

# Insurance & Reinsurance

## Law Briefing

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## Is there a rôle for the concept of the “real” claimant in a subrogated claim?

**Alison Padfield of Devereux Chambers considers *Graham v Entec Europe Ltd (t/a Exploration Associates)* [2003] EWCA Civ 1177, *The Times*, September 10, 2003, a recent decision of the Court of Appeal concerning extension of time periods under s.14A of the Limitation Act 1980 in the context of a subrogated claim, and suggests that the approach of the Court of Appeal to the question of whether there are any circumstances in which the insurer may be treated as the “real” claimant in a subrogated claim departs significantly from the approach traditionally taken by the courts.**

The doctrine of subrogation entitles an insurer, once it has paid the sum insured and provided it indemnifies its insured against costs, to bring a recovery action against a third party in the name of the insured (see *Castellain v Preston* [1882–83] L.R. 11 Q.B.D. 380). Insurance is a contract of indemnity, pursuant to which the insurer agrees to indemnify the insured in respect of losses actually suffered. At the same time, the fact that the insured has the benefit of insurance should not result in

a windfall to a wrongdoer who has caused loss to the insured. This is where the doctrine of subrogation comes into play: it allows the insurer to bring an action against the wrongdoer in the name of the insured (or to recover any proceeds from the insured if the insured brings an action in his own name after he has been indemnified against loss), ensures that the insured is never more than fully indemnified against the losses he has suffered, and does not profit from an event giving rise to loss. But the doctrine of subrogation could not operate without two other principles, which are interlinked and were established during the nineteenth century. These are, first, that it is no defence to a claim by an insured on a policy of insurance that the insured has a claim against a third party; and, secondly, that it is no defence to a subrogated claim that the insured has been indemnified by the insurer.

The result of these principles, taken together, is that the approach taken by the courts has, as far as the defendant is concerned, traditionally been to regard dealings between insurer and insured as *res inter alios acta* (or, to put it more bluntly, as being none of the defendant's business). The substance of the matter is borne out by the form of the action: it is the insured who is the party on the record once proceedings have started. Although it is commonly known to the other side that the insured has been indemnified and that the claim is a subrogated claim, this is not apparent from the form of the action, which looks to all the world like a claim brought by the insured against the third party.

The facts of *Graham v Entec Europe Ltd* were as follows. The claimant had been advised by a surveyor in relation to the causes of subsidence at a bungalow, and

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as to the remedial works required. The claimant was insured under a policy of property insurance, and the insurer indemnified him in respect of the damage to the bungalow. The insured’s claim was dealt with for the insurer by an outside loss adjuster who had been retained for this purpose. The insurer subsequently brought proceedings in the insured’s name, alleging negligence against the surveyor. The proceedings were begun after the expiry of the primary six-year limitation period under the Limitation Act 1980, and the insurer sought to rely on s.14A of the 1980 Act in order to extend the time for bringing the claim. Section 14A provides that an action may be brought within three years from the date of knowledge of the “plaintiff or any person in whom the cause of action was vested before him” (s.14A(5)).

On the face of it, the wording of the statute is clear: the “plaintiff” (now, of course, to be read as a reference to the claimant) is the insured; the cause of action was not previously vested in anyone; and it is therefore the insured’s knowledge that is relevant. Indeed, Potter L.J. indicated, in the introduction to his judgment in the Court of Appeal (at para.3), that the principal question raised by the appeal was whether a loss adjuster appointed by a claimant’s insurers in a subrogated claim could have knowledge attributable to the claimant for the purposes of s.14A. This encapsulation clearly identifies the insured as the claimant for the purposes of the statutory provision.

However, Potter L.J. subsequently recorded a concession made by counsel for the insured (as the party on the record) that, in relation to a subrogated claim, “the nominal plaintiff/claimant is fixed with the knowledge of the insurer for whose benefit the action is brought” (para.36). It is clear from Potter L.J.’s judgment that this concession was made under pressure from the Court of Appeal; and Potter L.J. indicated that, in his view, it was correct. He continued: “... I consider that the spirit and purpose of the Act is to concentrate upon the knowledge of the person who has the right and interest in pursuing the claim” (para.36). The avowed juridical basis for this construction was the similarity between the concepts of subrogation and assignment. Following an assignment, the knowledge of both assignor and assignee would be relevant for the purposes of s.14A, as the cause of action would have vested first in one and then in the other. This may explain Potter L.J.’s further formulation of the principle, which he was seeking to apply, as follows: “... it is plainly appropriate to construe the words ‘the plaintiff’ in clause 14A(5) as meaning/extending to a plaintiff

whether suing in his own name or the name of another by way of subrogation” (para.37). The use of the composite phrase “meaning/extending to” appears to suggest that the knowledge of both the insured and the insurer may, in appropriate circumstances, be taken into account for the purposes of s.14A, as it would be in the case of an assignment of a cause of action. At the same time, the formulation introduces the concept of a claimant suing in the name of another (or, in other words, the concept of the “real” claimant) in the proceedings being someone other than the party on the record.

