

Prof. dr XXX ADEMUN-ODEKE*

Windfall in marine and export credit insurance policies in Anglo-american and other common law jurisdictions

Additional exception or simply a further limitation and modification of indemnity and subrogation?*

PART II

UDC: 368.2:656(73)

Received: 5. 8. 2017.

Accepted: 20. 12. 2017.

Systematic scientific work

4. WINDFALL RELATIVE TO SUBROGATION AND INDEMNITY

4.1. The Relationship Between Windfall, Subrogation and Indemnity

Part I of this article surmised that windfall can only be understood in the context of indemnity, to which it relates through subrogation of the insurance contract. It also deduced that the principle of indemnity in insurance law is fundamental to its operation and forms one of its crucial cornerstones.¹ It is the

* Visiting Professor, Bilkent University Law School, Ankara, Turkey; Visiting Professor, Ankara University Law School, Ankara, Turkey; Deputy Director, Turkish Law of the Sea Centre, Ankara University Law School, Ankara, Turkey. LLB (Dar); LLM, PhD (Soton); MBIM; MIEEx; MNI; Ex-UN; Managing Consultant, Bahari Maritime Consultants, Southampton. The author is indebted to Lloyd's of London Insurance for the generous funding of a Fellowship via the US-UK Fulbright Commission that enabled the main research on Insurance of International Trade and Foreign Investments; Professors Martin Davies (Director) and Robert Force (Emeritus Director), Admiralty Law Institute, Tulane University Law School, New Orleans, USA, for hosting him; Professor Michael Tsimplis (Director) and Staff, Institute of Maritime Law, Southampton University Law School, for hosting him; Professor James Duggan, Director and his staff, Library Services, Tulane University Law School, for their enormous help; and Megan Gold and Debo Awofase, his Tulane and Southampton Research Assistants respectively. However, all responsibilities, shortcomings in and views expressed in the article are the author's own. E-mail: ademun.odeke@gmail.com

** Based on work in progress on books by the author on *Insurance of FOB CIF Contracts* and *Insurance of International Trade and Foreign Investments*.

¹ MIA 1906, for the official text see <https://www.legislation.gov.uk/ukpga/Edw7/6/41/contents>; indemnity is contained in ss.1, 32 and 79-81; s.79 provides that:

'controlling' factor holding subrogation together, a position supported by Justice Brett in the seminal case of *Castellain v Preston*.² The principle is now contained

“Rights of Insurer on Payment.

79 Right of subrogation.

(1) Where the insurer pays for a total loss, either of the whole, or in the case of goods of any apportionable part, of the subject-matter insured, he thereupon becomes entitled to take over the interest of the assured in whatever may remain of the subject-matter so paid for, and he is thereby subrogated to all the rights and remedies of the assured in and in respect of that subject-matter as from the time of the casualty causing the loss.

(2) Subject to the foregoing provisions, where the insurer pays for a partial loss, he acquires no title to the subject-matter insured, or such part of it as may remain, but he is thereupon subrogated to all rights and remedies of the assured in and in respect of the subject-matter insured as from the time of the casualty causing the loss, in so far as the assured has been indemnified, according to this Act, by such payment for the loss.

80 Right of contribution.

(1) Where the assured is over-insured by double insurance, each insurer is bound, as between himself and the other insurers, to contribute rateably to the loss in proportion to the amount for which he is liable under his contract.

(2) If any insurer pays more than his proportion of the loss, he is entitled to maintain an action for contribution against the other insurers, and is entitled to the like remedies as a surety who has paid more than his proportion of the debt.

81 Effect of under insurance.

Where the assured is insured for an amount less than the insurable value or, in the case of a valued policy, for an amount less than the policy valuation, he is deemed to be his own insurer in respect of the uninsured balance”.

² (1883) 11 Q.B.D. 380 at 386 that “indemnity is the controlling principle in insurance law”.

in s.1 of the MIA 1906.³ Except for life insurance,⁴ most insurance contracts including fire,⁵ motor,⁶ fidelity,⁷ burglary⁸ and ECGD⁹ policies are indemnity contracts to which indemnity and subrogation, and therefore windfall, apply. The rationale for applying indemnity to these insurance contracts was identified by Justice Johnston in *Brodigan v Imperial Livestock and General Insurance Co. Ltd.*,¹⁰ where he, in turn, cited with approval Lord Justice Bowen's statement in *Castellain v Preston*, that: "If such policies were regarded as value policies then the contract of insurance wouldn't be a contract against loss, but might become a 'speculation for gain.'"¹¹ Any connection with windfall, in this instance, being that the latter is an unintended consequence of the insurance function, not speculation on the insured's part.

