GLOBAL INSURANCE LAW CONNECT

# Global Insurance Law Connect
## Annual Review 2018

# Welcome

**Jim Sherwood**
*Chairman*

Insurers and reinsurers need legal advice that is specialist, international and relevant to the markets in which they operate. Our company was built to help you confidently face your insurance legal challenges around the globe.

Inspired by client demand, Global Insurance Law Connect has been organized as a formal grouping of insurance law firms, delivering the right advisers in the right places and in the right way. Members provide global access to specialist insurance law and legal advice on a range of issues across a wide variety of markets.

Whether you are in new or established markets, dealing with familiar or unusual issues, the advisors in our organisation will guide you through unfamiliar territories – delivering great outcomes as economically as possible while adding value through their commercialism and knowhow.

Over the past year Global Insurance Law Connect has worked hard to provide our clients with up to date articles, detailing key changes in the international insurance market, and we are really happy to be able to share this with you, in one place.

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# India updates ‘order of preference’ rules for reinsurers

*In August 2018, member firm, Khaitan Associates published an update on changes to the rules about competition between foreign and local reinsurers in India.*

The controversy over the enforced 'Order of Preference' for Indian and foreign reinsurers that has polarised the Indian insurance industry since 2015 refuses to die down.

This issue has dominated debate over the last two years ever since foreign reinsurers were permitted to open branch offices (FRBs) in India. The recent proposal by the regulator to alter the Order of Preference has reignited the debate.

*The status of the Indian reinsurer as the reinsurer of first preference would be removed in some insurance classes via the new proposed regulations.*

The Order of Preference forms part of the regulations set by the Indian insurance regulator – the Insurance Regulatory & Development Authority (IRDA) and they essentially accord ranked preferential treatment to onshore entities undertaking reinsurance business, namely Indian reinsurers and FRBs.

Under the existing regime, the Order of Preference operates in two stages: a) pricing and terms and b) placement of reinsurance business. Indian insurers are required to obtain the most competitive quotes and terms for their reinsurance contracts from qualifying Indian reinsurers and at least three FRBs that have been set up in India. Such best terms/benchmark terms must then be offered for participation to qualifying Indian reinsurers in the first instance and only thereafter to eligible FRBs, with a third-level offering to branches of foreign reinsurers established in the tax-free hub of Special Economic Zones/ International Financial Services Centre (**IIO**). The balance reinsurance placements, if any, are permitted to be placed with Cross Border Reinsurers (**CBRs**). Currently, CBR’s do not even feature in the first stage i.e. procurement of quote (price discovery and others), whereas in the second stage i.e. placement of reinsurance; such overseas reinsurers find themselves in the last category.

It must be pointed out that more than 350 CBRs seek reinsurance placements in India. There are currently two Indian reinsurers and 10 FRBs, which also includes services companies of Lloyd’s.

The recently proposed draft of IRDAI (Reinsurance) Regulations, 2018 ("Proposed Regulations") have raised the profile of this issue and reflect relaxations (though limited) in the order of preference norms. CBRs and IIOs are now permitted to participate in the first step of the quotation process alongside Indian reinsurers and FRBs. For placement of reinsurance business, offers can first be made to FRBs and thereafter to IIOs or CBRs which provide lead terms with meaningful capacity of not less than 5% for treaties and 10% for facultative reinsurance business. Such placement restrictions limit the availability of business to cedants as well as likelihood of the business available to IIOs and CBRs. Allowing CBRs to participate in the procurement of quote is a step towards promoting healthy competition and right pricing, however their position in the second category limits the scope of their business.

Further, under the Proposed Regulations, retrocession placements of Indian reinsurers, FRBs and CBRs and reinsurance requirements of IIOs and Insurance Pools are not subject to the order of preference stipulations.

*Allowing CBRs to participate in the procurement of a quote is a step towards promoting healthy competition and right pricing.*

In another positive step, the status of the Indian reinsurer as the reinsurer of first preference in India would be removed in some insurance classes via the new proposed regulations. Indian insurers transacting direct insurance business in fire, engineering and marine hull would be exempt from the order of preference. Such relaxations allow for retrocession placements according to interconnected risks and factoring in the probability for large losses. Risks may now be retroceded as per the risk and requirements of each business.

This risk-based approach allows for larger benefits and a higher degree of protection. With the second preference provided to FRBs, entering the Indian markets becomes a more lucrative opportunity for foreign reinsurers, but it is a major point of contention for FRBs that the order of preference rules were introduced after the regulatory framework was established for foreign reinsurers to enter the Indian markets. The rules were designed to give an advantage to Indian companies, and FRB's now seek to be treated at par with their Indian counterparts.

Overall, the revision of the existing regime under the Proposed Regulations is a well-intended step. However, in finalizing the revisions IRDAI will now face the more difficult challenge of managing the contrary expectations of all stakeholders. On one hand IRDAI is expected to facilitate the creation of an open, competitive and transparent market with the best available pricing; and on the other it must keep in mind the commitment to maximize retention of business within the country and incentivise reinsurers to continue and/or open new branches. Given that India nurses the ambition to become a regional reinsurance hub, perhaps the balance currently tilts in favour of the latter.

All eyes are now set on IRDAI for its final decision on the adjustments to the Order of Preference.

***Sakate Khaitan, Partner, Khaitan Legal Associates***

# China eases rules on foreign investment

*In June 2018, member firm Buren reported on some major changes to the regime of foreign investment in China.*

By the end of June 2018, the regime of foreign investment in China has met two significant changes. One is a shortened Negative List for Foreign Investments (the "2018 Negative List") jointly released by National Development and Reform Commission (NDRC) and the Ministry of Commerce (MOFCOM) which becomes effective on July 28, 2018; the other one is the promulgation of the revised Interim Administrative Measures for the Record-filing of the Incorporation and Change of Foreign-invested Enterprises (the "2018 Interim Measures") by MOFCOM which takes effect on 30 June 2018. The two changes have signified China's firm determination on attracting more foreign investments by further opening-up to the world, and simplifying the governmental formality.

## The 2018 Negative List – opening-up market access

The Negative List includes a list of industries in which foreign investment is either prohibited or restricte0d. Restricted industries usually require investment through joint ventures with Chinese companies. For industries which are not included in the List, foreign investors are basically given equal treatment to domestic Chinese investors. Compared to the Negative List issued in 2017, the 2018 Negative List has a significantly reduced number of restrictive measures, from 63 to 48. Recent announcements of an opening in the financial services, agriculture, shipbuilding, aircraft manufacturing and auto sectors have now been reaffirmed in official documents.

A summary of the key opening-up measures for the 2018 Negative List can be found in the list below.

**The Negative List 2018**

1. Agriculture
2. Mining
3. Manufacturing
4. Wholesale and retail industries
5. Transportation, warehousing and postal service industries
6. Financial Industry
7. Scientific research and technological services industries
8. Cultural Entertainment

## 1. Agriculture

- Removed the equity requirement for the selection of new crop varieties and the production of seeds, except the restriction on wheat and maize.

## 2. Mining

- Removed restrictions on the exploitation and exploration of graphite and special/rare coal.
- Removed restrictions on the smelting and separation of rare earth and tungsten (although exploration and mining of tungsten is still prohibited).

## 3. Manufacturing

### 3.1 Automotive

- Will remove the restriction on foreign capital share ratio of special vehicle and new energy vehicle manufacturing in 2018.
- Will remove the restriction on foreign capital share ratio of commercial vehicle manufacturing in 2020.
- Will remove restrictions prohibiting a foreign company from setting up more than 2 joint ventures manufacturing the same kind of vehicles in China in 2022.

