was whether warranty and waiver incorporated into the reinsurance contract. The discussion was focused on the effect of the warranty and waiver clause, and utmost good faith was not examined in detail. (para 209)
<i>Hill v. Citadel Insce</i> [1995] Lloyd's Rep IR 218	Intentional	Yes	Misrepresented and non-disclosure of the costs of XL protection. The court held that the reassured was liable to the breach, and the breach was intentional. (page 221)
<i>Hume v. AA</i> [1996] Lloyd's Rep IR 19	Not identified	N/A	Application of summary judgment. Utmost good faith was examined to the extent that whether it was a good arguable case only. (page 31)
<i>ICCI v. McHugh</i> [1997] Lloyd's Rep IR 94	Innocent	No	Business interruption insurance. Both parties alleged breach of utmost good faith, but both allegations failed. (page 135, 142)
<i>International Lottery Management Ltd v Dumas and Others</i> [2001] Lloyd's Rep IR 237	Intentional	Yes	Non-disclosure and misrepresentation of the authorization of establishing lottery business. The court held that the assured was liable for the breach. (para 70) The court also held that the translation and legal opinion from the assured was misleading. (para 52)
<i>International Management Group (UK)</i>	Intentional	Yes	Insurance in relation to the cricket matches between India and Pakistan. Non-disclosure and misrepresentation of the permission from Indian government and the previous events. The

<i>Ltd v Simmonds</i> [2004] Lloyd's Rep IR 247			court held that the assured was liable for the breach. (para 126) The breach was intentional. (para 138)
<i>Interpart Comercio e Gestao SA v Lexington Ins Co</i> [2004] Lloyd's Rep IR 690	Intentional	N/A	Presentation of a false certificate of inspection of goods for marine insurance policy. Application of summary judgment was refused, but the judge considered that the certificate was fraudulently made. (para 42)
<i>Involnert Management Inc v Aprilgrange Ltd</i> [2015] Lloyd's Rep IR 661	Innocent	Yes	Misrepresentation and non-disclosure of the true value of the yacht. The court held that the assured was liable for non-disclosure but not misrepresentation. The non-disclosure was not intentional. (para 79)
<i>James v CGU Insurance Plc &amp; Ors</i> [2002] Lloyd's Rep IR 206	Intentional	Yes	Allegation of arson by the assured. Non-disclosure of moral hazard, disputes with Inland Revenue and the use of property. The court held that the assured was liable for the breach. There is no evidence that indicates the intention of the breach (para 64, 67, 83), but the conduct of not honouring the warranty by the MBIA was a matter of dishonesty. (para 100)
<i>Jones v Environcom</i> [2010] Lloyd's Rep IR 676	Innocent	No	Allegation of the breach of broker's duty to warn the assured to disclose material information to the insurer. The court held that the broker was not liable for the loss of the assured. (para 110) The apparent fact is that the non-disclosure of the assured was unintentional. (para 73)
<i>K/S Merc-Scandia v Certain Lloyd's</i>	Intentional	No	Insurer's alleged a breach of post-contractual utmost good faith by the assured's fraudulent conduct of forgery signature on the letter that deceived the underwriter. The court held that

<i>Underwriters &amp; Ors</i> [2001] Lloyd's Rep IR 802			there was no breach of good faith as it didn't fall within any category of the post-contractual duty. (para 40)
<i>Laker Vent Engineering v Templeton Insurance</i> [2009] Lloyd's Rep IR 704	Innocent	No	Non-disclosure of dispute between the third party and the assured before the renewal of contract. The court held that the insurer was not entitled to avoid the contract. The assured did not think that there was a dispute between the parties at the underwriting stage. (para 62)
<i>Mander v Commercial Union Assurance Co Plc</i> [1998] 7 Lloyd's Rep IR 93	Not identified	N/A	Dispute about the declaration and whether reinsurance binding on the reinsurer. Utmost good faith was discussed as an obiter judgment, but the court held that the reinsurance could be avoided. (page 136)
<i>Marc Rich Agriculture Trading v Fortis Corporate Insurance</i> [2005] Lloyd's Rep IR 396	Not identified	N/A	Theft of cargo claim. Allegation of the breach of post-contractual duty of utmost good faith, namely non-disclosure of material information at claims stage. Application of summary judgment so no detail examination on this issue. (para 33)
<i>Markel v La Republica</i> [2005] Lloyd's Rep IR 90	Not identified	N/A	Application of the stay of proceeding. Utmost good faith was examined as to whether there was a good arguable case. (para 25)

