

The Key

Kennedys

Legal advice in black and white

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Total peace

Global settlements work better in recovery claims than in insurance ones.

Global settlements are a popular way of resolving complex construction disputes, as it saves the time and cost of litigating or having to agree individual values for individual claims. But can the paying party to a global settlement recover any of its outlay either from its insurers or from third parties whose failures triggered some of the claims? These issues were tackled in two recent cases, both of which stemmed from a global settlement of all disputes between Bovis and its employer regarding a large construction project.

Global settlements and insurance

Bovis had written advice from its lawyers that it was liable for certain matters, some of which were covered by its construction, engineering and design (CED) policy with Lumbermens. The written advice also ascribed amounts to the employer's claims.



This legal advice had been shared with Lumbermens, prior to the global settlement.

Following the settlement, Bovis tried to recover its apparently insured losses of approximately £19m under the CED policy. Lumbermens refused to indemnify Bovis and the case went to court (see Lumbermens

Mutual Casualty Co v Bovis Lend Lease [2004] EWHC 2197 Comm).

The CED policy provided that 'we the insurers hereby agree to indemnify the insured... for any sum which the insured may become legally liable to pay'.

Mr Justice Colman decided that Bovis' claim

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clearly failed. As the settlement agreement did not ‘ascertain’ the existence and extent of Bovis’ liability to its employer, there was no foundation for an indemnity claim. The key words in the policy were ‘legally liable to pay’: essentially, this meant that Bovis had to be held liable for an insured loss before it was protected by its insurance cover. Although a properly worded settlement agreement could render a company liable so as to meet this precondition, the global settlement agreement did not do this. It did not impose liability on Bovis for ‘any identifiable loss in respect of any identifiable insured eventuality’. Nor could Bovis legal advice be used to establish such liability, or its extent.

Arguably, Mr Justice Colman went too far when finding that the extent (rather than just the existence) of an insured’s liability has to be identified by a settlement agreement. However, Bovis’ appeal against his decision has been withdrawn.

For the present, therefore, a settlement agreement is not merely part of the process of determining a loss for the purposes of insurance. It is an essential ingredient in establishing whether cover is triggered at all. Unless it specifically ascertains the existence and extent of the insured’s loss – something that a global settlement agreement does not do – the indemnity under an insured’s policy will not be available, and nothing can be done later to rectify that position.

Global settlements and recovery

Contrast that with the role of global settlements in recoveries. Eighteen months before the *Lumbermens* decision, Bovis sought

to recover £6m of its global settlement outlay from two of its subcontractors (see *Bovis Lend Lease v R D Fire Protection Ltd* [2003] EWHC 939 TCC). In that case, Mr Justice Thornton held that global settlements could be the evidential foundation for a claim against those further down the contractual chain. A court would look at such a settlement and, by way of extrinsic evidence, identify that part of the global sum that was attributable to the defendants. It could do so even where the extrinsic evidence was limited. The figure determined by the court would then become the maximum which the claimant (in this case, Bovis) could recover, subject to proof that (1) the settlement was reasonable; (2) the subcontractor had in fact breached the subcontract; and (3) the subcontractor’s breach had, in turn, led to the breach of the main contract and the subsequent settlement.

Indeed, Mr Justice Thornton went further, ruling that the global settlement agreement could not be ignored. However, Bovis had to establish the financial detriment that it had incurred under the settlement agreement as a result of the subcontractors’ actions. Surprisingly, Bovis did not produce – and argued that it was impossible to adduce – evidence about how much of the global settlement sum was attributable to the subcontractors’ failings. It, therefore, failed to recover its £6m outlay from the subcontractors.

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Limitation period holds good

Even where insurers have entered into negotiations on a claim, they are entitled to rely on a contractual limitation period, unless they have made a clear representation that they will not do so.

A recent grant of summary judgment in the Commercial Court once more affirms that, unless insurers have made an unequivocal, unambiguous and unconditional promise to the contrary, they can raise the defence that an action is out of time.

In *Fortis Bank SA v Trenwick Insurance Co Ltd*, Mrs Justice Gloster said that the insurers were not estopped from relying on the existence of a limitation clause in the insurance contract, even though the parties had negotiated on the subject of quantum after that limitation period had expired.

Case facts

Fortis Bank had entered into a contract to purchase book debts and future debts from Zye Technology Limited. Following an alleged fraud under this agreement, the bank claimed £1m under its insurance policy with the defendant insurers.

