Legal Studies, Vol. 35 No. 2, 2015, pp. 280–301
DOI: 10.1111/lest.12059

Insurable interest – the doctrine that would not die

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The doctrine of insurable interest grew out of eighteenth-century anxieties over fraudulent seafarers and habitual gamblers. It was created by the courts, entrenched by statute and remains in place to this day despite the fact that it serves no practical or legal purpose. It was hoped by many that, when the English Law Commission and Scottish Law Commission established their joint review of insurance contract law in 2006, the doctrine would be consigned to the proverbial dustbin of history. Eight years later, these hopes have been dashed. The doctrine is here to stay. This paper asks 'Why' and finds the answer to be elusive.

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INTRODUCTION

It is 11 years since the Court of Appeal's judgment in *Feasey v Sun Life Assurance Co of Canada*,[1] arguably the last major English judicial pronouncement on the doctrine of insurable interest. Nine years have passed since the Gambling Act 2005, which muddied the already opaque waters on the doctrine. The English and Scottish Law Commissions' joint 'Issues Paper 4', which asked 'whether the law on insurable interest should be repealed', was published 6 years ago. Finally, it is over a year since the Commissions' paper 'Insurance Contract Law: Post Contract Duties and Other Issues' (the 'Second Joint Consultation Paper'), which returned to the doctrine, noted the UK insurance industry's opposition to repeal and raised more questions about its future.[2]

Yet, despite so much activity, the law on insurable interest remains a mélange of (largely) archaic statutes and contemporary judgments, with the courts' intent in the latter often being to overcome the deficiencies of the former. Sadly, if the Second Joint Consultation Paper is to be believed, the mélange is here to stay. Why should this be? What interests are served by maintaining the doctrine? What is stopping us from putting the doctrine out of its, and our, misery?

This paper looks, first, at the form and function of the doctrine of insurable interest. It then considers the submissions of those who opposed the doctrine's repeal. Unlike the calls for the doctrine's end, those for its retention are rarely considered in detail. The paper concludes by considering what the future may hold for the doctrine in the

* The author wishes to thank Robert Merkin and John Lowry for their helpful comments on earlier drafts of this paper. The usual disclaimer applies.

1. [2003] 2 All ER (Comm) 587.

2. The Commissions' Second Joint Consultation Paper and Issues Paper 4 may both be found at http://lawcommission.justice.gov.uk/areas/insurance-contract-law.htm (accessed 29 November 2013).

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UK and considers to what extent its reform or repeal would reduce disputes between insurers and policyholders over losses and claims.[3]

INSURABLE INTEREST – FORM, FUNCTION AND FLAWS

The following passages comprise only a brief review of the doctrine. This has been discussed at length on many occasions elsewhere, not least in the Commissions' own literature. The intention here is merely to explain the broad outlines of the subject to those readers who may not be familiar with the operation of insurance contract law.[4]

The doctrine

The basic principle of the doctrine is fairly simple – for a contract of insurance to be valid, the insured must have an 'insurable interest'. This means, in theory, that the insured will benefit from the preservation of the subject matter of the policy or suffer a disadvantage if it is lost. What it means in practice is not, however, so simple. Indeed, an insurable interest may exist in the absence of any 'disadvantage' or 'loss' for non-indemnity policies. There is also a question of 'when' the insurable interest needs to exist – at inception, at the time of loss or both?

Further, it is necessary to appreciate the differences between indemnity insurance and non-indemnity (or contingency) insurance and between marine and non-marine insurance. As to the first distinction, the classic exposition of the 'indemnity principle' was given by Brett LJ in *Castellain v Preston* as 'Every contract of marine or fire insurance is a contract of indemnity, and indemnity only, the meaning of which is that the assured in case of a loss is to receive a full indemnity, but is never to receive more.'[5] Thus, indemnity insurance compensates the policyholder for any loss that he may suffer (provided that it is covered by the policy), whereas non-indemnity policies pay him a specific sum of money upon the occurrence of a particular event, irrespective of whether any 'loss' has been suffered. Examples of indemnity cover include marine insurance, fire insurance and professional liability insurance, while non-indemnity cover includes most life policies, personal accident policies and valued policies.[6]

3. It should be noted that while the Commissions' Issues Paper 4 and Second Joint Consultation Paper looked at both England & Wales and Scotland, this paper focuses on the law in the former.

4. Those interested in a detailed discussion of the history and intricacies of the doctrine should look to, for example, J Birds, B Milnes and S Lynch (eds) *MacGillivray on Insurance Law* (London: Sweet & Maxwell, 12th edn, 2012) or R Merkin *Colinvaux's Law of Insurance* (London: Sweet & Maxwell, 9th edn, 2010). Alternatively, there are more concise treatments of the subject in J Birds *Birds Modern Insurance Law* (London: Sweet & Maxwell, 9th edn, 2013) and J Lowry, P Rawlings and R Merkin *Insurance Law Doctrines and Principles* (Oxford: Hart Publishing, 2011, 3rd edn, 2011).

5. [1881–1885] All ER Rep 493.

6. Parties may agree in the insurance policy on the value of the thing insured and this valuation is conclusive (unless there is fraud). The insured may recover this agreed value in the event of a total loss or a proportion of the agreed value for a partial loss. See Marine Insurance Act 1906, s 27.

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As to the second distinction, while the Marine Insurance Act 1906 (the MIA 1906)[7] codified the law governing the former, the latter remains a creature of the courts. Having said that, many of the principles developed in relation to marine policies, such as the doctrine of utmost good faith, also apply to non-marine policies.[8] There remain, however, many differences between marine and non-marine insurance law, the application of the doctrine of insurable interest being one of them.

The legislation

The legislative part of the 'mélange' comprises a number of statutes reaching back to the days of the Hanoverian monarchs. The five most important pieces of legislation begin with the Marine Insurance Act 1745 (the 1745 Act), which was the first UK statute to create a requirement for insurable interest in insurance contracts.[9] Its aim was to prevent what were described in its preamble as 'many pernicious practices, whereby great numbers of ships, with their cargoes, have been fraudulently lost or destroyed' as a consequence of policies being taken out by those who had no such insurable interest in the subject matter of such policies.

It seems that the 'pernicious practices' decried in the 1745 Act were not limited to maritime enterprises. The habit of taking out of policies on the lives of public figures[10] led to the Life Assurance Act 1774 (the 1774 Act).[11] The 1774 Act aims to prohibit 'a mischievous kind of gaming', to prevent insurance on lives being taken out without a valid insurable interest and declares null and void any policies without such an interest.[12]

Ongoing anxieties about the dangers of gambling also led to the passage of the Gaming Act 1845 (the 1845 Act), s 18 of which provides as follows:

> All contracts or agreements, whether by parole or in writing, by way of gaming or wagering, shall be null and void; and no suit shall be brought or maintained in any court of law or equity for recovering any sum of money or valuable thing alleged to be won upon any wager, or which shall have been deposited in the hands of any person to abide the event on which any wager shall have been made . . .

It is arguable that the 1845 Act is the only statutory basis – albeit an indirect one – for the application of the doctrine to non-marine indemnity policies. The situation is, however, problematical and is considered further below.

The MIA 1906 repealed the 1745 Act and, as noted above, codified the law on marine insurance. Section 4 of the 1906 Act states that:

7. The Marine Insurance Act 1906 is available at http://www.legislation.gov.uk/ukpga/Edw7/6/41/contents (accessed 29 November 2013).

8. The doctrine of utmost good faith, which has also created no little controversy, was reformed in respect of consumer insurance by the Consumer Insurance (Disclosure and Representations) Act 2012. The text of the legislation is available at http://www.legislation.gov.uk/ukpga/2012/6/contents/enacted (accessed 29 November 2013).

9. There are some very early authorities on the need for an insurable interest, such as *Goddard v Garrett* (1692) 2 Vern 269 and *The Sadler's Company v Badcock* (1743) 2 Atk 554.