<i>Micro Design v Norwich Union</i> [2006] Lloyd's Rep IR 235	Intentional	Yes	Burglary claim. Company name under the assured's name did not exist. Non-disclosure of previous policy cancelled due to the default payment. The court held that the assured was liable for non-disclosure. (para 104) It was held by the court that the assured was aware of the non-disclosed information. (para 87)
<i>Moore Large &amp; Co Ltd v Hermes Credit &amp; Guarantee Plc</i> [2003] Lloyd's Rep IR 315	Intentional	No	Non-disclosure of information in relation to debt and credit. Endorsement about raising credit limit could be avoided, but the court held that the insurer had waived the right of avoidance. (para 103) The court held that the breach was likely to be intentional. (para 56)
<i>Mundi v Lincoln Assurance Ltd</i> [2006] Lloyd's Rep IR 353	Intentional	Yes	Life insurance. Non-disclosure of past medical consultation record and drinking habit. The court held that the insurer was entitled to avoid the contract. (para 72) The court found that the non-disclosure was intentional. (para 57, 58)
<i>Mutual Energy Ltd v Starr Underwriting Agents Ltd</i> [2016] Lloyd's Rep IR 550	Innocent	No	Insurance claim of cable failure. Policy terms excluded avoidance unless fraudulent and deliberate non-disclosure or misrepresentation. The court held that the insurer could only avoid the contract if the breach was by dishonest conduct. (para 54) The assured's non-disclosure was based on an honest but mistaken belief. (para 81P)
<i>New Hampshire Ins Co v MGN Ltd</i> [1996] 5 Lloyd's Rep IR 103	Not identified	N/A	Fidelity insurance. The relevant issue was whether an avoidance of contract could affect other co-assured. The court did not examine this issue in detail (page 109)

<i>New Hampshire Insurance Co v Oil Refineries Ltd</i> [2003] Lloyd's Rep IR 386	Innocent	Yes	Public liability insurance. Non-disclosure of previous claims record. The court held that the insurer was entitled to avoid the contract. The court found that the non-disclosure was not intentional. (para 24)
<i>New Hampshire v. MGN</i> [1997] Lloyd's Rep IR 24	Not identified	N/A	Fidelity insurance. Allegation of non-disclosure and misrepresentation. The issue was whether avoidance of contract could affect other co-assured. The court held that the breach of utmost good faith for one co-assured did not affect the other co-assured. (page 58) The operation of utmost good faith was not examined in detail.
<i>Noble Assurance v Gerling-Konzern General Insurance</i> [2008] Lloyd's Rep IR 1	Not identified	N/A	Reinsurance. Application of an injunction for a legal proceeding in Vermont. Allegation of non-disclosure and misrepresentation of the coverage of the insurance contract after granting the arbitration award. The court did not examine the requirement of utmost good faith but only stated that it was opened to the reinsurer to plead the breach of the duty of utmost good faith. (para 101)
<i>Noblebright Ltd v Sirius International Corporation</i> [2007] Lloyd's Rep IR 584	Intentional	Yes	Property insurance. Fire accident. Non-disclosure of previous robbery record (with no claim) in the assured's warehouse. The court held that the non-disclosure was not waived by the insurer, and the insurer could avoid the contract. The court also held that a reasonable man who read the proposal form should have disclosed the previous no claim loss to the insurer. (para 68)



<i>North Star Shipping v Sphere Drake Insurance</i> [2006] Lloyd's Rep IR 519	Intentional	Yes	Marine war insurance. Explosion on the vessel. Non-disclosure of financial status and outstanding legal proceedings of the assured. The court held that the assured was liable for the breaches. (para 51)
<i>Norwich Union Life Insurance Society v Qureshi and Qureshi</i> [1999] Lloyd's Rep IR 263	Innocent	No	A property backed guarantee plan consisted of a life policy. Allegation of the non-disclosure by the assured against the insurer about the market information of Lloyd's. The court held the insurer was not in breach of the duty of utmost good faith. (page 272)
<i>O'Kane v Jones</i> [2005] 1 Lloyd's Rep IR 174	Innocent	No	Two insurance policies, one for the owner and one for the management company, covering hull and machinery. Allegation of non-disclosure of the record about the delay of premium payment of the owner's policy. The court held that the assured was not liable to the breach. (para 244)
<i>Odyssey Re (London) Ltd and Anor v OIC Run-off Ltd</i> [2001] Lloyd's Rep IR 1	Not identified	N/A	Reinsurance case. The issue was whether the contract was legally binding. Utmost good faith was not examined in the context of section 17 – 20 of the MIA 1906. (page 27)
<i>Orakpo v. Barclays Insce</i> [1995] Lloyd's Rep IR 443	Intentional	Yes	Property insurance. Non-disclosure of the state of the building. Fire accident. The court held that the assured was liable for the breach and found that the non-disclosure was intentional. (page 449)