### 3.2 Shipbuilding industries

- Removed restrictions on design, manufacture and repair of ships.

### 3.3 Aviation manufacturing

- Removed restrictions on design, manufacture or maintenance of mainline/ regional aircraft, design and manufacture of helicopters of 3 tones or above, manufacture of surface/surface effects aircraft, design and manufacture of drones/aerostats and design, manufacturing and maintenance of utility aircrafts.

### 3.4 Manufacturing of weapons

- Removed restriction on the manufacturing of weapons and ammunition.

## 4. Wholesale and retail industries

### 4.1 Grain

- Removed restrictions on the acquisition and wholesale of rice, wheat and maize.

**4.2 Gas stations**

- Removed restrictions on foreign investors not being able to establish more than 30 branches of chain petrol stations and not being able to sell different types and brands of refined oil from multiple suppliers.

## 5. Transportation, warehousing and postal service industries

- Removed restriction on the construction and operation of railway trunk line network and railway passenger transportation companies.
- Removed restrictions on international shipping agencies and international maritime transport companies.
- Removed restrictions on foreign-invested-to-equity-ratio of passenger vehicles.

## 6. Financial Industry

- Removed the restriction stating that "shares of a single overseas financial institution and related parties under its control or joint control as the originator or strategic investors shall not exceed 20% in a single Chinese commercial banks; total share of multiple overseas financial institutions and related parties under its control or joint control as the originator or strategic investors shall not exceed 25%".
- Changed the allowed proportion of foreign investment in securities companies from 50% to 51% in 2018. Will lift the proportion restriction in 2021.
- Changed the allowed proportion of foreign investment in futures companies from 50% to 51% in 2018. Will lift the proportion restriction in 2021.
- Changed the allowed proportion of foreign investment in insurance companies from 50% to 51% in 2018. Will lift the proportion restriction in 2021.

## 7. Scientific research and technological services industries

- Removed restrictions on surveying and mapping companies.

## 8. Cultural Entertainment

- New restriction on investing in performing art groups.
- The 2018 Interim Measure – "One Window, One Form"
- The release of 2018 Interim Measures mainly serves as a further enactment and confirmation of the simplified registration formality reform for foreign-invested enterprises – "One Window, One Form" – as put forward earlier this year on February 28 in the Circular jointly issued by MOFCOM and the State

Administration for Industry and Commerce (SAIC). According to the Interim Measures, starting form 30 June, 2018, a foreign investor is able to incorporate a foreign-invested enterprise (FIE) by filling in one single form, electronically submitted, to one government office, insofar as the industry he invests in does not fall into the 2018 Negative List as introduced above. This means that a foreign investor no longer needs to go through the procedures with MOFCOM (i.e. record-filing of setup) and SAIC (i.e. registration of setup) separately. Which previously meant filling in the same information repeatedly. Furthermor the new process will be realized as fully "paperless", "no on-site presence", and "free of charge". It is believed that this new reform introduced will generally improve the service effectiveness and streamline the registration procedure, which in turn will reduce the burden of foreign investors.


***Jan Holthuis, Partner, and Li Jiao,***
***Senior Counsel, Buren***

# Mexico: facing critical changes, but room for optimism remains

*In December 2018, member firm Ocampo updated us on the changing political and investment situation for insurers and other corporates in Mexico.*

In July 1, 2018, the people of Mexico voted for the left-wing Morena party candidate Andres Manuel Lopez Obrador. He won the election with 53% of votes. As well as winning the presidential race, the Morena party also won a majority in the Mexican Congress, setting the scene for huge change in Mexico.  There are already indications as to how this will impact the insurance market in the region.

Mr. Lopez Obrador will assume the presidency in December 1st, 2018.  Morena is a radical left-wing party that has, for example, praised the strict socialist Venezuelan government – responsible for creating hyper-inflation in Venezuela in 2018 – as a successful model. Morena and Lopez Obrador have both referred to their new government as heralding what they call the Fourth Transformation (the first being the declaration of Mexican Independence; the second Reformation Laws of 1861; and the third the Mexican Revolution of 1910), so it is clear that the scale of expected change will be huge.

*There remains much uncertainty for foreign investors and corporations about business conditions and economic stability in Mexico under the presidency of Lopez Obrador.*

One of President Obrador's main endeavours is to fight corruption by creating new laws and an Anti-Corruption Agency, although there is little clarity as to how he intends to implement this campaign pledge as yet. Obrador has also rejected many of the current administration's policies. Once elected President, he has said that will cancel the construction of the Mexico New International Airport (claiming that its construction is too implicated in bribery and corruption). Instead, his proposal is to overhaul three airports surrounding Mexico City: Santa Lucía and Toluca; and to optimize the existing airport. This has already created a local scandal.

On the positive side, since the election, Mexico, the United States of America and Canada have ratified the T-MEC (USMCA) trade agreement, having received the newly elected President's approval on the terms and conditions. This successor to NAFTA (the previous

North American Free Trade Agreement) provides much-needed stability for international trade in the region and means that insurers and other financial services will continue to be regulated under a credible international framework, as they were under NAFTA.

Despite this, there remains much uncertainty for foreign investors and corporations about business conditions and economic stability in Mexico under the presidency of Lopez Obrador.

Currently, the Mexican insurance industry has a gold-standard regime, with insurers required to apply the Solvency II model to their finances. Corporate Governance is mandatory too. But the incoming president has announced the appointment of a new president of the Insurance and Surety National Commission (the Comision Nacional de Seguros y Fianzas or CNSF).

The candidate is without experience in insurance, although his resume says he has managed the administration of surety and bonds. However, he will be the first inexperienced President to head the Commission in thirty years. It is expected that many other existing directors will leave the Commission too, allowing for the appointment of new and inexperienced candidates. The new team will have to undertake a long learning curve, one that has great potential to impact the insurance sector.

On the positive side, trade credit will very likely be the beneficiary of the changing Mexican situation. The uncertainty brings opportunities for insurance and surety companies to write insurance, surety and bonds to cover the damages caused by breach of contracts, or the damages and prejudices that arise from such breaches. There are also other financial instruments under development to ease the trade.

Mexico faces a further challenge to update its laws to improve the regulation of e-commerce, mainly in the financial field. Insurtech is now being analysed by the industry and the Insurance and Surety Commission is waiting for the industry to propose new business models to start regulation in this area. We consider that the changes Mexico will be facing might just be a good opportunity to start a new insurance model - one relying on blockchain.

Meanwhile in the oil and energy Industries, the current administration has modernized the legal framework to allow private and foreign competitors to participate in oil extraction, although the state retains control. Lopez Obrador would like to return to a fully state-controlled oil and energy sector, and one which does not allow any participation by foreign companies. He is also proposing to build new refineries, instead of developing the renewable energy industry.

These are huge changes.  Mexico's legal system does provide the "Amparo" trial to challenge either judicial or administrative resolutions that affects citizens' constitutional and human rights. The Amparo is intended to limit the state's power over the citizens and as of now it has been a successful counterweight against misuse of legislative power.

Moreover, the Mexican Supreme Court has been very proactive in setting precedents in case law around issues such as punitive damages. In fact, since 2011 when the Constitution was amended to elevate human rights to a constitutional level, the Court have focused heavily on consumer and human rights and the Mexican Supreme Court has said that they are trying to implement a "Case Law" system creating precedents and criteria to be followed by the Federal and Local Courts.

