CHAPTER FOUR

INSURANCE: SECTION 4

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4.1 Insurance : the concept

The duty to take out insurance against liability arising under the Act is provided in Section 4. Some points of detail concerning this section will be discussed later. But, before doing so, it appears to be desirable to deal with the concept of insurance. Two elements are essential in insurance -(i) risk of loss and (ii) indemnification against loss. Insurance provides protection or security against the risk, by creating a right to be indemnified. The classical description of the nature of the contract of insurance is that given by Channel, J.[1] :-

"..... It must be a contract whereby, for some consideration, usually but not necessarily for periodical payments called a premium, you secure to yourself some benefit, usually but not necessarily, the payment of a sum of money upon the happening of some event....". Then the "next thing that is necessary is that the event should be one which involves some element of uncertainty. There must be either some uncertainty whether the event will happen or not, or, if the event is one which must happen at some time or another, there must be uncertainty as to the time at which it will happen."

4.2 Some important features of contract of insurance

The contract of insurance possesses certain peculiar features. First, it is contingent and not absolute. It comes into operation, only if the risk protected against actually occurs. Secondly, except in the case of life insurance, it gives indemnity only. No one can make a profit out of a contract of insurance. Thirdly, on payment of the amount undertaken to be paid by the insurer to the assured, the former succeeds to the rights which the latter may have, to sue a third party whose act has caused the loss which was insured against. Fourthly, a person can, in general, take out insurance only if he has an "insurable interest"- a feature that helps to save a contract of insurance from being challenged as a wagering agreement. This is important, because an agreement by way of wager is "struck with invalidity at the outset, i.e. before the event contemplated by the wager has occurred:."[2] Fifthly, the contract of insurance is contract *uberri mae fidei*. The insured must disclose all material facts.

4.3 Duty of disclosure

The duty of disclosure requires that the insured must make full disclosure of all material facts; otherwise the contract may be avoided. The rationale of this requirement has been dealt with more than once in decided cases. As Lord Mansfield said,[3] insurance is a contract upon speculation, where the special facts upon which the contingent chance is to be computed, lie generally in the

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1. *Prudential Insurance Co.* v. *I.R.C.*, (1904) 2 K.B. 658, 663.
2. *Hill* v. *William Hill (Park Lane) Ltd.*, (1949) 2 All E.R. 452, 464 (per Lord Greene).
3. *Carter* v. *Boehm*, (1766) 3 Burr 1905, 1909.

knowledge of the assured only, so that good faith requires that he should not keep back anything which might influence the insurer in deciding whether to accept or reject the risk. As explained by Bayley, J.[1], the contrary doctrine would lead to frequent suppression of information. Hence the obligation to disclose all material facts known to the assured. It will then be in the interest of the assured to make a full and fair disclosure of all the information within their reach. In this context, "material fact" according to one view means every circumstance which would influence the judgment of a prudent insurer in fixing the premium or determining whether he will take the risk.[2] What is the test to be adopted regarding disclosure? Three tests have been adopted:-

(1) *Test of "prudent insurer"*, i.e. every circumstance is material which would influence the judgment of a prudent insurer in fixing the premium or determining whether he will take the risk.[3] The test is adopted by statute in legislation relating to marine insurance. In cases relating to non-marine insurance, the test adopted is of a "reasonable" insurer in some cases.[4]

(ii) The test of *reasonable assured* is sometimes adopted. "If a reasonable man would have recognised that it was material to disclose the knowledge, then the non-disclosure is fatal."[5]

(iii) *Test of current insurance practice.* In England, the Law Reform Committee[6] considered the matter and stated that the practical effect of the then existing rule relating to non- disclosure was that insurers were entitled to repudiate their liability whenever they could show that a fact within the knowledge of the insured was not disclosed which, according to *current insurance practice*, would have affected the judgment of the risk. However, the Committee took note of the position that "a fact may be material to insurers, in the light of the great volume of experience of claims available to them (insurers) which would not appear to a proposer for insurance, however honest and careful to be one which he ought to disclose". The recommendation of the Committee was "that for the purpose of any contract of insurance, no fact should be deemed (to be) material unless it would be considered material by a *reasonable insured* ".[7]

4.4 Facts usually considered material

According to a well known writer,[8] in general, it can be said that the following facts will usually be held to be material :-

1) All facts suggesting that the subject matter of insurance is exposed to more than ordinary danger from the peril insured against.