There are several anti-windfall measures within insurance law and practice. To prevent the insured making a gain from insurance he is precluded from recovering more than the actual loss. Any recoveries exceeding that would amount to windfall. Indemnity, therefore, refers to the insurer's role of placing a fully-indemnified insured back into the position he would be in if the loss had not occurred, less any excess he has agreed, unless underinsured. In other words, as in tort and unlike contract law remedies, insurance is backward rather than forward-looking. To recover, the insured must prove insurable interest. Pennfather J, in *Vance v Forster*,¹² enshrined this position when he laid down the rule that:

³ The section provides that:

"A contract of Marine Insurance is a contract whereby the Insurer undertakes to indemnify the assured in a manner and to the extent thereby agreed, against marine losses, that is to say the losses incident to a marine adventure."

Although originally a marine insurance principle, indemnity applies to non-marine insurance and the MIA 1906, although of English origin, applies to Ireland and common law jurisdictions and informally forms the basis of most insurance legislation worldwide.

⁴ *Dalby v India and London Life Assurance Co. Use* (1854) 15 CB 365.

⁵ *North British and Mercantile Insurance Co. v McLellan* (1892) 21 SCR 288.

⁶ *Page v Scottish Insurance Corporation Ltd.* (1929) 140 LT 571 CA.

⁷ *Employer's Liability Insurance Corporation v Skipper and East* (1887) 4 TL 55.

⁸ *Symons v Mulkern* (1882) 46 LT 736.

⁹ *Re Millar, Gibb and Co. Ltd.* [1957] 2 All ER 266.

¹⁰ *Brodigan v Imperial Livestock and General Insurance Co. Ltd.* (1927) 61 I.L.T.R. 193.

¹¹ *Castellain v Preston* (1883) 11 Q.B.D. 380 at 401.

¹² *Ibid.*, at 52.

"Although the insured cannot recover beyond the sum insured upon each particular item of insurance, he can't even recover that sum unless he can prove that he has sustained damage, and then he will recover a sum commensurate to the loss which he has sustained".¹³

Accordingly, the amount payable under the policy is measured to the extent of the insured's actual and real pecuniary loss. The importance and overriding requirement of indemnity underlies rules that operate in the event of a loss. Different considerations will apply regarding whether the claim relates to a total or partial loss in ships, goods or property. Once the insured's actual loss is measured and calculated, he will be indemnified accordingly.¹⁴ However, despite all these anti-windfall measures, its retention by the insured persists.

For these reasons, while special rules exist under indemnity principles to enable the insurer to measure the insured's loss and indemnify him accordingly, other rules such as unjust enrichment also operate to prevent the insured receiving a windfall or being doubly compensated for his loss. Allowing the insurer to stand in the place of the insured and exercise any rights the insured is entitled to exercise against a third party responsible for the loss is a further demonstration that subrogation was developed to aid indemnity, ensuring that the insured does not obtain more than is sufficient to satisfy that loss. Indemnity is, therefore, the main justification for subrogation and the prevention of unjust enrichment in insurance. Reasons for the departure of life, contingency and accident life policies from indemnity principles are that the amount payable to the insured in the event of a specified contingency is a fixed sum and that this amount is not calculated strictly in proportion to the measurement of the insured's loss. It is argued, however, that with the exception of perhaps life policies, certain aspects of contingency and accident policies should fall under indemnity principles, to aid indemnity in its role of preventing unjust enrichment. Surely, if an insurance contract does not fall under indemnity principles, it logically follows that subrogation will not apply and the insured will retain all benefits including windfall.

Conversely, why and how is the insured allowed to retain windfall in some but not all cases? Does that not in itself undermine subrogation and indemnity, the very cornerstones of insurance? In other words, should windfall retention by the insured (permissible in ECGD

¹³ *Vance v Forster* (1841) Ir. Cir. Rep 47.

¹⁴ For an interesting discussion of the various calculation rules which the courts and insurers apply in situations where there has either been a partial or total loss see: Birds, 2007 at 313

and other insurance branches) also form an additional limitation, exception or modification to subrogation and indemnity? If not, is the continued permitting of windfall retention therein, despite the rules above, based on policy, law or equity? This paradox of possible windfall limitations on an insurer's subrogation rights in some but not all insurance contracts is addressed below, within a paragraph which also establishes the link between windfall, subrogation and equity.