As a conclusion, Mexico faces a period of great change, which will impact some of its key industries. While it may be that the beneficiaries of this change will be law firms such as ourselves, who are already finding our services in demand from international clients, we nevertheless find the context of the new demand for our services a worrying one.  For insurers this market continues to offer opportunities, alongside some very demanding challenges.

***Aldo Ocampo, Partner, Ocampo 1890***

# Italy looks ahead to Brexit

*In October, member firm BTG updated clients on how to manage the impacts of Brexit for the insured in Italy.*

On 3rd October 2018 the Italian insurance supervisory authority IVASS sent a letter to all UK insurance undertakings operating in Italy about the information that they need to provide to Italian policyholders on the impact of Brexit.

IVASS referred to the "Opinion on disclosure of information to customers about the impact of the withdrawal of the United Kingdom from the European Union" issued by EIOPA on June 25, 2018*, and (by reference to the Freedom of Establishment and/or Freedom to Provide Service provisions) required all relevant bodies to:

**a.** Issue adequate information about the impact of Brexit on their Italian policyholders and beneficiaries, in accordance with the above EIOPA publication (this highlights the importance of all being made aware of the implications of Brexit "both for existing and for new contracts concluded before the withdrawal date in due time and are provided with clear and non-misleading information on the contingency measures taken or planned and on their impact on their insurance contracts");

**b.** Publish similar information on their websites;

**c.** Suitably instruct their information and distribution networks about the information to provide to current, and also potential, policyholders.

By 30th November 2018 all UK insurance undertakings operating in Italy must detail their plans in these respects and confirm that they have been carried out.

***Alberto Batini, Partner, BTG Legal and GILC Board Member***

# Insurance Distribution Directive delayed in Belgium

*In September, member firm Lydian shared information about the consequences of Belgium's delayed implemented of the EU's Insurance Distribution Directive.*

On 20 January 2016, the European Council adopted the Insurance Distribution Directive (IDD). The purpose of this directive was to create a level playing field among the distributors of insurance products, to strengthen the confidence of customers and to make regulatory treatment of the distribution of insurance products more uniform in order to ensure an adequate level of customer protection across the European Union.

The original transposition and entry into force deadline was 23 February 2018. In March 2018, the European Parliament delayed the transposition deadline until no later than 1st July 2018, and the entry into force deadline until 1st October 2018 at the latest.

Belgium, however, has not been able to implement the IDD into national law within these deadlines. A directive is only completely transposed/implemented into national law when all the objectives set out in the directive have been met. Belgium in the meantime adopted one Act and one Royal Decree (the Act of 31 July 2017 amending the 2 August 2002 Act on financial sector supervision, with respect to whistle-blowing, and the Royal Decree of 5 September 2017 approving the FSMA Regulation on the same). Those legislations are far from adequate to satisfy the objectives of IDD.

What, then, are the consequences of this delay?  When a directive is not implemented on time, its articles are granted 'direct vertical effect'. This means that, on certain conditions, individuals can rely on it in relations with the government. Individuals cannot invoke the articles of the directive against insurers, since they are not part of the government.

The Insurance Act of 4 April 2014 and the AssurMiFID regulations remain in force until the Belgian legislator modifies them.  The European Commission could launch an infringement procedure against Belgium. We admit such a risk is rather unlikely as the new IDD provisions are expected to enter into force during the month of October.


***Sandra Lodewijckx, Partner, and Anne Catteau, Senior Associate, Lydian***

# Subrogation in Switzerland – no longer perforated as a Swiss cheese

*In September 2018 member firm GBF described a landmark ruling in Switzerland that brought changes to the unique Swiss rules around subrogation for insurers and the insured.*

Around the world it seems to be clear that, once a property insurer indemnifies the assured, the insurer steps into the assured's shoes to seek recovery for its loss from those parties which caused the loss and that are liable to the assured. In short, this is the principle of subrogation.

The situation in Switzerland is, however, different. The whole jurisprudence in this respect originates from an old judgment of the highest court in Switzerland, the so called Gini/Durlemann case of 1954. In this case, the Claimant insurance company insured a cottage of one Peroni against fire. Peroni instructed Gini to paint his cottage, but the actual work was performed by Durlemann, one of Gini’s employees. Before Durlemann painted the cottage he tried to remove the old coating by heating it with a blowlamp. Unfortunately, there were easily flammable wood shavings inside the cottage, which Durlemann forgot to remove. The wood shavings caught fire and the cottage burnt down. The Claimant indemnified Peroni for the loss and then pursued its recourse claims against Gini, based on the contract for work and labour with Peroni.

What did the Supreme Court decide? It surprisingly held the employer, Gini, not liable on the following grounds: the Swiss Insurance Contract Act comprises only one provision on subrogation: Article 72. Article 72 solely deals with recourse claims against third parties liable in tort. For contractually liable parties there is no similar provision, hence the Court had to apply general contract law.

Article 51 of the Swiss Code of Obligations (CO) provides that, if several persons are liable to the aggrieved party for the same damage based on different legal grounds, these persons shall be jointly and severally liable to the aggrieved party. For the internal recourse amongst the liable parties, the damage shall then be primarily compensated by the person who caused it by negligence, then by the party liable in contract (without fault) and in the last instance by a person whose liability is based on causality only (i.e. strict liability without a contract and without negligence). For instance, if a contractually liable party, Party A, indemnifies the aggrieved party and if there is also a Party B who actually caused the loss through negligence, Party A would be able to hold itself harmless from the negligent Party B, but not vice versa.

The Supreme Court further argued that any recourse claim of an insurer against the contractual third party of the assured is a question of internal recourse between two contractually liable parties. Neither Gini as the contracting party with Peroni nor the Insurer acted negligently. Their liability was, hence, based on contract only (without any fault). In terms of internal recourse, both parties were on the same level and such issue was not solved by Article 51.

The Supreme Court held the insurer shall only be entitled to hold itself harmless from Gini, if it can prove his employee Durlemann caused the loss through gross negligence, at least. One argument for that outcome was that, if an assured seeks coverage from its insurer, the insurer can reduce the indemnity or deny it in full when the assured itself caused the damage by gross negligence or with intent. As a result, when the insurer assesses premium for its policy it assumes damages caused through negligence (but not gross negligence) are covered. If the insurer is unable to prove gross negligence, which can quite often be tricky, it does not step into the assured's shoes.

*In its latest ruling, the Federal Supreme Court decided to significantly change the previously practice... Contractual parties of the assured will then no longer be better protected than in other countries.*

A further result of the Gini/Durlemann case was that the insurer does not have a claim for recourse against a person whose liability is based on strict liability only because the property insurer on level two cannot take any recourse against a strictly liable party that is on Level three pursuant to Art. 51 CO.

In its latest ruling, however, the Federal Supreme Court decided to significantly change the previous practice. In its Judgment of 7 May 2018 (case no. 4A_602/2017), the Federal Supreme Court considered that any statutory liability (inclusive of strict liability) is covered by the notion of "obligation in tort" under Art. 72 (1) ICA, even if there is no fault. Art. 51 (2) CO on the internal recourse among multiple liable parties would no longer apply to the recourse of the insurer against the person causing the loss or damage and being liable under strict liability provisions.

The Federal Supreme Court thus allows the insurer's recourse against persons who are liable under strict liability provisions (such as principals or landlords), even if they caused the damage without actual fault. E.g. a property insurer is now also entitled to take recourse against the principal (e.g. the employer), who has a strict liability for the misconduct of his employees towards third parties (including contracting parties of the principal) according to Art. 55 CO. That was not possible before this judgment.