10. Issues Paper 4, para 2.5.

11. The Life Assurance Act 1774 is available at http://www.legislation.gov.uk/apgb/Geo3/14/48/contents (accessed 29 November 2013).

12. Life Assurance Act 1774, s 1.

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(1) Every contract of marine insurance by way of gaming or wagering is void.
(2) A contract of marine insurance is deemed to be a gaming or wagering contract –
    (a) where the assured has not an insurable interest as defined by this Act, and the contract is entered into with no expectation of acquiring such an interest . . .

Finally, there is the Gambling Act 2005 (the 2005 Act),[13] which was introduced to update the regulation of the gambling industry. Section 335 of the 2005 Act states 'the fact that a contract relates to gambling shall not prevent its enforcement', so as to enable consumers to bring proceedings against bookmakers and others if they refuse to pay on a valid wager. An unintended consequence of this measure may have been to remove the indirect imposition of a need for an insurable interest in indemnity policies pursuant to the (defunct) 1845 Act.[14]

What is an insurable interest?

The nature of an insurable interest is dependent upon the policy. By s 3 of the Life Assurance Act 1774 (the 1774 Act):

> And in all cases where the insured hath interest in such life or lives, event or events, no greater sum shall be recovered or received from the insurer or insurers than the amount of value of the interest of the insured in such life or lives, or other event or events.

The reference to 'event or events' gave rise to one of the many difficulties associated with the doctrine – does the 1774 Act apply beyond life policies? In *Mark Rowlands Ltd v Berni Inns Ltd*,[15] the Court of Appeal held that it did not, with Kerr LJ remarking 'this ancient statute was not intended to apply, and does not apply, to indemnity insurance'.[16] The ambiguity of the 1774 Act's language remains, however, despite the courts' intervention.

The 1774 Act does not specify the nature of the insurable interest in life policies, although s 3 suggests that it must be a financial interest. An insurable interest is, however, presumed to exist where it arises out of 'natural affection'. Consequently, there is one for policies on an insured's own life and where the policyholder takes out cover on the life of his or her spouse.[17] This presumption does not extend to other family relationships – a parent, for example, has no interest in the life of his child.[18] In other cases, the policyholder must demonstrate an interest in the life insured that is of a financial nature. For example, an employer may have an insurable interest in the life of an employee and vice versa.[19]

13. The Gambling Act 2005 is available at http://www.legislation.gov.uk/ukpga/2005/19/contents (accessed 29 November 2013).
14. This possibility was raised in J Davey 'The reform of gambling and the future of insurance law' (2004) 24(4) Legal Stud 507–515.
15. [1986] QB 211.
16. The Privy Council reached the same view in *Siu Yin Kwan v Eastern Insurance Co Ltd* [1994] 2 AC 199.
17. See *Wainewright v Bland* (1835) 1 M&W 32 and *Reed v Royal Exchange Assurance Co* (1795) Peake Ad Cas 70, respectively. Section 253 of the Civil Partnership Act 2004 extends the latter provision to civil partners.
18. See *Halford v Kymer* (1830) 10 B and C 724.
19. See *Hebdon v West* (1863) 3 B and S 579. Also, see *Fuji Finance v Aetna Life Insurance Co* [1997] ch 173 on 'key employee' cover.

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The 1745 Act did not provide any definition of an insurable interest in marine policies. This was, instead, elaborated upon in *Lucena v Craufurd*,[20] in which Lord Eldon held that an insurable interest was

> a right in the property, or a right derivable out of some contract about the property, which in either case may be lost upon some contingency affecting the possession or enjoyment of the property

This formulation, which has been criticised for being too narrow in its scope, found its way into the MIA 1906, s 5 of which provides that:

(1) Subject to the provisions of this Act, every person has an insurable interest who is interested in a marine adventure.
(2) In particular a person is interested in a marine adventure where he stands in any legal or equitable relation to the adventure or to any insurable property at risk therein, in consequence of which he may benefit by the safety or due arrival of insurable property, or may be prejudiced by its loss, or by damage thereto, or by the detention thereof, or may incur liability in respect thereof.

This is the only English statutory definition, to date, of insurable interest.

Lord Eldon's formulation has also been applied to non-marine indemnity policies,[21] although it has not been without challenges. In *Sharp v Sphere Drake Insurance, The Moonacre*,[22] the court held that an insurable interest in property might arise from the policyholder's duty to exercise reasonable care in respect of property in which he had no legal or equity interest. In *National Oilwell (UK) Ltd v Davy Offshore Ltd*,[23] Colman J extended this principle. He held that a subcontractor involved in a construction project had an insurable interest by virtue of his 'proximate physical relationship to the property in question' in the entire contract works, even though his duties were limited to supplying goods for only a part of those works. The rationale was that if the entire works were destroyed, his own contract would cease.[24]

In *Feasey*, which concerned life policies, Waller LJ laid down a three-step test for determining the existence of an insurable interest:

(i) What on the true construction of the policy was the subject matter of the insurance?
(ii) Was there an insurable interest that was embraced within that subject matter?
(iii) Was the insurable interest capable of valuation in money terms at the date of the contract?

Applying these tests, Waller and Dyson LJJ held in *Feasey* that a P&I Club had an insurable interest in its own liability to indemnify its members for the death and personal injury of their employees, and that its reinsurance covered this interest even

20. (1806) 2 Bos & PNR 269.

21. In *Macaura v Northern Assurance Co Ltd* [1925] AC 619, the policyholder was an unsecured creditor and the only shareholder in a company that owned a large amount of timber. The timber was destroyed by a fire but his claim on the policies that covered it failed because, in Lord Sumner's view, 'His relation was to the company, not to its goods . . .'

22. [1992] 2 Lloyd's Rep 501.

23. [1993] 2 Lloyd's Rep 582.

24. This approach echoes that of Lawrence J in *Lucena*, who disagreed with Lord Eldon's formulation and observed that 'A man is interested in a thing to whom advantage may arise or prejudice happen from the circumstances which may attend it.'

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though the reinsurance was framed as a life – and not a liability – policy. [25] Ward LJ did not agree with this approach and others have criticised both Waller LJ's tests and his general comments on insurable interest.[26] Further, although *The Moonacre* and *National Oilwell* were endorsed, albeit cautiously, in *Glengate-KG Properties Ltd v Norwich Union Fire Insurance Society Ltd*,[27] the scope of the new approach was limited in *Deepak Fertilisers v ICI Chemicals*.[28]

Finally, while the Commissions believed that the 2005 Act removed the requirement for an insurable interest in non-marine indemnity policies, it was noted in the Second Joint Consultation Paper that several respondents did not agree.[29] The Commissions, as a consequence, intend to clarify the position.[30] Yet, even if the doctrine has (or may have) been abolished for non-marine indemnity policies, a policyholder will still have to demonstrate an 'interest' in the subject matter of the policy at the date of the loss by virtue of the indemnity principle, as per *Castellain v Preston*.[31]

When is the interest needed?

The 1774 Act offers no indication of when the insurable interest in a life policy is needed – at inception or at the time of loss – although ss 1 and 3 suggest that it must exist at both.[32] In *Dalby v The India and London Life Assurance Co*,[33] it was held, however, that the interest only had to exist at inception. By contrast, s 6(1) of MIA 1906 states: 'The assured must be interested in the subject-matter insured at the time of the loss though he need not be interested when the insurance is effected.'[34] The position is relation to non-marine indemnity policies is dependent on the status of the 1845 Act. The overall position can, possibly, be best be demonstrated as in Table 1.

These distinctions are confusing enough, but there is the further difficulty that they are often unclear when applied to actual insurance policies. For example, Geoffrey

25. A P&I club is a mutual insurance association that provides cover for its members, who are usually ship-owners, ship-operators or demise charterers. Unlike an insurance company that provides marine cover, whose directors will be answerable to its shareholders, a P&I club is only responsible to its members.

26. See J Birds 'Insurable interest – orthodox and unorthodox approaches' (2006) J Bus L 224–231 for a further discussion of Waller LJ's approach in *Feasey*.

27. [1996] 2 All ER 487.