As we have seen, the courts have traditionally treated subrogated claims as if they really were what they appear to be – claims by the insured against a third party. The notion that the insurer is somehow the “real” claimant is at odds with the principles underlying the doctrine of subrogation and the very nature of insurance as a contract of indemnity. But *Graham v Entec Europe Ltd* is not the first time that an attempt has been made to persuade the courts to adopt this approach. Two examples, in particular, immediately spring to mind. First, disclosure. In a subrogated action, the insurer, as well as (and, in some cases, rather than) the insured, may have control of documents which fall within the definition of standard disclosure under the Civil Procedure Rules; yet the approach of the courts to disclosure has been to treat the insured, as the party on the record, as bearing the disclosure obligation. In *Wilson v Raffalovich* [1880–81] L.R. 7 Q.B.D. 553, the insurers brought a subrogated action in the name of the insured. An order was made that the insured should put in a further and better affidavit stating what documents were in its possession relating to the matters in question in the action. An application was made on behalf of the insurers, as the “real plaintiffs” to the action (Coleridge C.J. at p.554), to be relieved from further obedience to the order, as the insured was abroad and was refusing to co-operate with insurers. Intriguingly, the concept of the “real” claimant (or, as it was then, plaintiff) was expressly considered and rejected by the Court of Appeal in the nineteenth century in this case (at p.557). Although Jessel M.R. had considerable sympathy with the insurers, in his view the position was clear (at p.558):

“As long as these plaintiffs are the plaintiffs on the record, they must be taken to be the parties conducting the litigation, and they must conduct it according to the rules of English jurisprudence and obey the orders of the English Court in which the action is brought.”

Brett and Cotton L.JJ. concurred; Brett L.J. was also sympathetic to insurers, expressing regret that the Court of Appeal could not find in favour of the insurers (at p.559): “I am sorry to say that although it sounds exceedingly just, I do not think it is according to law.”

As the obligations as to disclosure and inspection of documents under the Civil Procedure Rules are expressed to be on each “party” to proceedings (see CPR 31.6, which defines standard disclosure, and the opening words of which are: “Standard disclosure requires a party to disclose ...”), it is suggested that there has been no change of principle as a consequence of the coming into effect of the Civil Procedure Rules.

The second example is the award of interest. Attempts to unmask the insurer as the “real” party to the proceedings in the context of claims for interest have, in the main, received short shrift from the courts. In *H Cousins & Co v D&C Carriers* [1971] 2 Q.B. 230, the Court of Appeal held that, in exercising its discretion in relation to the award of interest, the fact that the insurer has indemnified the insured is *res inter alios acta* as far as the defendant to the subrogated claim is concerned. Interest is therefore to be awarded as though the insured had not received an indemnity, and taking into account the insured’s financial position. The insured does not receive a windfall because a term is implied into the contract of insurance allowing the insured to retain interest accruing prior to the date of settlement by the insurer; and the insurer is entitled to the interest after that date. This might result in a windfall to the insurer in some cases, as the rate of interest awarded would normally be based on the claimant’s borrowing status, particularly in the Commercial Court, and an insurer is typically able to borrow funds at lower rates of interest than the average insured. Where the claimant insured has been indemnified by the insurer, and it is the insurer who will retain the interest after the date of indemnity, one might think that, in exercising its discretion in order to achieve a result that would be fair to both parties (this being the basic principle governing the exercise of the discretion to award interest: see *Birkett v Hayes* [1982] 1 W.L.R. 816, the court should award interest at a lower rate after the date of indemnity. Indeed, this was the approach taken by the Court of Appeal in *Harbutt’s Plasticine Ltd v Wayne Tank & Pump Co Ltd* [1970] 1 Q.B. 447, Denning M.R. using the memorable phrase, “The wind should be tempered to the shorn lamb” (at p.468), to express the principle that the insured’s changed circumstances following receipt of monies from the insurer should be taken into account by the court in exercising its discretion as to the award of

interest. In *H Cousins & Co v D&C Carriers*, the Court of Appeal distinguished *Harbutt’s Plasticine* on the grounds that the case had proceeded on the false assumption that, as between insurer and insured, the insured would be entitled to retain the whole of any award of interest.

It is suggested that the Court of Appeal should have taken a more literal approach to the construction of s.14A of the Limitation Act. This would have been consistent with the courts’ rejection of the concept of the insurer as the “real” claimant in relation to other aspects of subrogated claims; and, after all, the section makes express provision for assignment of causes of action, and could easily have done the same in respect of subrogated claims if this had been the intended meaning. There is an obvious tension between the requirement, in a subrogated claim, for the court to disregard the reality of the situation, and the requirement, whether in relation to the extension of the limitation period or in relation to the award of interest, to do justice between the parties. But the result is that the construction placed on the s.14A is a departure from, and difficult to reconcile with, the traditional approach to subrogated claims.

Returning for a moment to the facts of *Graham v Entec Europe Ltd*, it will be remembered that the insured’s claim was investigated for the insurer by an outside loss adjuster who had been retained for this purpose. The knowledge which was relevant for the purposes of s.14A of the Limitation Act 1980 was the knowledge not of the insurer itself (prior to any attribution), but of the loss adjuster. Having decided that the insurer’s knowledge was relevant, the Court of Appeal decided that, essentially on agency principles and by simple analogy with the position had the loss adjuster been an employee of the insurer, the knowledge of the loss adjuster could be imputed to the insurer so as to make it the insurer’s knowledge for the purposes of the statute. This being so, the Court of Appeal concluded that the proceedings had been commenced out of time.

*Alison Padfield is a barrister specialising in insurance and reinsurance. She is the author of Insurance Claims (Butterworths, 2003). Alison would like to thank Colin Edelman Q.C. for reviewing this article in draft form.*