The loss had been discovered in or around February 2000 and the insured did not bring proceedings until July 2003.

The defendants argued that the claim was made too late because general condition 13(b) of the insurance policy provided for a contractual limitation period of two years from the date of the discovery of the loss.

Negotiations

For two years following the discovery of the loss, the insurers and the insured were involved in discussions as to whether the loss was proved. Although no adequate proof of loss was provided, these negotiations included detailed discussions on the subject of quantum.

The bank argued that these discussions showed that the parties shared the assumption that Fortis had a valid claim which was not time-barred and that it was not necessary to start proceedings in order to keep this claim alive.

Proceedings

When the bank indicated, in June 2002, that it was planning proceedings under the policy, the insurers indicated that they would rely on the provisions of general condition 13(b) and that the insured was contract-barred from



bringing a claim. When the insured eventually brought proceedings, in July 2003, the insurers made an application for summary judgment on the basis of the limitation clause. The bank argued that the insurers were estopped from relying on general condition 13(b) because they had continued to negotiate as to the proof of the loss after the limitation period had expired.

Summary judgment

The application was heard on 29 October 2004 and 12 January 2005. Kennedys represented the insurers. Mrs Justice Gloster rejected the bank's arguments. She referred to Lord Justice Ward in *Seechurn v Ace* [2002] 2 *Lloyds Rep* 390, when he said that, in such circumstances, the claimant

must show that there is 'a clear, unequivocal, unambiguous and unconditional promise by the insurers that they would not raise the defence that the action was statute [or otherwise, time-] barred.'

Mrs Justice Gloster went on to say that 'the mere fact that an insurer has attempted to negotiate with the insured about a claim, both before and after the expiry of the limitation period, cannot per se amount to a waiver or an estoppel.'

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Cementing radical change

New design standards pose a major challenge for the UK construction industry.

Can you tell your BS 8110-1:1997 from your EN 1992: 2004? No? Well, very soon you will need to know the difference as the UK construction industry is about to undergo a sea change. British standards relating to the design of buildings and major components will be withdrawn by 2010 and replaced by harmonised European standards known as Eurocodes. The changes will include (among other things) new quality levels for the design of concrete and steel structures.

The new Eurocodes

The aim of the new Eurocodes is twofold: to establish a set of common design standards for the design of buildings and civil engineering works throughout the EU, and to increase the competitiveness of the European construction industry worldwide. They cover not only the design of the structure itself but also integral components such as concrete and steelwork.

The Eurocodes will be mandatory for all European works and are set to become the effective standard for the private sector in

Europe and, ultimately, worldwide. Consequently, they will have a major impact on the UK construction industry.

The new Eurocodes are different to our existing national standards. Construction professionals need to be aware of these new metrics now – and about how they will affect their work, their contractual requirements and their legal responsibilities. This is especially important in the case of construction projects that are likely to straddle the end of the transitional period for the withdrawal of British standards and the introduction of the new codes between 2008 and 2010.

Worldwide impact

The new harmonised European standards are being used to create market access for UK construction businesses in high-growth areas such as the Far East. The British Standards Institute has been holding seminars – in partnership with the Office of the Deputy Prime Minister and United Kingdom Trade and Investment – to promote the use of the Eurocodes in non-European markets, with a view to benefiting British manufacturers and suppliers of construction-related products, systems and services. Seminars have been

held in Hong Kong and other Far Eastern centres, and, as a result, Vietnam and Malaysia have said that they will base their national standards on the Eurocodes. Further opportunities in India and the Middle East are also being explored to try and give UK companies a head start on competitors in emerging markets.

The insurance market

In addition, insurers will want to be assured that designers and construction companies have understood how the new quality levels will affect their businesses, and have implemented

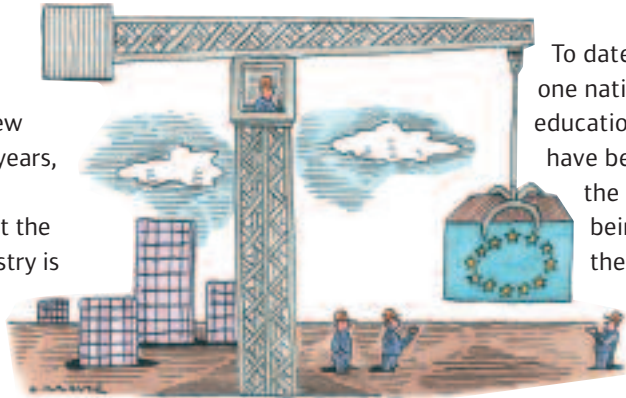
appropriate risk management procedures to prepare for the new regime. Over the years, UK case law has demonstrated that the construction industry is unlikely to be let off the hook because of a lack of knowledge or

practice; it has a responsibility to ensure that it is up to date and investigating the application of new methods or specification parameters, geotechnical, fire or seismic values.