28. [1999] 1 Lloyd's Rep 387.

29. The Lloyd's Market Association and Mark Templeman QC argued that the 2005 Act was not, nor was it intended to be, directed at insurance. Nicholas Legh–Jones QC questioned whether the 1845 Act had actually 'created an obligation for insurable interest in the form developed by the courts'.

30. For a further discussion of the implications of the 2005 Act, see C Nicoll 'Insurable interest: as intended' (2008) 5 J Bus L 432–447.

31. In the absence of any actual loss on the part of the insured, he will not recover any money from the insurers in respect of any detriment to the subject matter of the policy. For a discussion of this issue, see N Campbell 'The nature of an insurer's obligation' (2000) 42 Lloyd's Mar & Com L Q 42.

32. See *Goldsall v Boldero* (1807) 9 East 72.

33. (1854) 15 CB 365.

34. There is a question as to whether it needs to be 'expected' as per section 4. There is also an exception 'where the subject-matter is insured "lost or not lost" '. In this case, 'the assured may recover although he may not have acquired his interest until after the loss, unless at the time of effecting the contract of insurance the assured was aware of the loss, and the insurer was not'.

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Table 1: The need for and timing of insurable interest

Policy type	Inception	Loss
Life	Insurable interest required (by 1774 Act)	Not required
Marine	Not required (although may need to be 'expected' by s 4 of the 1906 Act)	Insurable interest required (by the 1906 Act)
Non-marine indemnity	Not clear – may be required if the 2005 Act does not apply to insurance	Not clear but need for 'loss' (under common law indemnity principle)

Lloyd and Derrick Cole commented in their response to Issues Paper 4 that 'A life assurance policy is clearly a non-indemnity policy but it can be argued that key-man insurance whereby an employer effects life insurance on the life of a valuable employee is indemnity insurance.'[35] Further, in *Swiss Reinsurance Co v United India Insurance Co Ltd*,[36] Morison J stated that the fact that elements of the risk covered by a composite policy had been rated separately (given that they differed in their nature) did not mean that the premium (or the policy) was severable. Thus, despite the apparent clarity of Table 1, the true position is much more opaque.

The flaws

The difficulties with the doctrine will have become apparent from the foregoing description. Indeed, the Commissions went so far as to refer to Robert Merkin's description of the law as 'a confusing and illogical mess'.[37] In summary, the Second Joint Consultation Paper identified 'three main reasons' for the current state of affairs and the need for reform:

(i) The law is a bewildering mixture of common law and statute.
(ii) The definition of insurable interest is uncertain.[38]
(iii) The doctrine differs depending on the type of insurance.[39]

Issues Paper 4 also identified a number of practical problems, including the fact that dependants other than spouses cannot obtain an insurable interest in their supporter's life (unless they can demonstrate some legal obligation on the latter's part to

35. Second Joint Consultation Paper, para 10.8.
36. [2005] 2 All ER (Comm) 367.
37. Second Joint Consultation Paper, para 1.25. The original comment was in R Merkin *Reforming Insurance Law: Is There a Case for Reverse Transportation?* Report for the English and Scottish Law Commissions on the Australian experience of insurance law reform (2007).
38. In J Lowry and P Rawlings' 'Rethinking insurable interest', in S Worthington (ed) *Commercial Law and Commercial Practice* (Oxford: Hart Publishing, 2003), the authors suggested that the policy considerations that underpinned Lord Eldon's formulation of the doctrine were 'no longer relevant'. The doctrine, it was suggested, 'harks back to a time when policy issues dictated that [insurable interest] should be a precondition to the validity of the insurance contract'. Those policy considerations were redundant and the indemnity principle was a sufficient safeguard against potential mischief.
39. Second Joint Consultation Paper, para 10.2.

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maintain them).[40] Further, Issues Paper 4 pointed out that the only party to suffer was the policyholder, given that the consequence for the absence of an insurable interest would be for the contract to be held void.[41]

THE DOCTRINE – THE CASE FOR ITS RETENTION

Despite its deficiencies, the doctrine is going to survive. It therefore makes sense to examine the reasons for this in some depth. Several of the responses to Issues Paper 4 are referred to in the Second Joint Consultation Paper and, while no details are publicly available, there were four reasons (also referred to as 'useful functions') given for the retention of the doctrine.[42] These were as follows:

(i) It provides a dividing line between gambling and insurance.
(ii) It guards against moral hazard.
(iii) It protects the insurer from invalid claims.
(iv) It is used to define where insurance is located.

A further three 'main reasons', in relation to indemnity policies, were referred to in the Second Joint Consultation Paper:

(a) It was the hallmark of insurance.
(b) It reinforced market discipline.
(c) It acted as a barrier against invalid claims.[43]

It was further suggested that 'The concept of insurable interest may also be useful in other circumstances, such as specifying the location of insurance.' On reflection, reasons (i) and (a) appear to be the same; reasons (ii) and (iii) and (b) cover the same issues; reasons (iii) and (c) are the same; and (iv) and the further suggestion are also the same. With that in mind, this paper focuses on reasons (i) to (iv) above.

Reason 1 – gambling v insurance

This was summarised as follows:

> It provides a dividing line between gambling and insurance. This distinction is crucial for both regulatory and tax purposes, and for those communities where gambling is forbidden. Insurable interest thus is an important part of the definition of insurance.

The need for a 'dividing line' between insurance and gambling seems to have three aspects – regulatory, tax and social. There is also the conclusion that insurable interest is integral to the 'definition of insurance'.

It is not feasible to discuss the minutiae of UK insurance regulation in a paper of this length. Several points can, however, be made to refute the assertion that the retention of the doctrine is 'crucial' to the regulatory treatment of insurance. First, the statutory basis for the regulation of insurance business in the UK is the Financial

40. See *Harse v Pearl Life Assurance Co* [1904] 1 KB 558.
41. Issues Paper 4, Pts 4 and 6.
42. Second Joint Consultation Paper, paras 10.11–10.12.
43. Second Joint Consultation Paper, para 12.5.

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Services and Markets Act 2000 (FSMA),[44] which established the Financial Services Authority (FSA).[45] The 2008 financial crisis led to much criticism of the FSA and it was replaced by the Prudential Regulatory Authority (PRA)[46] and the Financial Conduct Authority (FCA)[47] in 2013.

The focus of the legislation and the regulatory bodies is on 'regulated activities', the definition of which in para 2 of Sch 2 of FSMA includes:

> Dealing in investments
>
> 2(1) Buying, selling, subscribing for or underwriting investments or offering or agreeing to do so, either as a principal or as an agent.
>
> (2) In the case of an investment which is a contract of insurance, that includes carrying out the contract.

Such 'investments' also include 'Rights under a contract of insurance' pursuant to para 20 of Schedule 2 of FSMA.[48] The legislation does not define 'a contract of insurance' or the rights thereunder, as this is left to the Financial Services and Markets Act (Regulated Activities) Order 2000,[49] which – at s 3(1) – states that ' "contract of insurance" means any contract of insurance which is a contract of long-term insurance or a contract of general insurance' and lists several items that fall within that definition. Schedule 1 to the Order has a more extensive list of insurance contracts, but there is no reference to 'insurable interest', 'gambling' or 'wagering'.

Issues Paper 4 noted that the FSA 'thought that it would still be possible to distinguish insurance from other products without insurable interest'.[50] It also referred to the FSA's Policy Statement 04/19,[51] which was published, in part, because of the apparent need to address what is known as the 'Potts opinion'. In 1997, the International Swaps and Derivatives Association (ISDA) asked Robin Potts QC to provide an opinion on whether credit derivatives were insurance contracts for the purposes of the Insurance Companies Act 1982 (the predecessor to FSMA) and at common law.[52] Potts held that credit derivatives were not contracts of insurance and he relied on the absence of an insurable interest to support his conclusion. By contrast, the FSA stated in 04/19 that the presence of insurable interest was not a determining factor and it

44. FSMA is available at http://www.legislation.gov.uk/ukpga/2000/8/contents (accessed 29 November 2013).

45. The General Insurance Standards Council (GISC), a voluntary, non-statutory body, was responsible for the regulation of brokers and insurers dealing in general insurance until its responsibilities were taken over by the FSA in January 2005.