4.2. Windfall in Indemnity and Subrogation Exceptions

4.2.1. Windfall and the rights available to the insured

Besides life,¹⁵ personal accident¹⁶ and contingency¹⁷ insurances, should windfall in ECGD policies be added to the exceptions, limitations or modifications to indemnity and subrogation? The answer is in the affirmative. The reason being that application of the exceptions, limitations and modifications to subrogation in turn depends on how and when the insurers derive their rights. However, insurers may derive their rights of subrogation from up to four possible sources.¹⁸ The first is from *automatic subrogation*, where *Castellani v Preston*¹⁹ is still the authority for the proposition that subrogation applies automatically to all contracts of insurance, often referred to as the *first subrogation* (the second being *legal subrogation*, in turn, founded in *contractual subrogation*; the third being *tort-based subrogation* and the fourth *general subrogation*). All four types include equity elements and applications. Such applications would

¹⁵ *Dalby v India and London Life Assurance* (1854) 10 CB 365.

¹⁶ Considered part of life insurance and therefore not subject to indemnity principles: *Bradburn v Great Western Railway Co.* (1874) LR 10 Exch 1 at 2 per Bramwell B.

¹⁷ Contingency insurance based on contingency interest, s.7 MIA; *Clay v Harrison* (1829) 10 B & C 99.

¹⁸ Conditions limiting subrogation include:

(a) insurer entitled only to those rights available to insured - *Simpson v Thomson* (1877) 3 App Cas 279, at 284 HL, per Lord Cairns;

(b) insurer subrogated only to rights possessed by the insured - *Sea Insurance Co. v Hadden* (1884) 13 QBD 706 at 718 per Lindly LJ;

(c) insurer entitled only after payment - *Commercial Union v Lister* (1874) 9 ChApp 483 (fire but applicable to marine);

(d) include payment in diminution of loss but not voluntary gifts intended for his use alone - *Burnand v Rodocanachi* (1882) 7 App Cas 333 HL; and

(e) application may be excluded by the terms of the policy or trade usage - *Tate v Hyslop* (1885) 15 QBD 368, CA.

¹⁹ *Castellain v Preston* (1883) 11 QBD 380.

limit windfall to rights only available to the insured. There is also a near-universal consensus (Birds, 1979; Kimball, Davis, 1962, 841)²⁰ that insurers have another source of subrogation rights, whereby contracts often contain express subrogation clauses which may limit or extend the insurer's legal subrogation rights. These rights may be termed 'contractual' or 'conventional' subrogation. These clauses extend windfall to rights not available to the insured.

However, the right to subrogation can in no way be an absolute right. As will become evident below, first its application and exercise can be circumvented in many ways. Secondly, the insurer is entitled only to those remedies, rights or other advantages which are available to the assured himself. Thus, if for example two ships, A and B, are the property of the same owner, and A is sunk by the negligence of those in charge of B, the insurers of A, having paid as for a total loss, have no claim upon the owner, insofar as the owner cannot be answerable in damages to himself.²¹ Thirdly, the advantages to which the insurers by subrogation succeed include any payment made in diminution of the loss in respect of which the insurers are liable. These advantages are not confined to those which the assured has a right to demand. Furthermore, they do not include benefits in the nature of a voluntary gift,²² which he may have received from a third person if those benefits were intended to be received by him for his own use alone and not to accrue to the insurer.²³ This includes instances where the gift amounts to windfall. Finally, the application of subrogation may be excluded by the terms of the insurance policy or by any usage of trade to which it is subject.²⁴ Nevertheless, this context of windfall does not conflict with or affect this exception to the application of subrogation, since a gift does not constitute 'rights available to the insured'. For the purposes of windfall, there seems to be a difference between rights available to the insured generally and those available to the insured relating specifically to the

²⁰ (The Extension of Insurance Subrogation) available at www.j-stor.org, an online search engine providing online journals specialising in many areas of study.

²¹ *Simpson v Thomson* (1877) 3 App Cas 279 at 284, HL, per Lord Cairns LC, and at 288 per Lord Penzance.

²² As in a gratuitous transfer of the ownership of property: *Esso v Customs & Excise* [1976] 2 All ER 117; Birds, 2007, 312-3.

²³ *Burnand v Rodocanachi Sons & Co.* (1882) 7 App Cas 333, HL, explained in the South African decision of *Stearns v Village Main Reef Gold Mining Co.* (1905) 10 ComCas 89, CA, in a manner inconsistent with the explanation of Brett LJ in *Castellain v Preston* (1883) 11 QBD 380 at 391, CA.

²⁴ *Tate v Hyslop* (1885) 15 QBD 368, CA.

subject matter of a particular case. How does this affect the whole remit of subrogation and windfall?