<i>Patel v Windsor Life Assurance Co Ltd</i> [2008] Lloyd's Rep IR 359	Intentional	Yes	A life insurance for a named assured but inputted and claimed by another person. Non-disclosure of the attempt to defraud the insurer and fraudulent claim of the death of the assured. The court held that in any event the people in this case were not entitled to the claim. (page 371)
<i>PCW Syndicates v PCW Reinsurers</i> [1996] Lloyd's Rep IR 241	Innocent	No	Non-disclosure of the fraud of principle from the agent to the reinsurer. It was held that the fraud was not known and in any event Hampshire Land principle was applied and the reinsurer was not entitled to avoid the contract. (page 383)
<i>Persimmon Homes v Great Lakes</i> [2011] Lloyd's Rep IR 101	Intentional	Yes	After the event insurance cover. Non-disclosure and misrepresentation of a list of material information and dishonest conduct, and the court found that the insurer was entitled to avoid the contract. (para 106)
<i>Quinn Direct Insurance v Law Society</i> [2010] Lloyd's Rep IR 655	Not identified	N/A	Professional indemnity case which the insurer required the disclosure of all books and records from solicitors. The court held that the insurer was not entitled to obtain information in the manner like the law society. (para 27). The main concern of this case was not about the avoidance of contract.
<i>R &amp; R Developments v Axa Insurance</i> [2010] Lloyd's Rep IR 521	Not identified	N/A	Commercial and contract work insurance. Non-disclosure of insolvency record of the director. The assured pleaded that the question in the proposal form was ambiguous. No discussion was made on the intention and the avoidance of contract. (para 36, 42)

<i>Royal Boskalis v. Mountain</i> [1997] Lloyd's Rep IR 523	Intentional	No	War risk insurance covering dredging works. Allegation of the breach of post-contractual utmost good faith at claims stage, which was non-disclosure of information that was material to the war risk claim. The court held that the insurer was not entitled to avoid the contract even the non-disclosure and misrepresentation at the claims stage were deliberate.
<i>Sea Glory Maritime Co and Another v Al Sagr National Insurance Co (The "M/V Nancy")</i> [2014] Lloyd's Rep IR 112	Innocent	No	Marine insurance. Allegation of the non-disclosure and misrepresentation of the actual management company of the vessel, Port State Control inspection record, the U-turn authorisation practice, and the identity of the Designed Person Ashore. The court held that the insurer was not entitled to avoid the contract. (para 309, 310)
<i>Sherdley v Nordea Life &amp; Pensions</i> [2012] Lloyd's Rep IR 437	Not identified	N/A	Conflict of laws case. Utmost good faith was not examined in the context of section 17, 18, 19 and 20 of the MIA 1906. (para 51)
<i>Stowers v G A Bonus Plc</i> [2003] Lloyd's Rep IR 402	Not identified	Yes	Combined commercial insurance. Theft in the office premise. Non-disclosure of previous claim history. The court held that the assured was liable for the breach of duty. There was no examination on whether the non-disclosure was intentional. (page 405)
<i>Suez Fortune Investments Ltd v Talbot Underwriting Ltd (The</i>	Not identified	N/A	Marine risk. Broke down of engine due to pirate attack. This case concerned the quantum of indemnity and the definition of constructive total loss, and utmost good faith was not examined in detail (para 303)