46. The PRA is part of the Bank of England and responsible for prudential regulation and supervision. See the Bank of England's website, available at http://www.bankofengland.co.uk/PRA/Pages/default.aspx (accessed 29 November 2013).

47. The FCA is responsible for business supervision. The FCA website is available at http://www.fca.org.uk/

48. Paragraph 21 of Sch 2 to FSMA covers participation in Lloyd's syndicates.

49. The Order is available at http://www.legislation.gov.uk/uksi/2001/544/contents/made (accessed 29 November 2013).

50. Issues Paper 4, para 7.4.

51. The policy statement is available at http://www.fsa.gov.uk/pubs/policy/ps04_19.pdf (accessed 29 November 2013).

52. Issues Paper 4, paras 7.9–7.17. The ISDA's letter to the Law Commission on this point is available at http://www.isda.org/whatsnew/pdf/Law-Commission04-18-06.pdf (accessed 29 November 2013).

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added that 'some credit derivatives would no longer fit within the parameters of Potts' opinion'.[53]

There is no indication that the PRA and FCA have adopted a different opinion to that of the FSA. Indeed, the FCA Handbook makes no reference to 'gambling' or 'wagering' in its copious materials on insurance products.[54] Further, the FCA does not refer to the doctrine in its Guidance on the Identification of Contracts of Insurance (PERG 6).[55] It is suggested, in light of the contents of both the governing legislation and regulatory bodies' own publications, that the argument that the doctrine is 'crucial' to the regulation of insurance is mistaken.

Moreover, it is important not to neglect the role of the Financial Ombudsman Service (FOS), which was established in 2001 to resolve disputes between consumers and businesses providing financial services, including insurance companies.[56] The FOS makes its decisions on the basis of what it believes is fair and reasonable in the particular circumstances of each case, taking into account the relevant law and regulations, codes of practice and (where appropriate) good industry practice.

In 2013, the FOS dealt with a dispute between a Mr W and Zurich Insurance plc concerning the former's claim in respect of the theft of a motor vehicle, which did not belong to Mr W but to a limited liability partnership (Mr W was a director of a company that was one of the partnership's members). The FOS accepted that, on 'a strict application of English case law as it currently stands', Mr W's claim would fail. Nevertheless, the FOS held that:

> On the available evidence, it [. . .] appeared fair and reasonable [. . .] that Mr W's claim should be considered on the basis that he did have an insurable interest in the vehicle. He had the exclusive use, control and enjoyment of the vehicle. He benefited from its existence, and suffered a detriment as a result of its loss.[57]

The second aspect of the 'dividing line', that of the tax (and accounting) treatment of insurance, was addressed in Issues Paper 4. It noted that the UK Revenue & Customs' Notice IPT 1[58] on Insurance Premium Tax referred to an 'insurable interest' as one of 'many or all of the features' of an insurance contract and explained the doctrine as being that the policyholder 'must suffer a financial or other loss on the happening of the insured event'. This does not, however, describe the doctrine for life policies and is closer to the definition of the indemnity principle than that of insurable interest for non-life policies. It is also worth noting that the UK Revenue & Customs

53. Issues Paper 4, para 7.15. The Potts opinion is also discussed in O Juurikkala 'Credit default swaps and insurance: against the Potts opinion' (2011) 26(3) J Int'l Banking L & Reg 128–135. The nature of credit derivatives discussed by Potts is also covered in D Arner, P Lejot and Qiao Liu *Finance in Asia: Institutions, Regulation and Policy* (London: Routledge, 2013) ch 8, pp 343–345, 362–365.

54. The FCA Handbook is available at http://fshandbook.info/FS/html/FCA (accessed 29 November 2013).

55. PERG 6 is available at http://fshandbook.info/FS/html/FCA/PERG/6 (accessed 29 November 2013).

56. The FOS website is available at http://www.fos.org.au/centric/home_page.jsp.

57. The full decision is available at http://www.ombudsman-decisions.org.uk/viewPDF.aspx?FileID=6840 (accessed 29 November 2013).

58. IPT1 is available at http://customs.hmrc.gov.uk/channelsPortalWebApp/channelsPortalWebApp.portal?_nfpb=true&_pageLabel=pageExcise_ShowContent&id=HMCE_CL_000194&propertyType=document (accessed 29 November 2013).

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Notice 701/36 – Insurance[59] contains a paragraph entitled 'What is insurance?' which makes no reference to the doctrine and instead refers readers to case-law and FSMA. The centrality of the doctrine to the tax treatment of insurance is, therefore, also questionable.

Dealing with the third, social, aspect of the 'dividing line', it has already been noted that the 1774 Act reflected the perception that someone who takes out a policy in respect of a 'celebrity's' life is merely gambling (with the insurer playing the role of the bookie) on the fate of that celebrity. While it seems unlikely that those wishing to have a 'flutter' would decide to do so by purchasing a motor or life policy rather than by visiting a betting shop or an online gambling website, the belief in the need to distinguish between insurance and more debauched activities apparently persists.[60]

A legitimate concern, however, is the problem that may be caused to those whose religious or cultural norms proscribe gambling in any forms. The Second Joint Consultation Paper noted that, under Islamic (Shari'a) law, insurance is permitted and operates under the *takaful* system. It is perfectly possible, and is both commercially acceptable and a sign of cultural and religious plurality, for insurers to offer *takaful* compliant insurance. The removal of an 'automatic' need for insurable interest in all policies does not deprive individuals of the right and ability to enter into insurance contracts that have such a provision. Indeed, many companies offer a range of Shari'a-compliant financial products, including insurance.[61] This concern, therefore, appears to have been addressed.

Finally, there is the place of insurable interest within the legal definition of insurance. There is no statutory definition of 'insurance', although FSMA identifies a number of 'insurance contracts'.[62] The courts usually avoided defining 'insurance', although in *Callaghan v Dominion Insurance Co*[63] Webster J stated that an 'insurance contract' was

> an agreement to confer upon the insured a contractual right which, prima facie, comes into existence immediately when loss is suffered by the happening of an event insured against, to be put by the insurer into the same position in which the insured would have been had the event not occurred, but in no better position.

There is no mention of the doctrine of insurable interest here, although it must be conceded that this definition – with its reference to 'loss' – also fails to reflect the position under contingent policies. In *Prudential Insurance v IRC*,[64] Channell J said that one of the three characteristics of an insurance contract was that the policyholder had 'an interest in the subject-matter', with the event(s) insured against being 'prima facie adverse to the interest'. Although this is also a reference to insurable interest, it seems to reflect the indemnity principle rather than the doctrine. Indeed, this 'characteristic' of Channell J's analysis was rejected by the Court of Appeal in *Gould v*

59. Notice 701/36 is available at http://customs.hmrc.gov.uk/channelsPortalWebApp/channelsPortalWebApp.portal?_nfpb=true&_pageLabel=pageExcise_ShowContent&id=HMCE_CL_000129&propertyType=document#P35_3849 (accessed 29 November 2013).
60. See R Merkin 'Gambling by insurance – a study of the Life Assurance Act 1774' (1980) 9 Anglo-Am L Rev 331 for a discussion of the issues raised by the 1774 Act.
61. See the Institute of Islamic Banking & Insurance website, available at http://www.islamic-banking.com/
62. Interestingly, the Commissions' Joint Scoping Paper raised the possibility of introducing a statutory definition of 'insurance'. Little appears to have come of this suggestion.
63. [1997] 2 Lloyd's Rep 54.
64. [1904] 2 KB 658.

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Curtis,[65] where Buckley LJ pointed out the distinction between contingency and indemnity insurance. If anything, these authorities demonstrate the confusion shared by many over the doctrine of insurable interest and the principle of indemnity. This confusion would be removed, at least as far as indemnity policies are concerned, if the doctrine was repealed. This would leave insurers, policyholders and the courts to focus on the actual policy wordings to determine what was covered (i.e. the insurer's liability), whether it was, in fact, lost (i.e. quantum) and the extent to which that loss should be made good (i.e. the indemnity principle).