4.2.2. *Windfall and the assured's rights on the subject matter*

The second and perhaps most important of the major limitations on the exercise of the insurer's rights is where the insurer either has not paid up at all under the terms of the policy or has not paid the full indemnity. Case law has clearly established that subrogation does not arise until the insurer has indemnified the insured for his loss.²⁵ This was confirmed by Lord Justice Scrutton in *City Tailors Ltd. v Evans*,²⁶ where he opined that, "When the underwriter has paid and not until then is he subrogated to any of the legal rights the insured may have to reduce the loss".²⁷ This limitation in action is further supported by the decision in *Scottish Union & National Insurance Co. v Davis*²⁸ - a motor insurance decision. In this case, the insured's car with the agreement of the insurer was placed in a garage for repair. After three unsuccessful attempts at repair, the dissatisfied insured took his car elsewhere. The insurer paid the bill without getting a note of satisfaction from the insured. The insured subsequently received compensation from a third party and used it to fix the car.

The insurer's subrogation claim was rejected by Justice Russell, on the basis that, "You only have a right to subrogation in a case like this when you have indemnified the assured and one thing is quite plain... you have not done that".²⁹ The insured retained the windfall. The reasoning in this case appears to be that where the insurer attempts to indemnify the insured by authorising repairs to the subject matter of insurance (in this case a car) that subsequently turns out to be unsatisfactory, the insured cannot be said to be fully indemnified. As will be further apparent in paragraph 4.2.3 below, there is a difference between full indemnity

²⁵ To the extent that it is based on the general or *legal subrogation* as enunciated in *Castellain v Preston*, subrogation only becomes available when the insurer has discharged his liability under the contract. Until then he is not legally entitled to exercise any of the insured's rights. However, express contractual provisions may remove this right. Where such a clause is inserted in the policy, this limitation may be overridden by agreement of the parties. See Birds, 1979 for an interesting analysis of contractual subrogation.

²⁶ (1921) 91 J.L.K.B. 379.

²⁷ *Ibid.*, at 385.

²⁸ *Scottish Union & National Insurance Co. v Davis* [1970] 1 Lloyd's Rep. 1.

²⁹ *Ibid.*, at p.5.

and full compensation, both of which have a bearing on windfall. Full indemnity relates only to the insured value and not necessarily the full insurable value or market value of the subject matter of the contract. Neither does it include under-insurance and excess. For those reasons, case law relating to under-insurance and partial loss has caused problems in the determination of windfall in relation to subrogation and indemnity.

Hence, while the insured may insure the contents of his house, for instance, for a certain amount this may not necessarily correspond to the actual value of the contents of the house. Such an event is known as under-insurance,³⁰ whereby the insured will be said to be fully indemnified under the terms of the policy but may not be necessarily fully compensated for his loss. Under the rules relating to under-insurance, full indemnification by the insurer under the terms of the policy may not fully compensate the insured for his actual loss. Furthermore, the insurer is subrogated only to those rights possessed by the assured in respect of the matter to which the contract of insurance relates. Consequently, where a vessel such as on a demurrage or freight is damaged by collision, and her owners recover (from those by whose negligence it was caused) damages in respect of matters which are not covered by the policy on the ship, the insurers cannot, on paying for a total loss, claim from the assured the amount of those damages.³¹ This is because, where a vessel is partially damaged by a collision, the insurer is entitled to deduct from the cost of repairs one-third new for old, whereas the tortfeasor has no right to make any such deduction, which, in turn, affects subrogation and windfall.

The practice in such a partial loss case is to divide the amount recovered from the wrongdoer rateably between the vessel's owners and the insurers - *windfall sharing*.³² As such, the insured owner retains all damages awarded to him in respect of demurrage, and also the money paid in respect of the remaining two-thirds. The insurer retains only such portion of the damages as are attributable to the two-thirds which he has paid.³³ Nevertheless, this concept of *windfall*

³⁰ Provided in s.81 of the MIA 1906.

³¹ Under-insurance ss.32 and 81 of the MIA 1906; see also Note 36 below and for text p.7 below.

³² *Sea Insurance Co. v Hadden* (1884) 13 QBD 706 at 718, CA, per Lindley LJ.

³³ To the extent that it is based on the *general subrogation* or *legal subrogation* as enunciated in *Castellain v Preston*, subrogation only becomes available when the insurer has discharged his liability under the contract. Until then he is not legally entitled to exercise any of the insured's rights. However, express contractual provisions may remove this right. Where such a clause is inserted in the policy, this limitation may be overridden by agreement of the parties. See Birds, J, 'Contractual

sharing has not gained grounds in either English nor wider common law, and would only be possible if windfall applied to both parties' indemnity rights. That notwithstanding, the insured only has rights on the subject matter and the insurer on subrogation. Rather, this article maintains that windfalls are freak phenomena occurring outside both parties' actions and rights on the subject matter. This article argues that the occurrence of windfall is a freak situation, especially in ECGD policies, arising independently of either the assured's or the insurer's actions or rights on the subject matter. It is a result of unintended consequences which both English and wider common law are not equipped to deal with. Thus, any attempt to fit it within the rigid existing rules governing subrogation and indemnity is therefore illogical. This is irrespective of whether the full compensation and full indemnity considerations are involved.