Whether the Federal Supreme Court will deviate from the Gini/Durlemann practice as such is not explicitly stated in the named Judgment of 7 May 2018. After all, the Federal Supreme Court agrees with the criticism expressed in the doctrine that the insurer was wrongly deemed to be a person liable by contract as defined in Article 50 seq. CO, although it performs the insurance contract and does not pay compensation for non-performance or defective performance of the contract. We therefore consider it very likely that the Gini/Durlemann ruling will no longer find support in future trials. Contractual parties of the assured will then no longer be better protected than in other countries.


***Lars Gerspacher and Cem Arikan, gbf Attorneys-at-law, Zurich***

# UK Supreme Court ruling brings changes to the claims’ limitation period

*In December member firms BLM, GBF and BTG shared a discussion on the impact of a UK Supreme Court decision on the limitation period for claims*

The recent UK Supreme Court Decision on grounds for the suspension of the limitation period under the Athens Convention benefits minor Scottish pursuers but, in discussing the Court of Appeal decision in Higham v Stena Line, the Supreme Court has left something of a grey area for England and Wales.

## Background

The Pursuer was the infant son of a diver who died at sea on 14 August 2012. A claim was brought on their behalf, and was issued on 14 May 2015, 2 years and 9 months following the incident. Scapa Flow Charters applied for the matter to be struck out due to the limitation period in the Athens Convention and the issue was appealed to the Supreme Court.

## Issues

The key issue concerned article 16 of the Athens Convention, which would have required suit to be brought within two years of the date of the deceased’s disembarkation, no later than 18 August 2012 in this case. The Convention provides, however, that the law of the Court seized of the case can govern “suspension or interruption” to this period, provided proceedings are issued within three years of disembarkation.

The Prescription and Limitation (Scotland) Act 1973 was the relevant Scottish legislation for the issue. To paraphrase, this provides that if the pursuing relatives of the deceased are not of legal age, the period until they reach legal majority (16 in Scotland) is disregarded in the computation of the Limitation Period.

Scapa Flow Charters argued that this was not a suspension or interruption within the meaning of article 16. A suspension could only occur if it arose after the limitation period had begun, which was not the case in the current matter. The arguments put forward in support of the position were:

- The meaning of “suspension” must mean a provision which gives rise to a break in a course of events already in train, as discussed in Higham; and

- That the words “suspension or interruption” should have a technical meaning adopted from certain civil law systems for the sake of certainty. They pointed to international definitions whereby a suspension operates to pause a limitation period which has started to run, and resumes such period running after the issue suspending limitation, such as mental incapacity, ceases.

Thus, they argued that the Scottish Act could not suspend the limitation period, as it opted to postpone it by disregarding the period in which the Pursuer was a minor.

## The Court’s Decision

The Court has clarified the approach in Scotland, in that the wording in the Prescription and Limitation (Scotland) Act 1973 does suspend the limitation period in the Athens Convention in the case of minors, addressing SFC’s arguments as follows:

A technical approach to interpretation of the words “suspension and interruption” should not be adopted for the following reasons:

Conventions are supposed to be international, and thus the Court felt it was not appropriate to look at the domestic law of certain systems for a technical meaning of words which are applied in many common law systems. Thus, a broad approach should be adopted, and in any event the Court found that the word “suspension” can readily cover postponement as in the Scottish Act.

The Court found that there was no international consensus regarding the meaning of “suspension” when the Athens Convention was adopted. As such, there was no support for SFC’s argument for the case of certainty, particularly as it is undisputed that the 3 year long-stop period in the convention operates ‘across the board’ in any event.

Adopting such an approach would lead to ‘serious anomalies’ in its application, such as covering only mental incapacity that post-dated an incident and disregarding mental incapacity that pre-dated an incident.

The Higham definition of “suspension” referred to in the judgment included postponement as one of its definitions, and as such the postponement in Scottish law was a “suspension” under the Convention. In any event, as previously discussed, the Court had determined that “suspension” has a broader, rather than technical, meaning in different legal systems.

## Discussion

The Court's decision on the matter strayed beyond the Scottish issues above, into a discussion regarding the provisions of the English Limitation Act 1980 and the Athens Convention.

The judgment provides clarity in Scotland. It appears that in Scotland minor pursuers now have three years in which to issue proceedings for incidents at sea causing injury, or when pursuing a claim arising out of the death of a relative. The provisions for personal injury claims under the Prescription and Limitation (Scotland) Act 1973 concerning injury claims for minors and those without capacity mirror those discussed in this case and will doubtlessly apply in all injury claims for minors.

The Court also reaffirmed that judicial discretion cannot be used to disapply the two year time limit in the Athens Convention, in Scotland, England or otherwise.

## England and Wales

In Higham the Court of Appeal opined, obiter, that as certain provisions in the Limitation Act were said to apply to periods "prescribed by this Act", they may be disqualified from having any application to the provisions in the Athens Convention. The Supreme Court has disagreed with this argument and clarified that provisions in the Limitation Act are not disqualified from applying to the Athens Convention. In particular, they have stated that section 32 of the Limitation Act 1980 which postpones limitation in certain cases of fraud, concealment or mistake will suspend limitation under Article 16.

And so we come to the 'elephant in the room', what about minor claims in England and Wales? The Supreme Court has, rather interestingly, focused on s. 32 of the Limitation Act, and not referred at all to s.28, which extends the limitation period for minors and those without capacity. So the question is, is an "extension" under the Limitation Act a "suspension" under the Athens Convention? The answer appears to be that it is. The approach of the Court in this case was to adopt a broad approach in favour of the minor pursuer, which indicates the likely approach in future. Further, the following comment made in the judgment is almost certain to be used by Claimants in arguing this point if the issue is raised in England: "…In my view, where article 16(3) speaks of the law of the court seized governing "the grounds of suspension… of limitation periods" (in the plural) it was applying the grounds – such as minority or incapacity – which the lex fori would apply to domestic claims for personal injury, or death or loss or damage to property…"

The mention of minority or incapacity is likely to be highly influential when a Court comes to assess whether the extension under the Limitation Act is a suspension under the Athens Convention.

This will be a disappointing decision for carriers and insurers alike as it raises uncertainty concerning the rules, particularly in England and Wales, and could result in complex and costly arguments regarding limitation.

***Gemma Pearce, Marine Special Interest Group Team Leader and Partner BLM, UK***

## View from Switzerland

You may wonder why the Athens Convention is of any relevance in Switzerland, a country that does not have any direct access to the sea. The passenger's ticket may provide for Swiss law to apply. Such choice of law is, in principle, binding among the carrier and the passenger. However, the passenger may ask the court to apply the law of the state in which he or she has his/her ordinary residence if, for instance, he or she received the offer for the journey in this state (art. 120 of the Swiss Private International Law Act).

Under Swiss law, the 1974 Athens Convention as well as the 1976 Protocol apply. The 1990 Protocol has not been adopted by Switzerland.

In accordance with art. 17 of the Athens Convention a Swiss court may be competent to deal with passenger claims.

***The wording of art. 16 of the Athens Convention***

According to art. 16 para. 1 of the Athens Convention "any action for damages arising out of the death of or personal injury to a passenger or for the loss of or damage to luggage shall be time-barred after a period of two years.