Reason 2 – moral hazard

The second reason (or function) was as follows:

> It guards against moral hazard. By setting limits on the contracts that insurers may enter into, it protects insurers from themselves – from writing insurance which is overly speculative, or which encourages wrongdoing.

This reason seems to be based, in part, on the long-standing concern that a policyholder who has no insurable interest in the subject matter of the policy, and may benefit financially (by virtue of the claims payment) from the destruction of that subject matter, may instigate its destruction.

It is difficult to see how the presence of an insurable interest has deterred criminals when one examines, even on a cursory basis, the statistics on insurance fraud in the UK. For example, the UK Government's Annual Fraud Indicator published in March 2012[66] refers to insurance fraud of £2.1 billion per annum. Of this, £350 million was due to staged or induced motor accidents. The UK Insurance Fraud Bureau's report on so-called 'cash for crash' fraud suggests that many false claims involved the criminals' own vehicles.[67] Further, the most notorious recent example of life insurance fraud in the UK was John Darwin's disappearance in March 2002, when he was believed to have been killed while canoeing in the North Sea. Mrs Darwin made a claim on his life insurance policy despite the fact that her husband was still alive. Their plot was discovered over 5 years later and they were convicted for fraud. The fact that both Mr Darwin and Mrs Darwin would have had an insurable interest in the former's life does not seem to have deterred them.[68]

It is also worth recalling Bertram Harnett and John V Thornton's words when they addressed this point over 60 years ago:[69]

> Assume that X, an individual of criminal mind, seeks to defraud an insurance company. Assume further that the requirement of insurable interest does not exist

65. [1913] 3 KB 84.
66. The report is available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/118530/annual-fraud-indicator-2012.pdf (accessed 29 November 2013).
67. The Bureau's website is available at http://www.insurancefraudbureau.org/ – see also SA Rea Jr 'The economics of insurance law' (1993) 13 Int Rev Law & Econ 145–162, which argues that a property owner has a greater opportunity, compared to a non-owner, to damage his own property for fraudulent purposes.
68. The Darwins' case was dramatised by the BBC. See http://www.bbc.co.uk/programmes/b00rs2kc (accessed 29 November 2013).
69. In B Harnett and JV Thornton 'Insurable interest in property: a socio-economic re-evaluation of a legal concept' (1948) 48(8) Colum L Rev 1162–1188.

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> in his state. Can any one reasonably suppose that X will insure Building A, in which he has no property interest, burn it down, and then seek to collect the insurance? [. . .] Typically, X, as a reasonably prudent criminal will burn down his own property which he has overinsured. Since the property is his own, he can systematically plan the fraud and carry it out, undisturbed by prying eyes, and leaving the minimum of evidence – things he could only do with great difficulty were the property in the control of another.

This observation holds even greater weight today when the means of identifying such activities are even more powerful than in the 1940s.[70] Finally, it should also be recalled that, as the Commissions pointed out in Issues Paper 4, the argument that the doctrine is a deterrent to murder 'lacks logic', given that more murders are committed against spouses (in whose life the murderer would have an interest) than adult descendants (in whose life the murderer would not).[71] There is also the question of whether a private law doctrine has any place in a matter of public law.

The final aspect of this reason is that the doctrine 'protects insurers from themselves', maintains market disciple and ensures 'efficient underwriting procedures'.[72] The Commissions were, in the absence of evidence to the contrary, sceptical about these points. Indeed, it could be argued that the doctrine allows insurers to escape the consequences of inefficient underwriting procedures.[73] The Commissions did observe, however, that one of the alleged causes of the 2008 financial crisis was 'the involvement of banks and investors in financial instruments . . . which did not require the parties to show a direct interest in the trigger events' and that the doctrine restrained insurers from 'entering into speculative forms of trading'.[74] There are problems with this analysis.

There has been an enormous volume of expert (and not-so-expert) commentary on the causes of the 2008 financial crisis. While the details are beyond the scope of this paper, it is important to appreciate some key points. One of the alleged causes of the crisis was a growth in the practice of 'securitisation',[75] with the use of sophisticated financial products that some writers have described as having 'insurance-like' qualities.[76] It is alleged that these products 'neutralised' their holders' risks and, consequently, their motivation to maintain financial discipline. Moreover, these products – unlike general and life insurance – were operated by a variety of entities

70. For example, the International Association of Insurance Fraud Agencies (IAIFA) (website available at http://www.iaifa.org/index.html) was founded in 1985.

71. The UK Office for National Statistics crime & justice figures are available at http://www.ons.gov.uk/ons/taxonomy/index.html?nscl=Crime+and+Justice (accessed 29 November 2013).

72. Second Joint Consultation Paper, para 12.13.

73. See Nicoll, above n 30, in which it is submitted that the real issue is how a policy is constructed and that 'the onus [is] upon brokers and underwriters to ensure the words of the policy reflect what is intended'.

74. Second Joint Consultation Paper, para 12.15.

75. Securitisation is defined by The Financial Times as 'The creation and issuance of tradable securities, such as bonds, that are backed by the income generated by an asset, a loan, a public works project or other revenue source. Pooling of assets such as mortgages into securities that are sliced up and sold to different types of investor. Lenders pass on loans quickly, giving them few incentives to ensure they are repaid. Limited information on underlying assets makes them illiquid and hard to value.'

76. See M Smith 'The legal nature of credit default swaps' (2010) Lloyd's Mar & Com L Q 386.

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beyond the jurisdiction of financial regulators. On the other hand, the IMF has stressed that securitisation was not itself at fault.[77] Blame has also been directed towards those credit agencies that failed to assess the value of what was being traded in the world's financial markets.[78]

In light of such conflicting analyses, the suggestion that the doctrine of insurable interest somehow played a central role in ameliorating the financial crisis by imposing market discipline on insurers seems somewhat odd.[79] It is understandable, following the events of 2008, that many insurers would prefer not to be seen to be dealing in 'speculative' products, which some may see as a consequence of the abolition of the doctrine. The solution, however, would be to offer policies with or without a need for insurable interest and leave customers to choose between them, rather than perpetuate an unnecessary doctrine.

Reason 3 – invalid claims

This reason was summarised in the following terms:

> It protects the insurer from invalid claims. In theory, validity is a matter of policy wording: the contract should specify who can claim and in which circumstances. In practice, it is common for the policy to specify the subject matter of the insurance, without tying down the link between it and the insured. This is left to customary understandings, as upheld by court decisions specifying the type of insurable interest necessary for the type of insurance. Insurers feared that radical reform would interfere with these understandings. Claims could be made by a wider class of people, including those without close links to whatever has been insured.

In so far as 'invalid claims' relates to fraud, this has already been addressed. If the above summary is, however, an accurate reflection of the respondents' views, then the third reason seems to be broader than this and has two parts. The first is that courts' interpretation of insurance policies' 'customary understandings' is dependent upon the retention of the doctrine. The second resembles, in a way, the 'floodgates' argument that is often raised to resist claims that would, in the words of Cardozo CJ in *Ultramares Corporation v Touche*,[80] lead to 'liability in an indeterminate amount for an indeterminate time to an indeterminate class'.

As far as the first part of the third reason is concerned, it is worth recalling that insurance contracts are just that – contracts. Consequently, the general rules of contractual construction will be applied by the courts to any policy, irrespective of the presence of insurable interest. For example, the words in a policy must be given their

77. See *Containing Systemic Risks and Restoring Financial Soundness*, IMF Global Financial Stability Report (April 2008) ('IMF Report 2008') p xiii, available at http://www.imf.org/External/Pubs/FT/GFSR/2008/01/pdf/text.pdf (accessed 29 November 2013).
78. See V Bavoso 'Financial innovation and structured finance: the case of securitisation' (2013) 34(1) Company Law 3–12.
79. AIG, then the world's largest insurer, was a major casualty of the crisis, although was not a result of its traditional insurance activities. See WK Sjostrom Jr 'The AIG bailout' (2009) 66 Wash & Lee L Rev 943, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1346552 (accessed 29 November 2013).
80. (1931) 174 N.E. 441 at 444.