Being aware of the latest trends and developments will also be vital when it comes to assessing future insurance premiums. If insurers conclude that they face greater exposure over companies using the new codes – or fear that risks may simply pass unnoticed by their insureds – then they will almost certainly increase premiums accordingly.

Key final issues

Designers will need to be familiar with all 58 of the new design standards, covering the 10 main areas that include structural safety and durability issues, fire resistance, geotechnical design and earthquake resistance. National annexes are currently being developed alongside the Eurocodes, allowing each member state to adapt the Eurocodes within certain parameters so as to fit regional requirements relating to issues such as wind levels or snow loads. They also deal with structural safety and durability issues, fire resistance, geotechnical design and earthquake resistance.



To date, 21 Eurocodes, one national annex and one educational publication have been completed for the UK, and others are being developed with the publication of the final document, anticipated in 2007.

Withdrawal of the national British standards is due to be completed in 2010.

To ensure compliance with all European quality metrics, businesses operating in the construction industry would also be well advised to investigate the direct relationship (as far as construction works are concerned) between the Eurocodes and the harmonised standards for construction products.

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Mental Capacity

The Mental Capacity Act 2005 (MCA) significantly alters the way in which healthcare decisions relating to patients without capacity can be made.

For the first time, there is a statutory definition of adult incapacity. Under the Act, an adult is unable to make a decision for themselves if they cannot:

- understand the information relevant to that decision;
- retain that information;
- use or weigh the information as part of the process of making the decision; or
- communicate their decision.

Best interests

Previously, where an individual could not give consent, then he or she could be treated under the common law doctrine of necessity, according to which treatment necessary to preserve life or prevent serious deterioration in the patient's condition could be given in accordance with the individual's best interests. However, it was never entirely clear what constituted 'best interests'.

Under the new Act, several questions have to be resolved in arriving at a decision about what is in a person's best interests:

- Will the individual in future have capacity regarding the matter in question?
- If yes, when is that likely to be?

- What are the individual's past and present wishes and feelings?
- What directions are contained in any advance decision (see further below)?
- What beliefs and values might influence the individual's decision, if they had capacity to consent to treatment?
- Are there any other factors that the individual would consider if they were able to do so?

For the first time, the Act now requires consultation, if practicable, with the following:

- anyone named by the person lacking capacity as someone who should be consulted on the issue(s) in question;
- anyone caring for – or who is interested in the welfare of – the person without capacity;
- any donee of a lasting power of attorney (see below) granted by the person lacking capacity; and
- any deputy appointed under the Mental Capacity Act.

The MCA now provides two routes to obtaining consent to treatment in cases where the adult does not have capacity:

- (1) via a lasting power of attorney; or
- (2) via a court-appointed deputy.

Lasting powers of attorney

The Mental Capacity Act has repealed the Enduring Power of Attorney Act 1985 and introduced the concept of a lasting power of attorney. The two powers are similar, but the range of a lasting power of attorney is greater than that of an enduring power. Lasting powers, like enduring powers, need registration with the Court of Protection before they are valid.

The lasting power of attorney allows the donee (the person to whom the power has been granted) to make decisions relating to the healthcare treatment of the donor (the individual granting the lasting power) if the donor lacks capacity. This is new. However, if the donor wants the donee to make life-or-death decisions in the event that the donor becomes incapable of making such decisions for himself or herself, this must be specified in the lasting power.

Advance decisions

The Act also formalises the position in relation to what are now known as 'advance decisions' (previously 'advance directives'). Advance decisions can only be made by individuals with capacity who are 18 or over. They must be in writing, signed by the individual making the advance decision and witnessed by at least one other person.

An advanced decision is defined in the MCA as:

'a decision that if

(a) at a later time and in such circumstances as [the individual] specifies, a specified treatment is proposed to be carried out or continued by a person providing healthcare for [that individual], and

(b) at that time, [the individual] lacks capacity to consent to the carrying out or continuation of that treatment,

the specified treatment is not to be carried out or continued'.