<p><i>“Brillante Virtuoso”</i></p> <p>[2015] Lloyd's Rep IR 388</p>			
<p><i>Talbot Underwriting v Nausch, Hogan &amp; Murray</i></p> <p>[2006] Lloyd's Rep IR 531</p>	Not identified	N/A	Ship construction policy. Insurer contended non-disclosure of beneficiary. The court held that there was a real prospect for the insurer to avoid the contract as it was a preliminary trial for a summary judgment. (para 102)
<p><i>Ted Baker Plc v Axa Insurance Ltd</i></p> <p>[2017] Lloyd's Rep IR 46</p>	Not identified	N/A	Business interruption insurance. Whether the employee theft was covered under the policy. Utmost good faith was mentioned for the insurer's duty to act in good faith in requesting material document, but this was not an issue in this case (para 89)
<p><i>Decorum Investments Ltd v Atkin (The Elena G)</i></p> <p>[2002] Lloyd's Rep IR 450</p>	Innocent	No	Marine policy. Constructive total loss. Non-disclosure of the true user of the vessel was at security risk. The court held that the insurer could not avoid the contract as the insurer failed to prove there was a real risk. (para 101)
<p><i>Strive Shipping Corporation v Hellenic Mutual War Risks Association (BERMUDA) Ltd (The Grecia Express)</i></p> <p>[2002] Lloyd's Rep IR 669</p>	Innocent	No	Marine policy. Allegation of scuttling. Non-disclosure of previous loss. Misrepresentation of the value of the vessel. The court held that there was no breach of utmost good faith. (para 442, 479)

<i>Manifest Shipping Co Ltd v Uni-Polaris Shipping Co Ltd and others (The "Star Sea")</i> [2001] Lloyd's Rep IR 247	Innocent	No	Allegation of the breach of post-contractual utmost good faith. The court held that there was no breach of utmost good faith as there was a limited scope of application. (para 111)
<i>Transthene v. Royal Insce. (U.K.) Ltd.</i> [1996] Lloyd's Rep IR 32	Intentional	No	Insurance (fire and perils). Allegation of arson and fraudulent claim. Utmost good faith was examined in the context of fraudulent claim, and there was no examination in terms of the operation of law. (page 43)
<i>Travelers Casualty Surety v Sun Life Assurance</i> [2007] Lloyd's Rep IR 619	Not identified	N/A	Professional indemnity insurance. Breach of warranty and the issue was the applicable law. There was no issue of utmost good faith (para 369)
<i>Tryg Baltica International v Boston Compania de Seguros</i> [2005] Lloyd's Rep IR 40	Not identified	N/A	Conflict of laws case in relation to insurance contract. Utmost good faith was not a critical issue in this case and did not affect the application. (para 59, 61)
<i>Turville Health Inc v Chartis Insurance</i> [2013] Lloyd's Rep IR 404	Not identified	N/A	Applicability of arbitration clause in insurance contract and stay of proceeding. Utmost good faith was not examined in detail (para 41)

<i>Versloot Dredging Bv and Another v HDI Gerling Industrie Versicherung Ag and other (The "DC Merwestone")</i> [2016] Lloyd's Rep IR 468	Yes	No	Fraudulent claim case on the matter of whether collateral lie constitutes a fraudulent claim. Utmost good faith was examined in the context of fraudulent claim, no avoidance was awarded. (para 68)
<i>Wise Ltd v Grupo Nacional Provincial SA</i> [2004] Lloyd's Rep IR 764	Innocent	Yes	Reinsurance of cargo insurance. Translation error. The court held that there was a breach of utmost good faith. The breach was due to a translation error which was not intentional. (para 41)
<i>Yeganeh v Zurich</i> [2011] Lloyd's Rep IR 75	Not identified	N/A	Fraudulent claim case and the breach of utmost good faith was pleaded but denied (para 25)
<i>Zeller v British Caymanian Insurance</i> [2008] Lloyd's Rep IR 545	Innocent	No	Group health insurance of a company. Non-disclosure of medical condition and examination. The court held that there was no breach of duty and the assured was honest. (para 20)

### Annex 3 23 Hong Kong Cases In Relation To Utmost Good Faith

Case name	Intention (Intentional/Innocent/Not identified)	Whether the contract was avoided (Yes/No/N/A)	Summary
<i>K. Master &amp; Co. Ltd. v Eagle Star Insurance Ltd</i> HCA002343/1966	Not identified	N/A	Order of discovery under O.72 r.10 for several correspondences in relation to the sailed goods. Utmost good faith was not examined in detail.
<i>Success Insurance v George Kallis (Manufacturers) Ltd.</i> CACV000133/1980	Innocent	No	Non-disclosure of changing of vessel that carried the goods of the assured. The court held that the assured was entitled to rely on the agent's presentation and bills of lading. The assured was not in breach of the duty of utmost good faith.
<i>Bee Kay</i> HCA010790/1982	Not identified	N/A	Not an insurance case. Utmost good faith was mentioned beyond the scope of section 18,19 and 20 of the MIO.