4.2.3. Windfall and under-insurance: 'full compensation' or 'full indemnity'?

The above proposition, that windfall is also subject to both full compensation and full indemnity, continues to exorcise courts and needs further analysis. Until recently, there was still confusion between full compensation and full indemnity and the application of subrogation. However, the interplay of under-insurance or self-insurance and excess further complicates the determination of windfall. For instance, a self-insured by under-insured coupled with a large excess, especially in a falling market, may be indemnified and yet not be fully compensated. The reverse may be true in a rising market, but still to the insurer's detriment. Nevertheless, should the insurer bear the risks of the insured's under-insurance and excess in a falling market, in what is a contractual bargain? Buckley, on Irish jurisdiction, looks at the issue of whether the insurer must merely be fully indemnified under the terms of the policy before a duty to subrogation arises or has to be fully compensated in fact for his actual loss (Buckley, 2006, 138). This issue is very likely to arise in practice either through excess clauses,³⁴ which are commonly included in insurance contracts, or where the insured has insured the subject matter for less than its market value, (i.e. under-insured it).³⁵ For some time, it was thought that where the insured was fully indemnified under their policy, but the policy did not fully compensate him, the insured

subrogation in insurance', *op. cit.*, for an interesting analysis of contractual subrogation.

³⁴ See Note 16 of Part I to this article, on excess.

³⁵ Under-insurance, see also Note 31 above.

was entitled to remain *dominus litis* of any litigation subsequently brought against third parties (Mitchell, 1996, 347). In other words, an insurer was not entitled to any reimbursement out of third party funds until the insured was fully compensated for his loss. To the best of the author's knowledge, the only common law authority for this proposition is the Irish authority of *Driscoll v Driscoll*,³⁶ in which the insured argued that he did not need to contribute anything to the insurer out of third party compensation funds until he was fully compensated for his loss. O'Connor, Master of the Roles (MR), held this view to be correct and found in favour of the insured, holding that:

"I think that the foundation of the doctrine of subrogation is to be found on the principle that no one is to be paid twice on the one loss. The corollary of this is that a contract of indemnity against a loss should not have the effect of preventing the insured being paid once in full".³⁷

No authoritative decision on the issue existed under English law until relatively recently in *Napier v Hunter*,³⁸ where the House of Lords took a very different approach from *Driscoll v Driscoll* as to when an insurer is entitled to remedies against its insured. The case concerned a number of policies which contained excess clauses. Following the occurrence of the insured's risk, the insured were fully indemnified under the policy subject to their excess clauses. The issue before the court was whether the insurers were entitled to reimbursement after they had indemnified the insured under the terms of the policy, but before the insured were fully compensated for their loss under the excess clauses. The House of Lords held that the insured had agreed to bear the amounts of their underwriting losses represented by the excess clauses in their policies and accordingly they were not entitled to be indemnified out of the settlement money until the insurers were indemnified in full pursuant of their rights of subrogation.³⁹ Lord Jauncey summed up the law in the majority decision thus:

³⁶ *Driscoll v Driscoll* [1918] 1 I.R. 152. Subrogation is not an area of law that has given rise to frequent disputes in Ireland, although the cases that do exist illustrate well the core principles of the doctrine, which are generally in line with insurance principles laid down in the UK and other Common Law jurisdictions. See Corrigan, Campbell, 1995, 57. Indeed, this point relating to priority in a subrogated action is the only area of insurance law where there appears to be a divergence between English and Irish precedence. This article focuses on the Anglo-Irish jurisprudence, as it is more extensive.

³⁷ *Ibid.*, at p.153.

³⁸ *Napier v Hunter* [1993] 2 W.L.R. 42.

³⁹ *Ibid.*, at 43.

“If an insured has suffered an insured and uninsured loss, full indemnification of the former subrogates the insurers irrespective of the fact that the insured hasn’t yet recovered his uninsured losses.”⁴⁰

Accordingly, after the insurer has fully indemnified the insured under the terms of a policy, the principle of *unjust enrichment* kicks in. The insurer then has priority to any subsequent monies received by the insured regardless of whether or not he has been fully indemnified for his loss,⁴¹ which eliminates the insured’s windfall prospects.