However, the advance decision will not apply in certain circumstances. For example, it will not apply to life-sustaining treatment unless the advance decision is backed up by a statement from the individual that, even if life is at risk, the decision does indeed exclude the particular treatment being considered.

Anyone treating the donor who is ignorant of an advance decision will not incur any liability. Nor will they be liable if they withhold or withdraw treatment in the reasonable belief that an advance decision exists which is valid and applies to the treatment in question.

Greater freedom of choice

We have yet to see how the Mental Capacity Act will work in practice, but the statutory definition of incapacity is to be welcomed. For some time, the law regarding individuals without capacity has been complicated, and responsibility for treatment has traditionally rested with the doctors. The Act now gives patients a sound legal basis for appointing another individual to make medical care decisions in the event that they become incapable of consenting to such treatment themselves.

This Act has not yet come into power.

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Paying in: still the way

Should local authorities follow the example of the NHS trust in *Crouch* and make a written offer instead of paying into court?

The Court of Appeal's judgment in *Peter Crouch v King's Healthcare NHS Trust* is a major triumph for NHS trusts and the NHS Litigation Authority. The Court of Appeal accepted that, when the court exercises its discretion on costs, it should treat an offer by an NHS trust in the same way as a part 36 payment, unless there is some special factor about the circumstances of the case.

Background

In *Crouch*, the NHS trust admitted liability and the claim proceeded to trial, where the claimant was awarded damages of £30,208. Before trial, the trust had made a written offer to settle the claim for £35,000. This had been rejected.

An assessment-of-damages hearing took place on 2 and 3 September 2003 before His Honour Judge Latham. Because the judgment sum had not beaten the trust's offer, the trust applied for an order that the claimant should pay its costs from the date when the offer to settle expired.

The judge held that the trust had not successfully protected its position on costs because it had not paid money into court and expressed concern that defendants making written offers might not remain solvent until they had met their obligations. He ordered

the trust to pay all the claimant's costs, ignoring the written offer.

The appeal

The NHS trust appealed, saying that the judge should have made an order for costs in its favour, as if there had been a payment into court. The trust relied on part 36.1(2) of the Civil Procedure Rules (CPR), which gives the court the discretion to order that an offer to settle should lead to the same consequences as those in CPR part 36.20; it argued that the judge could and should have exercised this discretion.

Lord Justice Waller directed that, when a court exercises its discretion under part 36, it should have regard to all the circumstances of the case and ask whether it was right to apply the presumption in CPR 36.20. He thought that an NHS trust was bound to be 'good for the money' and that the offer was as good as a payment into court.

Implications of *Crouch*

Should a defendant local authority now choose to make a written offer rather than the usual payment in? This is an attractive idea for any public body; by making offers instead of paying money into court, a local authority can use the freed-up money to pay for services that may otherwise remain underfunded.

But our advice is that local authorities should avoid this approach. The NHS argued that the money paid into court could be tied up for many years; but it is rare for even complex personal injury cases to take more than three years from the issue of proceedings to a final trial – most of the work tends to be carried out under the personal injury pre-action protocol – and there is even less delay in non-clinical injury cases, meaning that money is released more quickly.