Para. 3 provides that "the law of the court seized of the case shall govern the grounds of suspension and interruption of limitation periods, but in no case shall an action under this Convention be brought after the expiration of a period of three years from date of disembarkation of the passenger or from the date when disembarkation should have taken place, whichever is later".

Para. 4 provides that “the period of limitation may be extended by a declaration of the carrier or by agreement of the parties after the cause of action has arisen. The declaration or agreement shall be in writing”.

***The UK Supreme Court case***

The Scots law of limitation enacted in section 18 of the Prescription and Limitation Act 1973 did not contain “grounds of suspension and interruption” as to extend the limitation period. It only postponed the start of the limitation period, in the case at hand, for minors. The Supreme Court concluded that a “suspension” in its natural meaning could also cover the postponement of the start of a limitation period. Therefore, the claim of the minor that has been brought after two years but before the three years deadline was not time-barred.

***Suspension and interruption in Switzerland***

Swiss law applies “suspension” and “interruption” to all civil claims. Suspension refers to the situation in which a limitation period does not commence and, if it has begun, is paused by a situation, such as the duration of an employment, and then resumes its running when the situation ceases (art. 134 Swiss Code of Obligations). Interruption refers to an event in which the limitation period, having been halted by an event such as debt enforcement, commences afresh for the full duration (art. 135 Swiss Code of Obligations).

In Switzerland there is no  postponement of the start of a limitation period for a minor’s claim against a carrier (unless the carrier is the minor’s father or mother; see art. 134 para. 1 no. 1 Swiss Code of Obligations). If the claim was presented under Swiss Law, then the minor’s claim would have been time-barred.

This being said, art. 16 para. 3 of the Athens Convention does not really fit into Swiss law by any other means. Suspension and interruption, in principle, are possible for eternity. In other words, a passenger would be able to interrupt and/or suspend the limitation period as often as he or she likes. The claim would then not be time-barred at all. If a carrier wishes to challenge and clarify the uncertainty it would have to file a negative action for a declaratory judgement (i.e. a judgement that confirms that the carrier owes to the passenger either nothing or a certain amount). The provision on limitation periods now suggests the following “but in no case shall an action under this Convention be brought after the expiration of a period of three years”, which would be unusual. At first sight, many lawyers would say the three year period is not a limitation period but rather a preclusion period where the passenger loses his or her right for damages completely after three years. Such deadline applies, for instance, under the Montreal Convention

(Convention for the Unification of certain Rules for International Carriage by Air), art. 35 of which reads under the title of “limitation of actions” as follows: “The right to damages shall be extinguished if an action is not brought within a period of two years, …”

The Athens Convention however does not use the word “extinguished“, it only provides that the right to damages may no longer be brought as an action before court. The other original version, the French one (the official language in Switzerland) reads as follows: «Délai de recours L’action en responsabilité doit être intentée, sous peine de déchéance, dans le délai de deux ans…»

In comparison to the Montreal Convention, the French wording of the Athens Convention does not speak of “déchéance” (i.e. forfeiture) but only of “prescription” and “délais de prescription” (i.e. limitation and limitation period). Also the German translation uses the terms “Verjährung” and “Verjährungsfrist” (i.e. limitation and limitation period) for art. 16 of the Athens Convention whereas for art. 35 of the Montreal Convention the word “Ausschlussfrist” (i.e. preclusion period) is being used.

The above seems to afford clarity, unless you read the Italian translation, another official language in Switzerland. Both, art. 16 of the Athens Convention and art. 35 of the Montreal Convention use the term “prescrizione” which means limitation period. The translation of art. 35 of the Montreal Convention should rather have used the term “perenzione”, used in Swiss law for the forfeiture of rights, i.e. for a preclusion period.

Switzerland faced the same language problems when they included the provisions of The Hague-Visby Rules into the Swiss law, in particular regarding the preclusion period as per art. III, section 6, of the Hague-Visby Rules that reads as follows: “… the carrier and the ship shall in any event be discharged from all liability whatsoever in respect of the goods, unless suit is brought within one year of their delivery or of the date when they should have been delivered. This period, may however, be extended if the parties so agree after the cause of action has arisen.”

The wording of the above clearly provides for the forfeiture of the rights to damage after one year. But the provisions of The Hague-Visby Rules are not directly applicable in Switzerland. When incorporating the rules into the Federal Act of 23 September 1953 on Navigation under Swiss Law, the preclusion period became a limitation period (art. 87 of the Navigation Act). Interruption and Suspension, therefore, is possible for eternity as described above.

Not only the strict limitation of the interruption and suspension tends, from a Swiss law perspective, to the forfeiture of rights but also para. 4 of art. 16 of the Athens Conventions according to which the limitation period can be extend by agreement or declaration of the carrier could cause confusion. Under Swiss law, it is clear and completely undisputed that such extension of the limitation period by agreement or declaration is possible. This holds true for many jurisdictions, I think. Why would one explicitly include such obvious possibility as a separate paragraph? From a Swiss point of view, such inclusion would make much more sense if the passenger's right would extinguish after the three years. In case of forfeiture of rights, it is not entirely clear whether the parties are able to prevent such forfeiture by mutual agreement or declaration of the defendant. It would, therefore, make much more sense to clearly stipulate in the convention that such extension is possible. This is exactly what happened in the Hague-Visby Rules (see above).

To sum up, art. 16 para. 3 of the Athens Convention provides for a limitation period of (maximum) three years that one cannot extend, unless the carrier agrees to such extension in accordance with para. 4 of art. 16. As lex specialis, such deadline prevails over the Swiss code of obligations according to which limitation periods may be extended by suspension and interruption eternally. Art. 16 para. 3 of the Athens Convention does not provide for the rights to be extinguished. The rights still exist after the lapse of the three years periods but cannot be brought as an action to court. But the passenger may still set off such claim against any possible claim that the carrier may have against him or her.

***Nando Stauffer von May, Partner gbf Attorneys-at-Law, Switzerland***

## View from Italy

Italy applies Annex I to the REGULATION (EC) No 392/2009 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 23 April 2009 on the liability of carriers of passengers by sea in the event of accidents. Annex I effectively embeds the Athens Convention 1974 as amended by the 2002 Protocol into the EU instrument.

In particular Art. 16 (Time bar of actions) of the Annex I of said EU Regulation – Para. 1,2 and 3 – provides for a two year time bar limitation period and refers to the law of the Court seized to govern suspension and interruption of limitation periods. In no case, however, shall an action under the Convention be brought after the expiration of any one of the following periods of time:

- a period of five years beginning with the date of disembarkation of the passenger or from the date when disembarkation should have taken place, whichever is later; or, if earlier;

- a period of three years beginning with the date when the claimant knew or ought reasonably to have known of the injury, loss or damage caused by the incident.

The Rule goes on to provide that, notwithstanding paragraphs 1, 2 and 3 of the Article, the period of limitation may be extended by a declaration of the carrier or by agreement of the parties after the cause of action has arisen.

This discipline is in fact identical to the one dictated by Athens Convention, so time extensions (or Parties agreements) are allowed in Italy in case the Parties should mutually decide to extend the limitation periods beyond the three or five years.