This view is consistent with the US decision in *NGDA MSC Med v Wall Street*,⁴² whereby although a subrogated insurer may recover only what it has paid to the insured, a partially compensated insured may still bring an action for the entire loss. The insured’s recovery is then impressed with a trust to the insurer for the payment. It is only on payment of the whole of the loss sustained by the assured, whether total or partial, that the insurer is entitled to be subrogated to his rights of action. Therefore, if the amount insured is less than the amount of that loss, the insurers, even though they have paid the amount insured, will not be subrogated to those rights. The assured, then, remains the person who has control of the suit in any proceedings brought by him against the person primarily liable, and will be entitled to compromise without the insurer’s assent, provided always that he acts in good faith without any intention to sacrifice their interests.⁴³ There would appear to be no conflict as the windfall does not affect the insurer’s priorities. Thus, windfall does not affect this exception and will apply irrespective of whether compensation is full or partial. That view also seems to be in line with *Yorkshire Insurance’s* suggestion that even subrogation itself:

“...was more than a convenient way of referring to those terms which were implied to give business efficacy to an agreement, whereby the assured should be fully indemnified and never more than fully indemnified by the insurer.”

⁴⁰ *Ibid.*, at 64.

⁴¹ On this point see *Kuwait Airways Corporation v Kuwait Insurance Co. SAK* (No.2) [2000] 1 Lloyd’s Rep 252; for (No.1) see [1999] 1 Lloyd’s Rep 803 and for (No.3) see [2000] 1 Lloyd’s Rep IR 678.

⁴² 2014 AMC 280; *CF MSC Flaminia*, 2015 AMC 1087 (SDNY) that an insurer pays the insured for a loss, the insured has interest in the claim and the action of the subrogated insurer’s counsel may not be imputed to the insured.

⁴³ *Commercial Union Assurance Co. v Lister* (1874) 9 Ch App 483 (a fire policy, but the principle of the decision applies equally to marine insurance).

It makes no difference to subrogation, and consequently on windfall, whether it is after or before payment by the insurer (Burglass, 1991, 444).⁴⁴ But would it make any difference to the sequence whether windfall is affected by implied and express provisions in the policy?

5. WINDFALL IN LAW AND EQUITY

5.1. Entitlement to Windfall in Law

The basis of windfall is best understood against the background of equity and subrogation. As a contractual outcome, windfall relates to subrogation and indemnity. However, does that position extend to equity principles as well? To appreciate this problem, it is necessary to examine first whether subrogation is an express or implied provision, and secondly whether it is an equitable or common law concept. The answer to the above might help explain why windfall is permitted in some, but not all, subrogation cases. Many authorities have centred on whether the doctrine originates from common law or equity and decisions of the Court of Chancery,⁴⁵ A strong proponent of the former view is Justice Diplock, who has referred to subrogation as a common law doctrine arising out of an implied term in every contract. He was of the view that common law courts called on the court of equity only where its auxiliary jurisdiction was needed to compel the insured to lend his name to his insurer for the enforcement of his rights and remedies,⁴⁶ In US law, however, subrogation seems to be of two types:

⁴⁴ *Global Insurance Intl. Mar.*, 2011 AMC 1568 where the \$147,000 amount paid to the insured by the insurer exceeded the \$64,000 to which the insured was “legally entitled”, the insurers were entitled to the difference. Note, however, that the \$80,000 difference was not a third-party payment and therefore a windfall, but rather due to a 63% comparative fault. It was rightly decided that the insured held that in trust for the insurers, otherwise it would be a clear case of windfall.

⁴⁵ The Court of Chancery was a Court of Equity in England and Wales that followed a set of loose rules to avoid the slow pace of change and possible harshness of the Common Law. It is currently the Court of Equity under the Lord High Chancellor that began to develop in the 15th century to provide remedies not obtainable in the courts of Common Law. Today, the court comprises the Chancery Division of the High Court of Justice; see also Note 3 above on the history of the doctrine.

⁴⁶ Most notably his statements can be found in the following cases: *Hobbs v Marlowe* [1977] 2 ALL E.R 241, 254-255, *Yorkshire Insurance Co. Ltd. v Nisbet Shipping Co.* [1962] 2 QB 330, 339. While in *Morris v Ford Motor Company* [1973] Q.B. 792, similar views were expressed by James J, at 812.

“...either conventional or legal; the former being where subrogation is express, by the acts of the creditor and the third person; the latter being (as is the case of sureties) where the subrogation is effected or implied by the operation of the law (Black, 1990, 1427)”.

This statement requires further clarification. By ‘conventional’, Black seems to mean express and by ‘legal’, he presumably means arising by the operation of the law. In that respect, he seems to confine subrogation to law (Black, 1990, 897),⁴⁷ thereby omitting subrogation in equity.⁴⁸ Once satisfied that the principle of subrogation derives its origins from common law rather than equity, the next question is whether the doctrine is contractual or an implied term under the contract. This is important as it determines whether and why the insured is allowed to retain windfall in some but not all cases. In other words, must the parties expressly provide for subrogation for it to arise or should courts be permitted to imply it? Correspondingly, should windfall also be implied or expressly provided for? This article proceeds on the basis that subrogation does not only arise automatically in the insurance contract, but that it can also be modified or limited by express contractual terms entered into by the parties. Against this assumption, however, it must be noted that Lord Denning has argued that subrogation derives its origins also from equitable principles.⁴⁹ This debate is crucial to understanding whether entitlement to windfall should be based on law or equity and therefore, whether the equitable doctrine of unjust enrichment should apply to windfall.