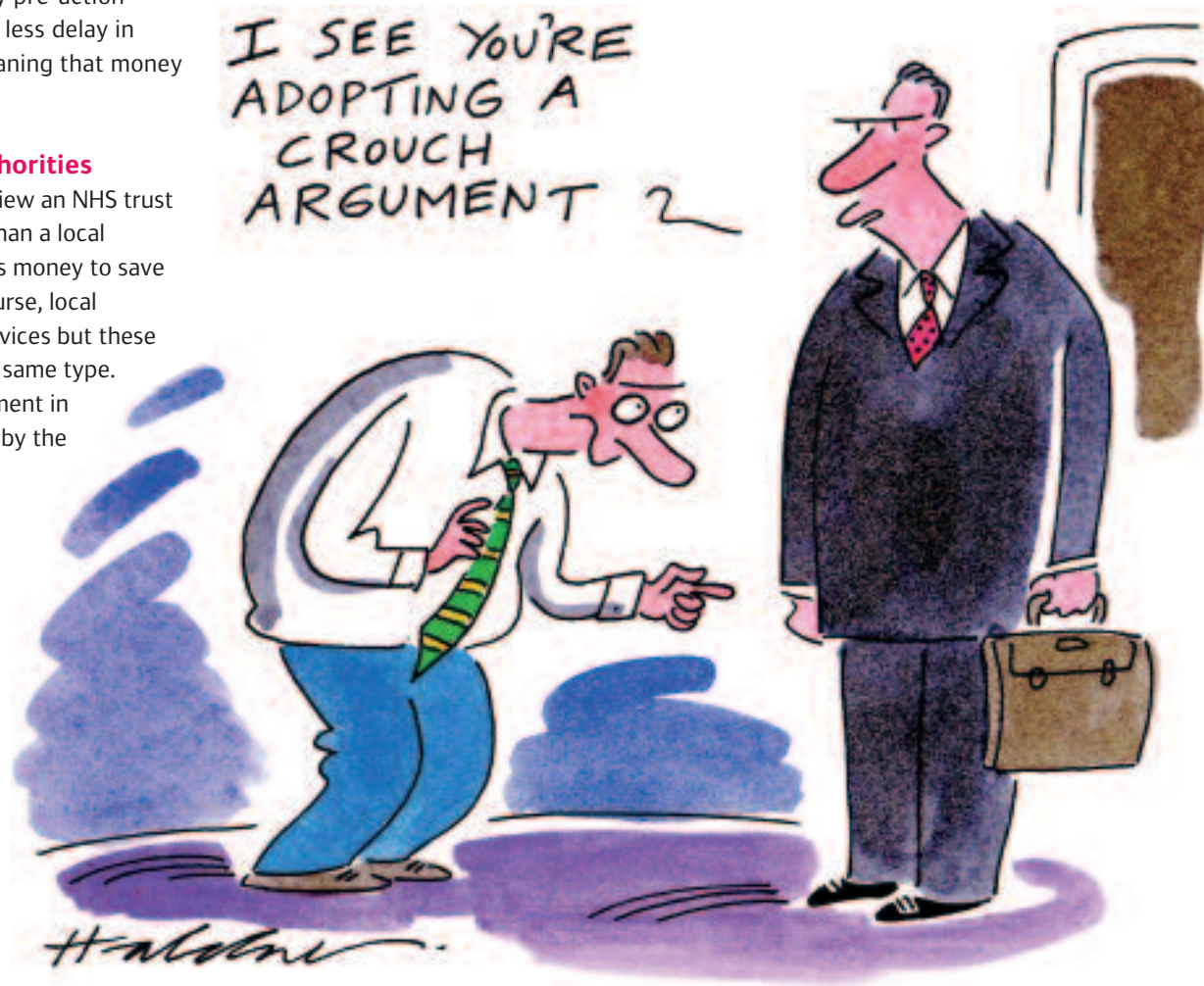
NHS trusts and local authorities

The courts are also likely to view an NHS trust in a more sympathetic light than a local authority. An NHS trust needs money to save lives and cure the sick. Of course, local authorities provide public services but these may not be seen to be of the same type. The decision to run the argument in Crouch was driven genuinely by the NHS and therefore carried considerable conviction – something which an insurer or claims handler, with many fewer witness statements in support, would find it difficult to match.

Whereas the NHS is self-funding, for major cases, local authorities tend to be insured. In those cases when a local authority is self-funding, the sums will generally be smaller. The smaller the sum, the harder it will be to win a Crouch argument.

Some local authorities surcharge the 'offending' department so that, where a

highways inspector is found to have been in breach of duty, a highways department may have to meet part or all of the uninsured judgment sum. If the money in question is seen to come from a particular department, this may or may not help. Most claims against local authorities relate to highways incidents



and an argument that the authority should not have to pay money into court because of the impact on street maintenance will not

carry the same weight as the one deployed by the NHS. This type of argument might be more attractive if a local authority care team was involved.

Finally, what pressure will a claimant be under? The effect of a well-assessed sum of

lawyers and judges felt that payments in should be retained. Part 36 payments into court are a very persuasive device in the defendant's toolbox. Will a simple offer to pay carry the same weight?

Advice to local authorities

It is unlikely that a local authority would be able to win a Crouch argument and there is the risk that additional costs would be generated in trying to justify the decision not to pay in. If a court found that the money should have been paid in, then a local authority would be faced with a substantial liability for costs that could have been avoided.

In local authority liability cases, the potential risks of adopting a Crouch argument more than outweigh the benefits of doing so. A decision against a local authority would have costs consequences and a potential effect on claims experience which would be less than beneficial.

money being paid into court should not be underestimated. A recent Law Commission consultation exercise found that a majority of

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EU Reinsurance Directive

Reinsurers have an excellent opportunity to expand their business across the EU.