<p><i>LOO KAM BU trading as Hung Hing Cheung Machinery Factory (a firm) DCCJ007514/1984</i></p>	<p>Innocent</p>	<p>No</p>	<p>Employee compensation case.  The late notice requirement was deemed to be waived. Increasing employee from one to two was not a significant change, so it was not a material non-disclosure.</p>
<p><i>Insurance Company of the State of Pennsylvania v Grand Union Insurance Company Limited CACV000186/1989</i></p>	<p>Innocent</p>	<p>No</p>	<p>First instance court held that the documents were fairly presented, no disputed point on the non-disclosure or fair presentation. The Court of Appeal allowed the appeal. But no further discussion on the duty of disclosure/misrepresentation.</p>
<p><i>Chan Woon-Hung trading as Ocean Plastic Factory v Associated banker Insurance Ltd CACV000036/1991</i></p>	<p>Innocent</p>	<p>Yes</p>	<p>EC case. Car accident injury. The court held that the employee needed to comply with the insurance contract with utmost good faith and should forward the summons to the insurer.</p>



<p><i>Wunsche Handelsgesellschaft International Mbh v General Accident Insurance Asia Limited (formerly known as New Zealand Insurance Co. Ltd.)</i> HCCL 73/1994</p>	<p>Innocent</p>	<p>No</p>	<p>The court reviewed the policies and cover notes and found that the insurer had made an adequate disclosure to the assured.</p>
<p><i>China (HK) Chemical &amp; Plastics Company Limited v China Insurance Company Limited</i> 1997, No.CL19</p>	<p>Not identified</p>	<p>N/A</p>	<p>Marine Cargo risk. The court held that the insurer was not entitled to seek a summary judgment in this case, as the matter of materiality was not yet determined.</p>
<p><i>Ingo International Limited v Canadian Eastern Life Assurance Limited</i> HCA 19675/1999</p>	<p>Not identified</p>	<p>N/A</p>	<p>The deceased did not disclose the financial status properly, as there were previous legal actions against him for unrecovered debt. The court held that it is more likely than not that the insurer could rely on these defences (breaching the duty of utmost good faith, both section 18 and 19) to strike</p>

			out the case. Nevertheless, the court did not touch upon the details of the breach.
<i>E.L.A.Z. International CO. v Hong Kong &amp; Shanghai Insurance Company Limited</i> HCCL000016_2003	Innocent	No	Marine cargo was stolen in America during a transit voyage which the destination would be Mexico. The insurer refused to pay claim and contended that the assured breached the duty of utmost good faith. The court did not examine this argument. (para 155)
<i>HKSAR v Chan King Lam</i> HCMA482/2009	Not identified	N/A	EC insurance fraud case making a claim without an accident. Utmost good faith was not examined in detail.
<i>HKSAR v Lee Kwok-fung Simon</i> DCCC 364/2014	Not identified	N/A	Insurance fraud case. No discussion on the utmost good faith. The only relevant part was “the insurance contract is a contract of utmost good

			faith.” (para 6, 33)
<i>Lam Charn Yung v Axa</i> (2004) DCCJ1522/2004	Intentional	Yes	The assured with breast cancer failed to disclose her medical record history to the Insurer before the formation of the contract. The court held that there was a breach of the duty of disclosure and the contract was avoided.
<i>The Ming An Insurance Co. (H.K.) LTD v Chan Man Dun</i> CACV 96/2005	Not identified	Yes	Motor insurance contract. The court held that as the chassis and engine number were important for the motor registration, these particulars were material to the insurer. The court also held that the insurer was induced by the misrepresentation to enter into the insurance contract. Hence, the insurance policy was avoided.
<i>Leung Yuet Ping v Manulife (International) Limited</i>	Not identified	Yes	Failed to disclose medical condition. The court held that the non-disclosed