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1. *Lindenau* v. *Desborough* (1828) 8 B & C 586, 592.
2. *Locker & Wool Ltd.* v. *Western Australian Insurance Co. Ltd.*, (1936) 1 K.B. 408.
3. Ivamy, General Principles of Insurance Law (1975), page 112.
4. *Mutual Life Insurance Co. of New York* v. *Ontario Metal Products Co. Ltd.*, (1925) A.C. 344, 351 (P.C.).
5. *Joel* v. *Law Union and Crown Insurance Co.*, (1908) 2 K.B. 863, 884 (C.A.).
6. L.R.C., 5th Report 1957; Cmd. 62, para 4 and 14.
7. *Cf.* Law Commission Report No.104 (October 1980).
8. Ivamy, General Principles of Insurance Law (1975), page 117.

2) All facts suggesting that the proposed assured is actuated by some special motive.

3) All facts showing that the liability of the insurers might be greater than would normally be expected.

4) All facts relating to the "moral hazard".

5) All facts which, to the knowledge of the proposed assured, are regarded by the insurers as material.

In the Canadian Province of Quebec, article 2485 of the Civil Code provides that, "The insured is obliged to represent to the insurer fully and fairly every fact which shows the nature and extent of the risk and which may prevent the undertaking of it or affect the rate of premium."[1]

4.5 Disclosure in liability insurance

Of the five propositions mentioned above, some are applicable to liability insurance. A few illustrations are offered below, for a concrete understanding of the subject.

Illustrations

(i) In fire insurance of a motor car, the structure and locality of the garage may be material, if it increases the chances of fire or diminishes the chance of fire being extinguished.[2] The logic here is, that the subject-matter is exposed to more than ordinary danger.

(ii) Over-valuation of property, if deliberate and with motive of speculation, is non-disclosure of material fact.[3]

(iii) In an "all risks" policy of pictures and objects of art, it is material to disclose that the premises are unoccupied outside hours of business, because that fact would increase the insurer's liability.[4]

(iv) In a case of public and products liability insurance,[5] it was held that failure to disclose a previous attempt to renew an insurance similar to the insurance proposed, would amount to failure to disclose a material fact. This falls under the category of "moral hazard". This is on the logic that one of the matters to be considered by an insurance is the question of moral integrity of the proposer- what has been called the "moral hazard".[6]

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1. Ivamy, General Principles of Insurance Law (1975),page 120, footnote 13, referring to *reselodge Ltd.* v. *Castle,* (1966) 2 Lloyd's Rep. 113.
2. *Dawsons Ltd.* v. *Bonnin,* (1922) 2 A.C. 413.
3. *Thames and Mersey Marine Ins. Co.* v. *Gunford Ship Co.,* (1911) A.C. 529 (A.C.)
4. Haase v.Evans, (1934) 448 Ll. L. Rep. 131.
5. *Claude R. Ogden & Co. Pty. Ltd.* v. *Reliance Fire Sprinkler Co. Pty,Ltd.* (1975) 1 Lloyds' Rep. 52 (Australia).
6. *Locker & Woolf Ltd.* v. *Western Australian Insurance Co. Ltd.,* (1936) 1 K.B. 408 (C.A.).

(v) If the assured *knows* that a certain fact is regarded by the insurers as material, then that fact is regarded as material in law. Such knowledge can be presumed from the fact that specific question is asked about it.[1]

(vi) A fact which is expressly made the "basis of the contract", undoubtedly makes it a material fact. Such a clause makes the truth of the answers (on the facts included in the "basis" clause) a condition precedent.[2]

In England,[3] the recommendation of the Law Reform Committee in this regard was that "notwithstanding anything contained in or incorporated in a contract of insurance, no defence to a claim should be maintainable by reason of any misstatement of fact by the insured, where the insured can prove that the statement was true to the best of his knowledge and belief".

4.6 Policy of insurance and cover note

Section 4(1) of the Public Liability Insurance Act requires that the owner shall take out a "policy of insurance". Strictly speaking, in law, a "policy" is a formal document evidencing a contract of insurance. Although no particular form of policy is usually prescribed by law, in practice, it is an elaborate document incorporating a variety of clauses. A policy is preceded by a "cover note" in many types of insurance (though not in life insurance). Black, *Law Dictionary* (1990) explains "cover note" as a written statement by the insurer's agent that coverage is in effect. The purpose of a cover note in motor insurance was explained at length by Pearson, J.[4] (as he then was). From his judgment, it is enough to quote the following passage:-

> "The typical motorist is an impatient person, in the sense that having bought a car he wishes to take delivery and drive off in it at once and he would not be willing to wait for the traditional steps to be taken at Lloyds' before he could obtain cover. Therefore, even in the United Kingdom, there has to be the familiar system of the cover note which is issued at once on receipt of proposal and covers the assured and puts the underwriters on risk for the period while the proposal is being considered and until a policy is either granted or refused."