Under Italian law there are two types of limitation periods. The first is an 'extendable' time bar, subject to being interrupted by a simple registered Letter of Claim. The second type is the 'rigid' time bar, which can be interrupted only by way of Court action. Usually only the extendable time bar could be derogated by a time extension or agreement between the parties, while the rigid time bar does not allow interruptions beyond the Court lawsuit remedy. The Athens Convention 1974 and the corresponding EU regulation No. 392/2009 who incorporates the Convention as EU legislation does in fact provides, from an Italian law perspective, a hybrid institute, which is the "relatively rigid" time bar, where the three or five years' time bar could exceptionally extended only by time extension or parties written agreement. This is a unique institute under Italian law which applies strictly to cases subject to the EU Reg. 392/2009 and 1974/2002 Athens Convention but will not be applicable beyond the scope of such harmonized legislation. There are no recent relevant court decisions on the subject matter in Italy.

***Alberto Batini, Senior Partner BTG Legal, Italy***

# Labor law alert – union dues in Brazil

*In June 2018 member firm Santos Bevilaqua Advogados gave an update on a Brazilian Supreme Court ruling which impacted employers in Brazil, as well as announcing the creation of a new industry group for reinsurers in Brazil.*

On 29$^{th}$ June 2018, the Brazilian Supreme Court ("STF") dismissed 20 direct challenges of unconstitutionality (ADIN n. 5794), which had been filed by various union entities, by a majority (6 votes to 3). The court declared the constitutionality of the point of Labor Reform (Law 13,467/2017), which eliminated the mandatory nature of paying union dues.

As a reminder, in short, with the advent of Labor Reform (on 11/13/2017), union dues became voluntary, and the interested party must now expressly consent to having labor dues withheld to be paid to their respective union, whether the employer or employee. This represents a new paradigm to the way the Brazilian labor union system will finance itself, which could potentially have a major impact on the union structure as a whole.

Under these circumstances, even though appeals are still possible, the Supreme Court's ruling is an important step towards settling this matter; in addition, of course, to the law now being fully in force, until and unless a future court decision to the contrary is handed down.

# Brazilian reinsurance group launched

Santos Bevilaqua is working together with SUSEP (the Brazilian Insurance Supervisor) and the Brazilian Reinsurance Companies Association, in the elaboration of new regulations to develop a Latam insurance and reinsurance hub in Brazil. The group has already discussed the new resolution about risk transfers from abroad to Brazilian local reinsurers, to be probably issued in September 2018. The group is also discussing changes in the regulation to make feasible the securitization of risks through insurance linked securities in the Brazilian capital markets.

***Juliano Castro, Partner,***
***Santos Bevilaqua Advogados***

# Insurance implications of the Genoa bridge collapse

*After a motorway bridge collapsed suddenly in Italy in mid-2018, member firm BTG wrote for Insurance Day about the consequences for the Italian insurance market.*

Natural and man-made disasters in the first semester of this year hit at a global level 36 billion dollars in economic losses. Out of these $34bn are NatCat (earthquakes and weather-related disasters). The remaining $2bn are related to man-made disasters. Out of the total, $20bn were insured, while $16bn were not. The amount of insured losses increased compared to last year, where $34bn out of $64bn of natural and man-made disasters stayed uninsured.

An educated guess from JP Morgan analysts estimated that the recent Genoa bridge collapse will cost the insurance and reinsurance industry between 400 and 600 million euros overall. The greatest part of the insured damages concern the property and the business interruption sectors. The main exposures are the property damages to the public infrastucture (bridge) and, immediately after, the BI for the motorway concessionist Autostrade per l'Italia Spa (ASPI). In addition to these, other exposures are the third party liability, including motor and life insurance subrogations, as well as business interruption of the railway line.

Financial lines covers will also presumably kick in at some point, including D&O of the concessionist managers and officers, considering the ongoing criminal investigations and the future possible civil action for damages from victims' heirs. However, since the causes of the incident are not yet assessed with a required degree of certainty, it is not possible at this stage to draw conclusions on Maximum Possible Loss reserves.

All in all it is likely that the different policies involved will be probably limited and, for this reason, notwithstanding the fact that the disaster is potentially very high, it is unlike that the event will significantly affect the three groups of insurers/reinsurers involved (Allianz, Swiss Re and Talanx, Hanover Re Group). For Talanx analysts estimate an insured loss around 20 million Euro. For Allianz the estimate is around 50 million euros and for Swiss Re around 70 million euros (Source: Assinews).

In the above respect it is worthwhile to note that the main deficiency in terms of coverage, according to MF (Milano Finanza), might concern the third party civil liability claims. The maximum insured amounts here are reported to be around 100 million euros, definitely below the expected level of indemnifications for each of the 43 victims (estimated around 700-800 million euros each). The property cover affords a maximum insured amount of 300 million Euros. Such amount might be sufficient for the reconstruction of a new bridge but possibly not to cover demolition costs in view of the complexity of the operation. So another shortfall may come from here.

Currently, existing natural disaster insurance schemes are under financial distress in a number of countries. Furthermore, many countries, such as Italy, do not have an adequate system of protection against the financial and economic consequences of natural disasters. Italy is one of the European countries with the lowest penetration of NatCat insurance, considering that penetration rates vary very much in the EU Member States. So Italy is characterised by a public dependency on government support in the wake of disastrous events but such a system can no longer be afforded to cover all financial losses.

At this point in time, other infrastructure owners and managers in Italy should carry out a full review of their insurance and reinsurance schemes as well as rethink their risk management policies. The challenge here is to avoid, inter alias, possible legitimate exceptions by insurers based on non-disclosures or aggravation of risk, particularly where engineering deficiencies or infrastructure fragilities became known but insurers were not informed upon renewal. Insurability is based on the declaration of the insureds about whether or not the building complies with the technical regulations that were in effect when it was constructed.

For what concerns the Italian law, this is the basic function of the legal provisions established by articles 1892 and 1893 of the Italian civil code.

The deterrence effect against non-disclosure is even stronger than in common law, in the case of fraudulent intention: the insurer can refuse to pay the claim while keeping the premiums. When inaccurate information has been provided by the insured without fraudulent intention, Italian law provides that the benefit paid in case of occurrence of the loss is reduced to account for the higher risk (art. 1893). A similar rule applies in case of risk worsening after the insurance contract is concluded (art. 1898). Under Italian law the insured has the duty to disclose all subsequent, material information relating to the magnitude of the risk, even after the insurance has been purchased. If such duty is not fulfilled and hidden information is not otherwise detected by the insurer, the claim the latter has to pay in case of occurrence of the loss is reduced to account for the higher risk. The insurer can even refuse to pay the claim when the information at issue, if known, would have influenced his decision to accept the risk.

To help manage risks to assets, a public entity should carry out a risk assessment to decide whether to insure assets, and, if it does decide to insure them, the appropriate insurance cover. That assessment should use accurate, up-to-date valuations that consider matters such as indemnity value, replacement cost, maximum probable loss, demolition costs, and inflation.

After a risk assessment, a public entity may choose not to insure its assets – it may choose to self-insure. This is where the public entity chooses not to insure the asset because the cost of damage to, or loss of, its assets can be met from cash reserves, borrowings, the Government, or funds that a group of entities have pooled together to help meet such costs.

It becomes important therefore for infrastructures managers and owners to achieve a better understanding of:

- the nature of insurance cover of public assets;
- the extent to which those assets are uninsured;
- any significant policy exclusions that mean assets are not covered for certain types of events (such as earthquakes and tsunamis);
- the proportion of claims that public entities will not be able to recover (that is, the "excess" or "deductible" under the insurance policy);
- other public assets that may require insurance (for example, investments, investment property, and intangible assets), and
- other types of insurance may be obtained (for example business interruption, professional liability, and new construction insurance).