The Denning view has been confirmed in the relatively more recent case of *Napier v. Hunter*.⁵⁰ The issue there was whether the insurer had an equitable proprietary interest in certain money held by the insured’s solicitor, or a common law right to action for money had and received (in other words a mere personal right). The court ruled that upon payment to the insured under the policy, the doctrine of subrogation had conferred on the insurer an equitable proprietary

⁴⁷ Arising by the operation of the law and arising from property cases as in *Federal Land Bank of Baltimore v. Jones* 179 Va. 394 18 S. E 2d 917 at 920; *Martin v Hickenlooper* 90 Utah 150, 59 P.2nd 1139 at 1141 and *Lervold v Republic Mut. Fire Ins. Co.* 142 Kan.43 45 P.2d 839 at 842.

⁴⁸ As to equitable subrogation see, supra, subsection (e) immediately below.

⁴⁹ However, in *Morris v Ford Motor Company* [1973], Justice Denning at 800-801 and Stamp LJ at 806-807 disagreed with James J and held subrogation to be based on equitable principles.

⁵⁰ *Napier v Hunter* [1993] 2 W.L.R 42.

right in the form of a lien over the settlement money.⁵¹ Justice Templeman concluded that, “an insurer has an enforceable equitable interest in the damages payable by the wrongdoer”.⁵² However, it is doubtful whether *Napier v Hunter* is an authority for general contractual or simply equitable subrogation at common law. This position varies from those cited above and by other commentators such as Rawlings and Lowry (Rawlings, Lowry, 2003, 589) who, in quoting *Mitchel* (Mitchell, 1996, 348) noted that:

“In Lord Napier and Ettrick Hunter, the House of Lords construed the idea of indemnity in light of the contract so that the rights of subrogation arose once the insurers had met their obligations under the contract, even though the insured’s loss might not have been fully covered”.

That notwithstanding, in another recent approval of the equitable jurisdiction of the doctrine, Birds is of the persuasive view that it is certainly incorrect to say that subrogation is exclusively equitable, as it appears to have been applied in common law courts long before the fusion of law and equity (Birds, 1979, 128).⁵³ Black (Black, 1990, 539) also agrees, referring to equitable subrogation as a, “Legal fiction through person who pays debt for which another is primarily responsible is substituted, or subrogated, to all rights and remedies of others”. He cites the Michigan Supreme Court decision of *Commercial Union Ins. Co. v. Medical Protective Co.*⁵⁴ as his source. From the above, and since the origins of the doctrine remain obscure, a safer conclusion is that subrogation may be classified as a legal doctrine supported by equity, which can be modified, extended or limited by express provisions (Birds, 1979, 31). Perhaps the same categorisation should be extended to its creation, and unintended consequence, windfall. How does that relate to legislative provision of windfall?

5.2. Entitlement to Windfall under the MIA 1906

Whatever differences of opinion exist as to the origins of subrogation, its principles and operations are

⁵¹ *Ibid.*, at p.43. As noted, the courts have on occasion invoked equity to refuse subrogation on discretionary equitable grounds. Of particular interest is the case of *Morris v Ford Motor Company* [1973] Q.B. 793 discussed below.

⁵² *Ibid.*, at p.46.

⁵³ (Contractual subrogation in insurance). This fact was indeed highlighted by Diplock J in *Yorkshire Insurance Co. v Nisbet Shipping Co.* [1962] 2 Q.B. 330 at 339.

⁵⁴ *Commercial Union Ins. Co. v Medical Protective Co.* 426 Mich. 109, 393 N.W. 2d 479 at 487.

now codified in the MIA 1906,⁵⁵ s.79(1)⁵⁶ and s.79(2).⁵⁷ The assured is “indemnified according to this Act,⁵⁸ when he has received the indemnity agreed upon, even though he may remain out of pocket”.⁵⁹ This implies that whether or not the insured is out of pocket is irrelevant for the determination of entitlement to windfall. It had long been established by case law that the right of subrogation is a necessary incident of the contract of indemnity, and it operates on every right and remedy, “by which the loss is insured against can be or has been diminished”.⁶⁰ If the assured is indemnified under contract, it was formerly suggested that the insurer might recover from a third party more than he has paid.⁶¹ However, this position is no longer tenable since it has now been definitely decided that this is not so, and that the insurer cannot recover under the doctrine of subrogation more than it has paid.⁶² Accordingly, this puts the solution to windfall entitlement squarely in equity. Being an equitable principle, courts are, therefore, not necessarily bound to award windfall to the insurer as a matter of law or contract only. They can exercise discretion to act as they equitably see fit. This partly explains the continuing acceptance of windfall retention by the insured in some but not all cases, despite subrogation doctrine and indemnity principle.