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natural and ordinary meaning, as per Stuart-Smith LJ's comment in *Yorkshire Water Services Ltd v Sun Alliance and London Insurance plc*:[81]

> The words of the policy must be given their ordinary meaning and reflect the intention of the parties and the commercial sense of their agreement. Thus they must be construed in their context.

Unfortunately, policyholders and insurers often disagree over the meaning of words within a policy, 'natural and ordinary' or otherwise, and wasteful litigation is a regular outcome of their failure to resolve this basic point at inception.[82] Even so, it is difficult to see how a court could interpret a policy so as to allow those 'without close links to whatever has been insured' to claim on a policy unless the words thereof demonstrate that to be the parties' intention. Similarly, under the *ejusdem generis rule*, the courts construe individual words in a policy according to the context within which they are used in the policy, unless it is clear that the parties intended another meaning. It is also the courts' practice to adopt a particular meaning for the same words used in similar policies by different insurers,[83] which would militate against a sudden expansion in the number of possible beneficiaries of a particular form of policy.[84]

Further, as Lord Hoffmann explained in *Investors Compensation Scheme Ltd v West Bromwich Building Society*:[85]

> Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.[86]

Lord Hoffmann added, citing Lord Diplock in *The Antaios Compania Neviera SA v Salen Rederierna AB*,[87] that where a detailed analysis of the words in a commercial contract led to a conclusion that flouted 'business common sense', the document 'must be made to yield to [that] business common sense'. This approach was confirmed by the Supreme Court in *Re Sigma Finance Corp (in administrative receivership)*[88] and in *Rainy Sky and others v Kookmin Bank*.[89] It was also demonstrated as recently as the Supreme Court's decision in *Employers' Liability Insurance 'Trigger' Litigation: BAI*

81. [1997] 2 Lloyd's Rep 113.
82. For example, in *Ted Baker Plc & Anor v Axa Insurance UK Plc & Ors* [2012] EWHC 1406, the Commercial Court held that 'theft' was to be given its ordinary and literal meaning, and rejected the insurer's contention that this ordinary meaning should give way to a business commonsense meaning derived from the background facts.
83. See *Dino Services Ltd v Prudential Assurance Co Ltd* [1989] 1 Lloyd's Rep 379.
84. The fact that the courts are required to do so does, however, remind us that insurers often apply different meanings to the same words and apply the same meanings to different words from policy to policy.
85. [1998] 1 WLR 896. In *De Souza v Home and Overseas Insurance Co Ltd* ([1995] LRLR 453 at 456), Mustill LJ warned that sometimes it is 'better to withdraw a little from the authorities to the former ground of this policy and these facts, and to look critically at each authority to see whether it really leads inexorably to a solution of our present problem'.
86. This 'background knowledge' is that which existed at the time of the contract and would be regarded as relevant by a reasonable person but – an important 'but' – it does not include the details of any negotiations, as per the rule laid down by Lord Wilberforce in *Prenn v Simmonds* [1971] 2 All ER 237.
87. [1985] 1 AC 191.
88. [2009] UKSC 2.
89. [2011] UKSC 50.

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(Run Off) Ltd v Durham,[90] where Lord Mance, in his leading judgment, began his analysis by stressing the need 'to avoid over-concentration on the meaning of single words or phrases viewed in isolation, and to look at the insurance contracts more generally'. Longmore LJ sounded a note of caution, however, in *Dornoch Ltd v Royal and Sun Alliance Insurance plc*,[91] when he remarked that 'there are dangers in judges deciding what the parties must have meant when they have not said what they meant for themselves'.

Despite the fact that it would be preferable if parties were clearer in their intentions, especially in light of Longmore LJ's concerns, it is difficult to see how the repeal of the doctrine of insurable interest would lead to an assumption by the courts that insurers and policyholders (who would, after all, still be the only ones paying the premiums) would be happy for strangers to benefit from their policies. That has certainly not been the experience in Australia since the doctrine was repealed there, as is discussed further below.

The second part of the third reason, the 'floodgates' argument, has been employed on many occasions before the English courts, notably to resist demands for compensation for pure economic loss and psychiatric injury in negligence claims.[92] In respect of the former, it was reflected in the House of Lords' decisions in *Caparo Industries plc v Dickman*[93] and *Murphy v Brentwood DC*,[94] which contributed to the judicial trend against the expansion of negligence following *Anns v Merton London Borough Council*.[95] In respect of the latter, Lord Steyn made it clear in *White v Chief Constable of South Yorkshire*[96] that abolishing or relaxing the rules restricting the recovery of damages for psychiatric injury 'would greatly increase the class of persons' who could recover such damages.

The floodgates argument has been the subject of much debate over the years. Lord Roskill identified both the basis of, and the flaw in, the argument when he commented in *Junior Books Ltd v Veitchi*:

> if it be just that the law should henceforth accord that remedy, that remedy should [not] be denied simply because it will, in consequence of this particular development, become available to many rather than to few.[97]

Consequently, if it is correct to repeal or reform the doctrine of insurable interest because of its various flaws, the fact that this may enable more people to take out insurance and make legitimate claims on their policies should not be a bar to such repeal or reform.

90. [2012] UKSC 14. Commonly referred to as '*The Trigger Litigation*'.
91. [2005] EWCA Civ 238.
92. In *R (on the application of Prudential Plc) v Special Commissioner of Income Tax* [2013] UKSC 1, it was held that extending the principle of legal advice privilege beyond its current limits risked opening a proverbial floodgate and permitting far too much documentation and advice to be withheld from disclosure.
93. [1990] 2 AC 605. Lord Bridge explicitly referred to Cardozo CJ's comment in *Ultramares* in the course of his judgment. In addition, Lord Oliver warned of creating 'a liability wholly indefinite in area, duration and amount and would open up a limitless vista of uninsurable risk for the professional man'.
94. [1990] 2 All ER 908.
95. [1978] AC 728. Other notable cases in this area include *Spartan Steel v Martin* [1972] All ER 557 and *Junior Books v Veitchi* [1983] 1 AC 520.
96. [1999] 2 AC 455.
97. [1983] 1 AC 520 at 539.

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Reason 4 – the global market place

The fourth and final reason was summarised as follows:

> In an increasingly global market place it is used to define where insurance is located and therefore which regulatory or tax regime it falls within.

This is a rather odd response given that, as will be seen, many jurisdictions use the doctrine and, consequently, it is difficult to see how it distinguishes an English insurance contract from one governed by, for example, Canadian or Hong Kong law. The fourth reason also seems to take little account of governing law or jurisdiction clauses in insurance contracts. In the absence of such clauses (which would, arguably, be a slip on the part of a reasonably competent broker or underwriter), contractual disputes between parties located in the UK and elsewhere are subject to the common law rules on conflict of laws or the EU Jurisdiction and Judgments Regulation.[98] While such matters are beyond the scope of this paper, the doctrine is unlikely – alone or in priority over other considerations – to determine which law should govern or which courts adjudicate a dispute over a particular insurance contract.[99]

Support for the fourth reason was provided by a paper by the ACE Group entitled 'Structuring Multinational Insurance Programmes: Current Challenges in the Asia Pacific Region' (the ACE paper).[100] The ACE paper examines the difficulties faced by a hypothetical multinational's parent company seeking consistent worldwide insurance cover for its various subsidiaries. It is explained that the parent company faces regulatory problems if it takes out a master policy against which its subsidiaries may claim (if and when their losses may not be covered by their own 'local' policies). These problems arise because some jurisdictions prohibit the insurer under the master policy from conducting business in their territory by directly insuring such risks. The solution proposed in the ACE paper is to remove the subsidiaries from the master policy and instead 'rely upon the basic legal concepts of insurable interest', which – in this case – would be the parent's liability to indemnify its subsidiaries. The ACE paper then, very briefly, examines the doctrine in Australia, Singapore, Hong Kong, Malaysia and New Zealand.[101]

Despite using the term 'insurable interest', the authors appear to be referring to the indemnity principle when they discuss how the scheme would operate. It is proposed

98. See S Sime *Blackstone's Civil Practice: A Commentary* (Oxford: Oxford University Press, 2013) ch 16. The Regulation is available at http://europa.eu/legislation_summaries/justice_freedom_security/judicial_cooperation_in_civil_matters/l33054_en.htm (accessed 29 November 2013).