HCA 2380/2006			information was material and thus the insurer was not liable to pay claim.
<i>Ace Insurance Limited v Metropolitan Electrical Appliance Manufacturing Co. Ltd</i> HCA328/2008	Innocent	No	The plaintiff insurer applied for a summary judgment for the recovery of "Self-Insured Retention". The court examined the relationship between good faith and utmost good faith. The court held that the claim was settled in good faith, as a result the defendant could not refuse to pay deductible.
<i>Kam Hing Trading (Hong Kong) Ltd v The People's Insurance Company of China (Hong Kong) Limited</i> HCCL 27/2009	Innocent	No	Sink of vessel and loss of cargo. Non-disclosure of the class of the vessel. The court held that the assured had no such knowledge, and thus the pleading of utmost good faith must have failed. (para 186) But the assured failed to claim against the insurer on other grounds which were irrelevant to

			utmost good faith. (para 185)
<i>China Ping An Insurance (Hong Kong) Company Limited v Tsang Fung Yin Josephine</i> CACV HCA 308/2010	Not identified	N/A	Motor insurance. Failure to give notice and in breach of policy terms. Utmost good faith was mentioned but not examined. (Para 36)
<i>Hua Tyan Development Limited v Zurich Insurance Company Limited</i> [2014] 2 Lloyd's Rep. 637	Not identified	N/A	Allegation of non-disclosure of the deadweight capacity of the vessel. The court held that the warranty had covered this issue and thus the examination of utmost good faith was not necessary. (para 56)
<i>Ng Fui v Kam Chi Ming</i> HCA 739/2011	Not identified	N/A	Avoiding investment contract and seeking damages. Not an insurance case. (para 10, 36)
<i>HKSAR v Man Choi Wa</i> DCCC 572/2013	Not identified	N/A	Criminal charges of fraud and attempted of insurance claims. Utmost good faith was mentioned but not examined. (para 46)

<p><i>Possehl Electronics Hong Kong Limited v China Taiping Insurance (HK) Co Ltd CACV 9/2014</i></p>	<p>Not identified</p>	<p>N/A</p>	<p>Time bared claim appeal refused by the court. Utmost good faith was mentioned but not examined. (para 2)</p>
<p><i>HKSAR v Jeho DCCC 596/2015</i></p>	<p>Not identified</p>	<p>N/A</p>	<p>Criminal charge of fraud and attempted fraud of insurance claim. Utmost good faith was mentioned but not examined (para 168)</p>

## Annex 4 The Questionnaire Of The Hong Kong Survey

Question number(s)	Question(s)	Answer(s)
Q1	How often do you handle cases that are related to the duty of utmost good faith (i.e. non-disclosure and misrepresentation) in your daily practice?	A few times a week/A few times a month/ A few times a year/Less than once a year/Never/Other (Please specify)
Q2	How often do you handle cases that are related to the breach of the duty of utmost good faith by the agent to insure in your daily practice?	A few times a week/A few times a month/A few times a year/Less than once a year/Never/Other (Please specify)
Q3	The current duty of utmost good faith only provides one remedy, which is the remedy of avoidance (to avoid the insurance contract as if it never exists). Do you agree that the legislation shall provide alternative remedies?	Yes/No/No comment
Q4	How often do you handle cases that are related to misrepresentation under the Misrepresentation Ordinance in your daily practice?	A few times a week/A few times a month/A few times a year/Less than once a year/Never/Other (Please specify)

Q5	The Insurance Act 2015 replaced the duty of utmost good faith with a new duty of fair presentation in England and Wales. To what extent do you agree that the said change of law affects your daily practice?	Strongly agree/Agree/Neither agree nor disagree/Disagree/Strongly disagree
Q6	The Insurance Act 2015 imposed a new proportionate remedy to replace the single remedy of avoidance under the duty of utmost good faith. Do you agree that the said new proportionate remedy should be introduced in Hong Kong?	Yes/No/No comment
Q7	Under the Insurance Act 2015, the assured is required to conduct a reasonable search of information available to the assured (whether the search is conducted by making enquiries or by any other means) before disclosing material information to the insurer. Do you agree that the said new duty of reasonable search should be introduced in Hong Kong?	Yes/No/No comment
Q8	The Insurance Act 2015 is acted as a “default regime” (the rules which apply in the absence of any contractual terms to the contrary). Do you think this approach is desirable for a law reform?	Yes/No/No comment