In the past, public disaster relief was often followed by new tax burdens (additional income tax or VAT tax) or other taxes (increase in the excise tax on petrol) that applied to all citizens. In addition, these taxes were not eliminated once the repair or reconstruction work was completed. It is highly likely that, also in the case of this last disaster, most of the insurance shortfall will be covered through additional taxation. So Italy therefore needs to reconsider the level of insurance penetration in NatCat and man-made disasters, which at the moment appears very low.

***Alberto Batini, Partner, BTG Legal***

# Resolving product liability disputes in China

*An overview of a seminar held in September 2018 on product liability disputes in China – co-hosted by member firms Buren and BLM.*

Accessing pragmatic expert advice about product liability claims in China is a major challenge for insurers and businesses. The Global Insurance Law Connect presentation at BLM's London offices by Chinese member firm Buren on 13 September confirmed that while the court system may be unpredictable at times, using local expertise with experience of using the court process for the benefit of western clients, can provide realistic advice and a potential path to successful recovery from manufacturers and suppliers based in China.

Jan Holthuis and Li Jiao updated an audience of insurers and corporate clients and provided a comprehensive overview of potential causes of action, limitation periods applicable to each, and procedure when bringing claims in China and/or relying on Chinese law. It became clear that while there may be similarities with western jurisdictions and law as to the legal tests, such as burden of proof, and measures of losses to be applied, the key to success is understanding how the courts operate and how judges will approach disputes.

Interestingly, claims in tort provide an avenue for claiming pure economic loss, whereas of course this is not available under English law save in extremely limited circumstances. However, a key issue is being able to provide sufficient evidence to satisfy a Chinese court, including being able to prove how a payment by an insurer in the UK can be evidenced in China, and justified as necessary and/or reasonable in English law, before it can be recovered in Chinese proceedings; and understanding the rules as to use of expert evidence which will be accepted by local courts.

Similarly, access to the judiciary is very different. Judges express opinions at an early stage, often through personal phone calls to a party's lawyer without the other party's lawyer being present (or even knowing), and indicate whether the judge considers the evidence is satisfactory or not. There is general distrust of lawyers by the Chinese courts, and the evidence presented is scrutinised with scepticism, particularly where not supported by original documentary evidence.

Specific local factors can also have an effect on the outcome of a claim.  Knowing how to use a local process is critical and Jan and Li provided examples of successful claims through the Chinese courts on behalf of insurers.

The presentation was very well received and provoked interesting questions and discussion.  It also highlighted the strength and capability of the network and its member firms to handle and advise on cross-jurisdictional claims involving China and Chinese law.


***Jim Sherwood and Michael Harvey, BLM, UK***


***Jan Holthuis and Li Jiao, Buren Legal, China***

# Considering alternatives to "reverse bad faith" claims

*Member firm Foran Glennon Palandech Ponzi & Rudloff on the evolving views in different US states around "reverse bad faith" claims by an insurer against its insured.*

While an insured's claim against its insurer for bad faith is recognized in most jurisdictions, there is no corresponding recognition for a "reverse bad faith" claim by an insurer against its insured. As a concept, "reverse bad faith" is an action by an insurer against its insured "when the insured wilfully submits a fraudulent claim and then sues the insurer in tort for the insurer's 'bad faith' in refusing to pay the fraudulent claim. However, even after considering the public policy reasons for allowing a reverse bad faith claim, and acknowledging wrongdoing by insureds, courts have been unable, or unwilling, to take the next step, and recognize a "reverse bad faith" cause of action. This article analyzes courts' reasons for refusing to accept "reverse bad faith" claims, and alternatives to a "reverse bad faith" claim.

## Failing to accept "reverse bad faith"

Over the past few decades, insurers have attempted to plead "reverse bad faith" to no avail. Insurers' arguments are usually based on public policy. Specifically, insurers have argued that there is strong public policy against accommodating insureds attempts to profit by filing false or incomplete claims in the hopes of reaping the benefits of suing the insurer for bad faith failure to settle or delaying settlement. Those benefits include expedited and greater settlements in order for the insurer to avoid the high litigation costs of defending a bad faith claim. The increased litigation and settlement costs for such claims will likely raise premiums for all policyholders, and result in financial harm to shareholders. Accordingly, a "reverse bad faith" cause of action would deter false or incomplete claims and frivolous bad faith actions, thus serving a legitimate public purpose. Courts have yet to be persuaded.

Generally, courts have held that the public policy implications of an insured's special relationship with its insurer trump the public policy reasons cited by insurers. For example, in Agricultural Insurance Co. v. Superior Court, 70 Cal.App.4th 385 (Cal. Ct. App. 1999), the insured's property was damaged by an earthquake. Following the earthquake, the insured submitted a claim to its insurer. The claim was partially paid, but controversies between the parties arose, and the insured sued for bad faith and breach of contract. After an investigation revealed that the insured "had deliberately misrepresented and concealed material facts," the insurer cross-claimed to plead, among other things, "reverse bad faith" and fraud. The court, however, held that a claim of “reverse bad faith” does not exist. Although there is an implied covenant of good faith and fair dealing in every contract, although each party is bound to it, and although this principle applies to insurance contracts, the potential liability for breach is different for insurers and insureds.” Furthermore, the court stated that the insurer’s exposure to potential liability for acting in bad faith “flows from special factors which do not apply to the insured. It identified those special factors as the fiduciary responsibilities owed by the insurer to the insured, the adhesive nature of insurance contracts, and the dilemma faced by insureds in paying for damages if the insurer breaches the contract. The court also rejected the insurer’s arguments that business entities controlled by wealthy individuals (like the plaintiff in Agricultural), have equal bargaining power, and thus, should be subject to tort liability. Even if the insured had equal or even greater bargaining power than the insurer, the court stated that the insurer provided “no basis for a ruling that the same words in an insurance policy can impose varying duties on different insureds according to their respective levels of wealth. Accordingly, the Agricultural court’s “special factors” provided the basis for denying the claim for reverse bad faith.

The Sixth Circuit applied a similar reasoning in State Auto Property and Casualty Insurance Co. v. Hargis, 785 F.3d 189, 196 (6th Cir. 2015) in rejecting the insurer’s argument for reciprocal application of Kentucky’s Unfair Claims Settlement Practices Act (“KUCSPA”). State Auto’s argument was based on the strong public policy against allowing insureds to profit from their own wrongdoing while simultaneously subjecting insurers to inordinate increased costs for investigation, defense, and litigation.” Further, the insurer argued that “without reverse bad faith, insureds can take a ‘no risk gamble’ by seeking punitive damages, while their insurers (and by extension shareholders and policyholders) bear the burden of the high investigation and defense costs associated with those [bad faith] claims.” In rejecting State Auto’s arguments, the court relied on the reasoning of the Supreme Court of Kentucky in Farmland Mutual Insurance Co. v. Johnson, 36 S.W.3d 368, 379-80 (Ky. 2000):

Insofar as the exclusion of the insureds from the scope of KUCSPA is concerned, the legislative decision to exclude the insured from the class is reasonable and natural. One reason for this distinction is that the insured is not in the insurance business. A second reason is that a bad faith action is based upon the fiduciary duty owed by an insurance company to its insured based upon the insurance contract. The KUCSPA is designed to “protect the public from unfair trade practices and fraud.” Furthermore, the disparate bargaining positions of an insured and an insurer following a loss are sufficient to justify treating the insureds as a different class for purposes of inclusion within the scope of the act. 36 S.W.3d at 380.