4.7 Cover note as creating liability

That the cover note itself creates a contractual liability (subject to its own terms) is now well established, not only in motor insurance[5] ' but also in accident insurance[6] as well as in fire insurance.[7] There are quite a few decisions expressly laying down the following propositions:-

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1. *Glicksman* v. *Lancashire and General Insurance Co.*, (1927)A.C. 139 (H.L.).
2. *Anderson* v. *Fitzgerald*, (1853) 4 H.L. Cas. 484 (life insurance).
3. L.R.C. 5th Report, *Conditions and Exceptions in Insurance Policies* (1957), Cmd. 62, para 14.
4. *Julien Praet et Cie S/A* v. *H.G. Poland Ltd.*, (1960) 1 Lloyd Rep. 420, 428, Ivamy General Principles of Insurance Law (1975)page 90-91.
5. *Cartwright* v. *Mac Cormack (Trafalgar) Insurance Co. Ltd.*, (1963) 1 All E.R. 11 (C.A.) (Third Party).
6. *Levy* v. *Scottish Employers' Ins. Co.*, (1901) 17 T.L.R. 229.
7. *Mackie* v. *European Assurance Society*, (1869) 21 L.T. 102.

(i) The cover note is, in itself, a contract of insurance.[1]

(ii) If loss occurs during the currency of the cover note, then the cover note governs the rights and liabilities of the parties.[2]

(iii) The contract contained in the cover note can therefore be enforced by the assured, provided that he has complied with its conditions.[3]

It would therefore seem that although the Public Liability Insurance Act speaks of a "policy of insurance", yet, once the assured obtains a cover note, he is protected(if he complies with its terms) under the law of insurance. And, if that be so, he should be deemed to have complied with the mandate of Section 4(1). There are at least two reasons for reaching this conclusion:-

(i) statutes relating to matters dealt with in business should be construed in the light of the practice usually followed in the business;

(ii) since, under the general law of insurance, a valid contract comes into existence on the issue of cover note, the object of the Public Liability Insurance Act is substantially achieved.

4.8 Section 4(1): Duty of owner to take out insurance policies

The mandate of Section 4(1) is that every owner shall "before he starts handling any hazardous substance ", take out insurance policies against liability to give relief under Section 3(1). The sub-section does not go into any details of the contents or nature of the policy. It is enough if protection by way of insurance is taken against the liability arising under Section 3(1). Non-compliance is punishable under Section 14(1).

A verbal point arises under Section 4(1). The statutory obligation must be performed before the owner starts handling any hazardous substance. Having regard to the definition of "handling" in Section 2(c), insurance must be taken before each of the steps or processes mentioned in Section 2(c), such as manufacture, processing, treatment etc, is commenced. Taken literally, this would mean, that for every separate hazardous activity, the insurance must be taken separately. But this would not be practicable. What seems to be intended is, that the owner must take out the insurance before actually commencing a business in the course of which a hazardous substance is "handled". The point needs attention.

The proviso to Section 4(1) gives a breathing period to existing operations.

4.9 Section 4(2): Renewal of policy

Section 4(2) provides for periodic renewal of insurance policies taken under Section 4(1).

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1. *Mackie* v. *European Assurance Society,* (1869) 21 L.T. 102, 104 (Malins, V.C.).
2. *Re Coleman's Depositories Ltd. and Life and Health Assurance Association* , (1907) 2 K.B. 798.(C.A.).
3. *Roberts* v. *Security Co. Ltd.,* (1897) 1 Q.B. 111, 116 (C.A.).

4.9 A Section 4(2A) to (2D): Details of insurance policy and Relief Fund

In 1992, there were inserted, in Section 4 of the Public Liability Insurance Act, four sub-sections, namely, (2A) to (2D). The first two deal with certain details concerning insurance policies, while the next two sub-sections deal with crediting certain amounts to the Environment Relief Fund, to be constituted under Section 7A.

4.10 Section 4(3): Exemption from obligation to insure

Section 4(3) empowers the Central Government to grant exemption, from the obligation to insure, to Government, Government corperations etc. This is on the condition that they maintain a separate fund in accordance with the rules for meeting the liability under Section 3. It is worth noting that no power is given to exempt a foreign corporation, nor any company or firm in the private sector. Besides this, there is no power to exempt authorities which do not form part of Government. Hence Universities or research institutions or national laboratories which are neither corporate bodies nor directly managed by the Government, cannot be exempted.

4.11 No exemption from liability

A point that is likely to be missed should be mentioned here. It concerns the scope of the exemption that can be granted under Section 4(3). The exemption (where granted) has to be confined to the obligation to insure. No exemption can be granted in respect of the no fault liability introduced by Section 3. Thus, the provisions of that section cannot be relaxed even in respect of the Government or other authorities mentioned in Section 4(3).