99. *Dicey, Morris & Collins: The Conflict of Laws* (London: Sweet & Maxwell, 15th edn, 2012) is the definitive text on this subject. See also A Briggs *The Conflict of Laws* (Oxford: Oxford University Press, 2nd edn, 2008).

100. Second Joint Consultation Paper, para 12.12. The ACE paper is available at http://www.acegroup.com/Media-Center/ACE-Perspectives/Multinational.html (accessed 29 November 2013).

101. There are several surprising comments in relation to these jurisdictions. For example, it is implied that both Australia and New Zealand recognise the doctrine, whereas they do not, and it is suggested that 'there is no settled legal insurable interest requirement for non-life or non-marine policies' in Hong Kong, although an 'insurable interest is deemed to exist if [for example] the policyholder has legal or equitable title to the subject matter'. In actuality, the position in Hong Kong – with the exception of the absence of the Gambling Act 2005 – is on all fours with that in England & Wales.

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that such a scheme would cover the parent's own obligations or liabilities towards its overseas 'subsidiaries, affiliates and joint ventures' rather than these entities' liabilities to other third parties. Consequently, any claim by the parent on the policy would be justified by the fact that it had suffered loss by virtue of its need to indemnify its subsidiary in accordance with the indemnity principle (which would not be affected by the absence of insurable interest). How the doctrine is needed to operate such a scheme is difficult to see, particularly as the ACE paper uses an Australian master policy as an example despite – as already noted – the fact that Australia has abolished the doctrine.

On the wider subject of the 'global market place', Issues Paper 4 refers to a number of other jurisdictions and describes the approach that they take towards the doctrine. These are summarised in Table 2.

This is an eclectic survey of other jurisdictions, but it does demonstrate that while insurable interest is common in a number of major common law and civil law jurisdictions, it is not a universal doctrine.

Looking, first, at Australia, Issues Paper 4 explains that the Insurance Contracts Act 1984 (ICA)[102] was passed by the Australian Federal Parliament following a 1982 report by the Australian Law Reform Committee (ALRC),[103] which recommended the abolition of the requirement for an insurable interest at inception and at the time of loss for both non-life and non-marine policies (although the ALRC also recommended the doctrine's retention for life policies).[104] Consequently, s 16 of the ICA states:

> A contract of general insurance is not void by reason only that the insured did not have, at the time when the contract was entered into, an interest in the subject-matter of the contract.

Further, in respect of the need for an insurable interest at the time of loss, s 17 of the ICA adds:

> Where the insured under a contract of general insurance has suffered a pecuniary or economic loss by reason that property the subject-matter of the contract has been damaged or destroyed, the insurer is not relieved of liability under the contract by reason only that, at the time of the loss, the insured did not have an interest at law or in equity in the property.

The ICA was amended in 1995 to introduce a new s 18, which repealed the doctrine in respect of life policies. This move was apparently prompted by the recognition that the anti-gambling provisions in the law 'served no useful purpose'.[105] A further, minor, change in the ICA was provided by s 20, which stated that persons benefitting from a policy need not be named within the policy document.

Thus, contrary to what the ACE paper suggested, Australian insurance contracts are not subject to the doctrine of insurable interest. Further, its repeal does not appear to have had a deleterious effect on the Australian insurance industry. According to the

102. The ICA is available at http://www.comlaw.gov.au/Details/C2004C00163 (accessed 29 November 2013).

103. The ALRC website is available at http://www.alrc.gov.au/ and ALRC Report 20 on insurance contracts is available at http://www.alrc.gov.au/report-20 (accessed 29 November 2013).

104. See M Kirby 'Australian insurance contracts law: local reform with a global relevance' (2011) 4 J Bus L 309–329 for a discussion of the implementation of the ICA.

105. See Merkin, above n 37, para 8.7.

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Table 2: Insurable interest in other jurisdictions

Jurisdiction	Life policies	Indemnity policies
Australia	Not required	Not required
New York, USA	Required	Required
Canada	Required (with exceptions)	Required
Spain	Required (or the consent of person whose life is insured is required)	Required
Slovakia	Not required	*Not discussed in Issues Paper 4*
Germany	*Not discussed in Issues Paper 4*	Not required (but indemnity principle applies)
France	*Not discussed in Issues Paper 4*	Does not appear to be required (but contracts contrary to 'accepted morals' are prohibited)

OECD's figures, gross premiums rose from AU$61.2 billion in 1999 to AU$78.28 billion in 2008, which suggests that the country's insurers were doing well prior to the global financial crisis.[106] With respect to New Zealand, which was also referred to in the ACE report, ss 6 and 7 of its Insurance Law Reform Act 1985 abolished the doctrine of insurable interest for life policies and limited it for indemnity policies.[107] As with its near neighbour, the New Zealand insurance industry enjoyed a period of sustained growth in premiums in the years up to 2008.

While Canada (both federally and at the provincial level) retains the doctrine, Lord Eldon's formulation was rejected by the Canadian Supreme Court in *Constitution Insurance Company of Canada v Kosmopoulos.*[108] Mr Kosmopoulos was the sole shareholder and director of a leather goods company. The company's offices were leased in his own name and the insurance policy on the office was also in his own name. The insurers were 'well aware' of these facts. A fire in a neighbouring property damaged the company's offices but the insurers declined the claim on the policy.

The Canadian Supreme Court held that Mr Kosmopoulos was entitled to recover under the policy on the basis that, as the sole shareholder he was, in the words of Wilson J, 'so placed with respect to the assets of the business as to have benefit from their existence and prejudice from their destruction', which meant that 'He had a moral certainty of advantage or benefit from those assets but for the fire.' Wilson J went on to criticise Lord Eldon's formulation in *Lucena* and cast doubt on the traditional anti-gambling justification for the doctrine. The judge also expressed an appreciation of commercial realities when he stated:

> A broadening of the concept of insurable interest would, it seems to me, allow for the creation of more socially beneficial insurance policies than is the case at present with no increase in risk to the insurer.

106. See the OECD's Insurance Statistics Yearbook 1999–2008, available at http://www.keepeek.com/Digital-Asset-Management/oecd/finance-and-investment/insurance-statistics-yearbook-2010_ins_stats-2010-en-fr (accessed 29 November 2013). Performance still 2008 has not been as healthy, which is a problem shared across many jurisdictions.
107. The New Zealand Act is available at http://www.legislation.govt.nz/act/public/1985/0117/latest/whole.html#DLM75989 (accessed 29 November 2013).
108. (1987) 1 SCR 2.

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The gross premiums of the Canadian insurance industry increased from CA$70.05 billion to CA$121.3 billion in the period from 1999 to 2008, which does not suggest that the industry suffered from the courts' relaxed approach to the doctrine.

Finally, the New York Insurance Law, while retaining the doctrine, refers to an insurable interest in property in the following terms:

> In this article, 'insurable interest' shall include any lawful and substantial economic interest in the safety or preservation of property from loss, destruction or pecuniary damage.[109]

This language is closer to that of *National Oilwell* rather than Lord Eldon's formulation. Other US states, such as California, Utah and Wisconsin, have also repealed or amended the scope of the doctrine (at least to an extent that it is wider than Lord Eldon's formulation). There is no evidence that the insurers operating in those states have suffered as a consequence.