State Auto Property and Casualty Insurance Co. v. Hargis, 785 F.3d at 196. Other states have similarly rejected the public policy arguments addressed in State Auto in refusing to recognize a "reverse bad faith" cause of action.

Given the decisions regarding the viability of a "reverse bad faith" claim, it is hard to disagree with Couch on Insurance that the utility of "reverse bad faith" is "more illusory than real. It must be remembered, however, that not every jurisdiction has heard a "reverse bad faith" claim. Further, though courts have yet to be persuaded, there are at least arguable public policy reasons for recognizing reverse bad faith claims.

## Alternatives to "reverse bad faith"

At present, without a recognized claim for reverse bad faith, a plaintiff-insured has every reason to claim bad faith against its insurer in nearly any litigation. However, although a "reverse bad faith" cause of action has not yet gained acceptance, there are alternatives for an insurer defending against an unsupported bad faith claim. Two of these acceptable alternatives to "reverse bad faith" are: 1) fraud; and 2) statutory remedies.

*In sum, an insurer may have a few arrows in its quiver to use when forced to defend against a fraudulent claim and/or an insured's filing of a frivolous bad faith action.*

Courts may reject "reverse bad faith" as unnecessary because an insurer can bring a claim for fraud against its insured. The Supreme Court of Ohio, for example, denied a claim for "reverse bad faith" while stating that "[t]here are other avenues for the insurer to pursue in the event that an insured submits a fraudulent claim. An insurer drafts the policy, can refuse the insured's claim, and could assert a cause of action against the insured for fraud. In the context of insurance, claims of fraud by an insured is not limited to statutory or common law fraud. Most insurance policies expressly provide that fraud by an insured is an absolute defense to coverage. Thus, insurers can deny an insured's fraudulent claim by relying on a concealment or fraud provision in the policy.

Courts have gone even further in recognizing fraud as a defense to coverage. In Neidenbach v. Amica Mutual Insurance Company, 842 F.3d 560, 567 (6th Circuit 2016) (applying Missouri law), the Sixth Circuit went so far as to void the applicable insurance policy pursuant to the policy's "Concealment or Fraud" provision where the insured materially misrepresented the value of personal property lost in a fire. Approximately one year prior to the loss and claim, the insureds had filed a Chapter 13 bankruptcy petition stating they had only $7,000 worth of personal property. However, on the insureds' sworn statement of loss to the insurer, "they sought reimbursement of $262,500 worth of personal property — a difference of $250,500.[16]" Agreeing with the district court, the Sixth Circuit stated "that the misrepresentations on the Proof of Loss were material because an accurate inventory of the property destroyed by the fire was necessary for [the insurer] to make a coverage determination. Coupled with a finding that these material misrepresentations were intentional, the court voided the policy under the "Concealment or Fraud" provision.

In addition to defenses based on fraud, some states provide statutory remedies to insurers faced with frivolous bad faith claims. Tennessee, for one, has adopted a statute titled "Action brought in bad faith by policyholder," T.C.A. §56-7-106, which states:

In the event it is made to appear to the court or jury trying the cause that the action of the policy holder in bringing the suit was not in good faith, and recovery under the policy is not had, the policy holder shall be liable to the insurance company, corporation, firm, or person in a sum not exceeding twenty five percent (25%) of the amount of the loss claimed under the policy; provided, that the liability, within the limits prescribed, shall, in the discretion of the court or jury trying the cause, be measured by the additional expense, loss, or injury inflicted upon the defendant by reason of the suit.

The right to pursue an action under this statute "becomes vested in the insurer at the time of the institution of the insured's action, and thus the action becomes part of the controversy. Illinois, Massachusetts, New Jersey, and Nebraska also have statutes which provide that an insurer may, under certain circumstances, maintain a cause of action against an insured for bad faith in bringing a suit.

In sum, an insurer may have a few arrows in its quiver to use when forced to defend against a fraudulent claim, and/or an insured's filing of a frivolous bad faith action. Choosing which alternative to "reverse bad faith" to employ will rest on the facts of the case, the applicable policy language and the law of the applicable jurisdiction.

## Conclusion

The relatively few courts to have considered the question of common law "reverse bad faith" have ruled against recognizing this cause of action. However, as many jurisdictions have never considered the question, the viability of the doctrine remains uncertain. Public policy arguments in favor of recognition of "reverse bad faith" do exist. Indeed, the above-quoted Tennessee statute suggests that at least one state legislature finds the reasons for "reverse bad faith" compelling; perhaps, a court will too. But even if courts continue to reject the viability of a "reverse bad faith" claim, they may accept a claim of fraud against the insured, depending on the facts of the case and the relevant policy language. Accordingly, with or without widespread acceptance of a "reverse bad faith" claim, insurers are not completely defenseless against fraudulent claims or frivolous lawsuits.

***Paul C. Ferland, Foran Glennon Palandech Ponzi & Rudloff PC*, New York USA.**

# Data breaches top list of concerns for insurance industry

*In spring 2018, BLM published its Q1 2018 Broker Pulse report, which highlighted current broker concerns around both data and the increasing numbers of employment tribunals.*

Ahead of the imminent arrival of General Data Protection Regulation ('GDPR'), brokers across the UK have identified data breaches as the single largest threat to insurers and their clients. Findings from the 2018 Q1 Broker Pulse survey, published by insurance and risk law firm BLM, found that almost nine in 10 (88 per cent) of brokers saw data breaches as a key risk to their customers in 2018.

The quarterly poll, considered a barometer for insurance trends in the UK, also identified that increasing awareness of data security across the board was the biggest concern for businesses ahead of the GDPR deadline this month.

Helen Devery, BLM partner and head of the firm's broker sector, commented: "The proliferation of customer data has been a growing threat for some time now and it's fair to say the prospect of GDPR being in place will be sending concerns to businesses large and small.

"Having recently seen Under Armour and its MyFitnessPal app users subjected to the third largest data breach in history, these findings back the view that data security poses an unparalleled financial risk for businesses in the digital age. Indeed, whilst the investigation into Cambridge Analytica's use of Facebook data will encourage more prudent data sharing in future, this is a real time issue, and businesses are facing greater pressures than ever before to keep their customers' data safe."

Another issue expected to present itself in the next 12 months is an increase in employment tribunal claims following the Supreme Court's decision to remove fees associated with making a claim. Despite it being anticipated that the number of claims will more than double in 2018, the Q1 Broker Pulse found that only five per cent of businesses involved had reviewed their practices in light of the ruling.

Helen Devery added: "The removal of fees related to employment tribunals has certainly opened the door to the potential for more spurious and fraudulent claims being made. There currently appears to be very little political will to introduce any alternative fee system so the industry will be watching with a close eye to see how the numbers change as we approach the first year anniversary."

The Q1 Broker Pulse also found that the Far East remained a major problem for insurers pursuing the recovery of damages relating to defective products. A report commissioned by the International Trademark Association (INTA) and the International Chamber of Commerce, said the global economic value of counterfeiting and piracy could reach $2.3 trillion by 2022 – a figure backed in the UK, with 80 per cent of brokers telling BLM that defective products from the Far East were still an issue.

"The results of the Broker Pulse provide an important reflection of some of today's most pertinent issues across the world of insurance, from the growing significance of securing digital assets, to managing threats around fraudulent claims and ensuring that global supply chains are adequately protected. While GDPR preparation has lingered long on every business's priority list", Devery finished, "the consequences of non-compliance should be enough to ensure that no stone is left unturned in protecting against loss."