On 7 June, the European Parliament decided to approve the Reinsurance Directive. The directive now awaits formal adoption by the EU Council. This is anticipated in the next few months. Member states will then have to implement the directive within two years of the date of its formal adoption.

Background

Currently, there is no harmonised framework for the supervision of reinsurance business in the EU. The Reinsurance Directive will create a single regulated market for pure reinsurance business, similar to the one that already exists for direct insurance. This will remove the present anomaly whereby reinsurance activities carried out by direct insurers are subject to regulation, whereas the activities of pure reinsurers are not.

The directive will apply to reinsurers who only conduct reinsurance activities and who are established, or wish to be established, in the EU. For this purpose, 'reinsurance' is defined as 'the activity consisting in accepting risks ceded by an insurance undertaking, by another reinsurance undertaking, or by an institution for occupation or retirement provision falling under the scope of Directive 2003/41/EC'. The recitals to the directive say that this definition will also cover captive reinsurers.

As noted above, the directive will not apply to direct insurers who also carry on reinsurance activities, as they are already subject to the non-life and life directives. Nor will it apply to governments providing reinsurance as a last resort.

Key provisions

(1) *Single passport for reinsurers*

A reinsurer who is authorised in one EU territory will be able to write cross-border business anywhere else in the EU, either by establishing itself in other member states or

by providing services directly from its home state. Either way, prudential supervision will be provided by the reinsurer's home state regulator (which, in the case of the UK, will be the Financial Services Authority).

(2) *Initial authorisation*

Authorisation will be required in the member state where the reinsurer's head office is located. However, reinsurers who are already authorised to conduct reinsurance business in a member state will be exempt from this requirement. The principal requirements for any reinsurance firm seeking authorisation will include the following:

- The objects of the firm must be limited 'to the business of reinsurance and related operations'. This will not prevent a firm from carrying out associated activities, such as actuarial advice and risk analysis, or owning direct insurers as subsidiaries.
- A 'scheme of operation' will have to be submitted. This must evidence the nature of the risks to be covered, the types of reinsurance arrangements that will be used, guidelines about the principles applicable to retrocession, estimates of the cost of establishing administrative services, and the financial resources available to meet such costs.



(3) Solvency margins

The solvency margin requirements applicable to life and non-life insurance business respectively are currently set out in the so-called 'Solvency I' Directives, which were adopted in February 2002. An EU project known as 'Solvency II' is currently underway, with the stated objective of improving protection for insureds by updating the solvency requirements applicable to insurers.

The reinsurance directive is a 'fastrack' interim solution for reinsurers, pending finalisation of Solvency II. Broadly speaking, under the directive, the solvency margins currently applied to direct non-life insurance are likely to apply to both life and non-life reinsurance. Retrocession by a reinsurer to another reinsurer may be taken into account in solvency calculations, but only up to a maximum of 50% of the gross amount of claims. There is continuing debate (and

concern by those in the life reinsurance market) about whether it is correct to apply the same approach to both life and non-life reinsurance solvency margins.

(4) Collateralisation

From a political perspective, this has been one of the more controversial aspects of the directive. A perceived benefit of the new legislation is the promotion of competition among EU states by (among other things) prohibiting any member state from demanding the posting of collateral as a condition of conducting business in the territory. Despite strong lobbying that collateral requirements should cease immediately, the European Parliament has endorsed the compromise transitional arrangement set out in the directive. This gives member states a further 12 months (from the date of implementation of the directive into their own national law) to

abolish collateral requirements. Countries affected are Germany, France and Portugal, as they currently demand collateral. In theory, therefore, all EU collateral requirements should be abandoned (at the latest) by the end of three years from the date when the directive is formally adopted.

The abolition of collateral is also seen as an essential element in support of the EU's negotiations with the US, which aim to make it easier for European reinsurers to enter the US market (where collateral requirements are still prevalent). Any delay in the abolition of collateral requirements in the EU, therefore, can only delay the progress of the negotiations with the US.

Conclusions

The impending Reinsurance Directive provides an opportunity for reinsurers to expand their reinsurance business

throughout the EU. The UK already has an established supervisory and regulatory regime for reinsurers. It is therefore ideally placed to act as host regulator (through the FSA) for reinsurers wishing to establish themselves in the UK and then exploit their passporting rights through the conduct of reinsurance business in other EU territories.

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For further information about any of the articles within this issue please contact the author concerned or your usual partner.

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