THE FUTURE FOR THE DOCTRINE

Unfortunately, in light of the strong support for the retention of the doctrine by those who responded to Issues Paper 4, the Commissions decided to recommend 'restating current principles in a clearer way' in relation to indemnity policies and 'widen[ing] the category' of those permitted to take out life policies. The Second Joint Consultation Paper contained six specific proposals in respect of indemnity policies and four in respect of life policies reflecting these broad objectives.[110] The 32 responses to these further proposals are not available, but the Commissions did publish a paper entitled 'Summary of Responses to Second Consultation Paper: Post Contract Duties and Other Issues' in February 2013.[111] They are revealing.

In response to a proposed statutory requirement that an insured under an indemnity policy has an insurable interest in the subject matter of the insurance, 77% of the respondents agreed and 13% disagreed (the remainder responded 'other'). The respondents rejected, by 59% to 23%, a proposal to leave the definition of insurable interest entirely to the courts. Instead, 69% favoured a non-exhaustive statutory list of types of interest that 'would be sufficient to constitute an insurable interest'. Their attitude is also apparent from the fact that 80% of them agreed that those with an indemnity policy should have an insurable interest at the time of loss and 69% felt that they should also possess it (or expect to do so) at inception.[112] This would mark a retrograde step from the current law. The respondents were more flexible when it came to life policies. Sizeable majorities agreed that parents should be entitled to take out insurance on the life of a child under 18 and that cohabitants should have an insurable interest in each other's lives.

109. Article 34, s 3401 is available at http://codes.lp.findlaw.com/nycode/ISC/34/3401 (accessed 29 November 2013).

110. Second Joint Consultation Paper, paras 12.36–12.69, 13.66–13.116.

111. Of these 32 responses, 14 were from insurers, brokers and their trade associations, and a further ten from lawyers, 'legal associations' and the judiciary. There do not appear to have been any from consumer groups or similar bodies. The Summary of Responses document is available at http://lawcommission.justice.gov.uk/consultations/post_contract_duties.htm (accessed 29 November 2013).

112. The suggestion was that 'the insurance would only be void if there was never a real probability that an insurable interest would be acquired'.

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Despite there being little evidence that the doctrine of insurable interest maintains the distinction between insurance and gambling, guards against moral hazards and prevents invalid claims, a sizeable proportion of the UK insurance industry embraces the doctrine. Indeed, many in the industry oppose the courts' attempts to ameliorate the consequence of the doctrine, usually in favour of policyholders, in such cases as *National Oilwell* and *Feasey*. Why is this so? Surely the indemnity principle provides a sufficient safeguard against claims by those who have suffered no loss? A cynic would suggest that insurers defend the doctrine because it defends them from claims that they would prefer not to pay. Sadly, the respondents' submissions that the doctrine 'protects insurers from themselves' and allows them to rely on 'customary understandings' of policy wordings tend to support such a suggestion.

The doctrine is generally used as a purely technical defence, much in the same way as the principle of utmost good faith was,[113] in circumstances where insurers are unable to demonstrate that the policyholder has committed fraud. This was certainly the case in *Macaura*.[114] It is also raised as a defence when insurers are presented with the consequences of having failed to adequately identify who or what was covered in the policy. This was, arguably, the problem in *National Oilwell*. It is submitted that the answer to fraud is the greater use of claims investigators, loss adjusters and investment in agencies such as IAIFA. The answer to risks that are difficult to assess or define is for insurers to either decline to underwrite them or to put more effort into drafting their policies.

Unfortunately, as has already been touched upon, the difficulties caused by poorly drafted policy wordings are as great as, if not greater than, those caused by the doctrine of insurable interest. Moreover, they would remain even if the doctrine was repealed. For example, in *The Trigger Litigation*, the Supreme Court was tasked with deciding what was meant by the terms 'sustained' and 'contracted' in employers' liability (EL) policies in the context of claims by individuals who have suffered from exposure to asbestos fibres in the course of their employment.[115] The difficult legal and ethical issues raised by this case, and subsequently in *IEG Ltd v Zurich Insurance Plc*,[116] did not include the doctrine.

The problem with policy wordings is hardly a new one; indeed, Issue 4 of the FOS' *Ombudsman News*, published in April 2001, contained an item entitled 'Calling a Spade a Shovel – Lack of Clarity in Policy Documents'.[117] Yet, in 2012–2013 the FOS reported that complaints relating to Payment Protection Insurance (PPI) represented 74% of all new complaints and that, of these, 'Many complaints we see hang on what the smallprint of the PPI policy says and means.'[118] Efforts to improve, clarify or standardise policy wordings include various statement of best practice and model

113. Utmost good faith has now been abolished for consumer insurance by the Consumer Insurance (Disclosure and Representations) Act 2012, which is available at http://www.legislation.gov.uk/ukpga/2012/6/contents/enacted (accessed 29 November 2013).
114. See Lowry and Rawlings, above n 38.
115. See G Meggitt 'The "rock of uncertainty" – mesothelioma, insurers and the courts' (2013) J Bus L 563.
116. [2013] EWCA Civ 39.
117. Available at http://www.financial-ombudsman.org.uk/publications/ombudsman-news/4/calling-a-spade-a-shovel.htm (accessed 29 November 2013).
118. The FOS annual review and PPI factsheet are available at http://www.financial-ombudsman.org.uk/publications/ar13/about.html#product (accessed 29 November 2013) and http://www.financial-ombudsman.org.uk/results.html?q=ppi%20policy (accessed 29 November 2013), respectively.

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wordings issued by the Association of British Insurers (ABI).[119] The Chartered Insurance Institute (CII) has recently published a report that addresses the 'lack of clarity for a long time now – for insurers, adjusters and customers – over certain aspects of BI [business interruption] policies'.[120] Perhaps the most significant development in this respect was the introduction of the Market Reform Contract at Lloyd's in 2007.[121]

Unfortunately, the Commissions did not address contract certainty and clarity in policy wordings – beyond Issues Paper 2 on warranties and Issues Paper 9 on the requirements for a formal marine policy – in any great detail. The reasons for this lack of action and the advantages (and disadvantages) of any reform are important matters but must be left to another paper. Moreover, the truth is that, irrespective of any efforts to improve wordings, the doctrine of insurable interest will continue to apply to UK insurance policies and will continue to create confusion. Any reforms that the Commissions propose in their draft Bill, which is expected by the summer of 2014, are unlikely to represent the clear break with the past that many hoped for when the insurance contract law review started in 2006.[122] Indeed, if future legislation introduces a need for an insurable interest at the inception of indemnity policies, this will represent a break with the past only by increasing the application of the doctrine.

Australia abolished the doctrine of insurable interest, in part, in 1984 and, in its entirety, in 1995. This decision, and indeed the overall reform project embodied with the ICA, was met with considerable opposition from the Australian insurance industry. Yet, as noted by Robert Merkin, 'Twenty plus years on, the system appears to have bedded down with relatively little difficulty.'[123] It should also be noted that the Insurance Contracts Amendment Act 2013 became law on 28 June 2013, introducing further reforms to the ICA, including a definition of third-party beneficiaries of policies.[124] Australia is forging ahead in the field of insurance law reform, having introduced a third major set of changes to its substantive law since the 1980s, while the UK has only the (albeit welcome) Consumer Insurance (Disclosure and Representations) Act 2012 to show from almost 8 years of work. In the absence of any major developments from the insurance industry, the Commissions or Parliament, it can only be hoped that the courts (and the FOS) will continue to display a creative and constructive approach towards the doctrine.

119. The ABI website is available at https://www.abi.org.uk/

120. See http://www.barnesandnoble.com/w/business-interruption-policy-wordings-harry-roberts/1117218412?ean=9780900493959 (accessed 29 November 2013).

121. See J Burling *Lloyd's Law and Practice* (London: Routledge, 2014).

122. An up-to-date overview of the Commissions' proposals may be found in D Hertzell and L Burgoyne 'The Law Commissions and insurance contract law reform: an update' (2013) 19 J Int'l Mar L 105.

123. Merkin, above n 37, para 1.3.

124. The Act is available at http://www.comlaw.gov.au/Details/C2013A00075 (accessed 29 November 2013).

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