Q9	To what extent do you think the change of law in relation to the duty of utmost good faith/fair presentation is likely to affect the charge of premium by the insurer?	Very likely/Likely/Neither likely nor unlikely/Unlikely/Very unlikely
Q10	If there will be a law reform for the duty of utmost good faith in Hong Kong, which of the following will you consider as the most desirable approach for the said reform?	The reform shall follow the approach of the Insurance Act 2015/The reform shall be independent from the Insurance Act 2015/No comment/Other (please specify)

## **Annex 5 The Draft Bill Of The New Marine Insurance Ordinance (Section 17, 18, 19 and 20)**

### **Section 17 The duty of utmost good faith**

(1) A contract of insurance is a contract based on 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. The court or arbitrator may declare the contract subsisting and award damages in lieu of avoidance, if of opinion that it would be equitable to do so, having regard to the nature of the breach of utmost good faith and the loss that would be caused by it if the contract were upheld, as well as to the loss that avoidance would cause to the other party.

(2) This section does not apply to matters arising under or in relation to the duty of fair presentation, which is provided in section 18, 19 and 20 of this ordinance. The Misrepresentation Ordinance is not applicable to the cases which involved the disputes of utmost good faith/fair presentation.

### **Section 18 The duty of fair presentation – non-disclosure**

(1)(a) 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 person who is responsible for the assured's insurance (the actual assured), and the assured is deemed to know every circumstance which, in the ordinary course of business, ought to be known by the actual assured, unless it is a knowledge of fraud perpetrated by the assured. If the assured fails to make such disclosure in the absence of a valid defence, the insurer may be entitled to seek one of the following remedies:

- (i) The remedy of avoidance if, but for the breach, the insurer would not have entered into the contract of insurance at all, or
- (ii) Additional premium if, but for the breach, the insurer would have entered into the contract with a higher premium.

(1)(b) The assured is deemed to know what should reasonably have been revealed by a reasonable search of information accessible to the actual assured. Information that can be found on the internet is not deemed to be known by the assured.

(1)(c) If the person who is responsible for the assured's insurance is an agent of the assured, the knowledge of fraud, which is perpetrated by the agent against the assured, is not imputed to the assured.

(1)(d) For the purpose of section 18(1)(a), the assured is entitled to raise a defence on the ground that the a reasonable assured would not have expected that the material circumstance is disclosable to the insurer.

(2)(a) Every circumstance is material which a prudent insurer would want to know about in fixing the premium or determining whether he will take the risk and on what terms.

(2)(b) For the purpose of section 18(1), whether the insurer is induced by the assured's non-disclosure or misrepresentation of the risk, in each case, is a question of fact, and there should not be a presumption of inducement unless there is a justifiable ground for such a presumption.

(3) In the absence of inquiry the following circumstances need not be disclosed, namely—

(a) any circumstance which diminishes 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 his business, as such, ought to know. The insurer is also deemed to know what should reasonably have been revealed by a reasonable search of information accessible to the insurer.

(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.

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

(5) The term "circumstance" includes any communication made to, or information received by, the assured.

(6) For a claim of non-disclosure, the insurer/underwriter needs to prove that had the material circumstance been disclosed, the insurer/underwriter would not have entered into the insurance contract, or would have entered into the insurance contract with additional premium.

### **Section 19 is now omitted/repealed**

### **Section 20 The duty of fair presentation - misrepresentation**

(1) Every material representation made by the assured or his agent to the insurer during the negotiations for the contract, and before the contract is concluded, must be true. If it be untrue the insurer may be entitled to seek one of the following remedies:

- (a) The remedy of avoidance if, but for the breach, the insurer would not have entered into the contract of insurance at all, or
- (b) Additional premium if, but for the breach, the insurer would have entered into the contract with a higher premium.”

(2) A representation is material which a prudent insurer would want to know about in fixing the premium, or determining whether he will take the risk.

(3) A representation may be either a representation as to a matter of fact, or as to a matter of expectation or belief.

(4) 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.

(5) A representation as to a matter of expectation or belief is true if it be made in good faith.

(6) A representation may be withdrawn or corrected before the contract is concluded.

(7) Whether a particular representation be material or not is, in each case, a question of fact.

(8) For a claim of misrepresentation, the insurer/underwriter needs to prove that should the material misrepresentation not have been made, the insurer/underwriter would not have entered into the insurance contract, or would have entered into the insurance contract with additional premium.