How does that reconcile with the opposing equitable principle of *unjust enrichment*? In other words, should windfall be divorced from unjust enrichment? Secondly, what about the requirements for the insured to account to the insurer for receipt of windfall under the Act. Finally, how does that relate to the statutory requirement that the insured holds any windfall received by him in trust for the insurer? This is contained in s.32 of the MIA, the only provision in

⁵⁵ The Act has been held to codify Common Law rules applicable equally to both marine and non-marine insurance: *Joel v Law Union Insurance Company* [1908] 2 K.B. 863.

⁵⁶ For the text see Note 1 above.

⁵⁷ *Ibid.*

⁵⁸ Notably ss.1, 32, and 79-82 MIA 1906; *North of England Iron SS Insurance Association v Armstrong* (1870) LR 5 QB 244.

⁵⁹ *Goole and Hull Steam Towing Co. v Ocean Marine Insurance Co.* [1928] 1KB 589; *Yorkshire Insurance Co. Ltd. v Nisbet Shipping Co. Ltd.* [1962] 2 Q.B. 330.

⁶⁰ See Notes 1 and 63-64 above; *Castellan v Preston* at 388, 404 CA; and *cf.*, *West of England Fire Ins. Co. v Isaacs* [1896] 2QB 377 (fire policy); *Goole and Hull Steam Towing Co. v Ocean Marine Insurance Co.* [1928] 1KB 589.

⁶¹ *North of England Iron SS Insurance Association v Armstrong* (1870) LR 5 QB 244.

⁶² *Yorkshire Insurance Co. Ltd. v Nisbet Shipping Co. Ltd.* [1962] 2 Q.B. 330; *Goole and Hull Steam Towing Co. v Ocean Marine Insurance Co.* [1928] 1KB 589.

the Act which refers to windfall, albeit indirectly as an excess, providing thus:

“32 Double insurance.

(1) Where two or more policies are effected by or on behalf of the assured on the same adventure and interest or any part thereof, and the sums insured exceed the indemnity allowed by this Act, the assured is said to be over-insured by double insurance.

(2) Where the assured is over-insured by double insurance -

(a) The assured, unless the policy otherwise provides, may claim payment from the insurers in such order as he may think fit, provided that he is not entitled to receive any sum in excess of the indemnity allowed by this Act; (emphasis provided)

(b) Where the policy under which the assured claims is a valued policy, the assured must give credit as against the valuation for any sum received by him under any other policy without regard to the actual value of the subject-matter insured; (emphasis provided)

(c) Where the policy under which the assured claims is an unvalued policy he must give credit, as against the full insurable value, for any sum received by him under any other policy; (emphasis provided)

(d) Where the assured receives any sum in excess of the indemnity allowed by this Act, he is deemed to hold such sum in trust for the insurers, according to their right of contribution among themselves” [emphasis added].

Although the obligation to “hold [windfall] in trust” for the insurers is in relation to double insurance, this principle can be extended to windfall in the whole insurance law. This implies that the insurers are the beneficial owners of the windfall and correspondingly the insured must pass it to them or account to them for the windfall. The insured’s failure to refund such proceeds puts them squarely in the field of *unjust enrichment*.

5.3. Windfall and Equitable Principle of ‘Unjust Enrichment’

Having established that equity principles apply to subrogation doctrine and indemnity principle, does it follow that they should govern windfall issues, itself a product of the doctrine and principle respectively? The answer is in the affirmative. This is despite criticism of windfall conflicting with another equity

principle - unjust enrichment.⁶³ There are, however, flaws in this criticism. First, separation of windfall from unjust enrichment would be over-stretching the equitable remedy of restitution, itself a consequence of unjust enrichment, and since subrogation is a correlative of indemnity, ensuring that the insured does not make a profit on insurance. It is fundamentally aimed at protecting the insurer from fraud and unjust enrichment. On the other hand, the separation would also seek to import issues of quasi contracts and collateral contracts, central to unjust enrichment, into the insurance contracts, to which they are both alien.⁶⁴ This rationalisation of subrogation is well illustrated in what has become the *locus classicus* of subrogation in *Castellain v Preston*⁶⁵ - a property decision. The central issue in this case was whether a vendor of a house that was subsequently burned down was entitled to keep the insurance proceeds he received as well as the purchase price he also received for the same subject matter. Justice Brett laid down the much-cited rationale for subrogation as:

“The very foundation in my opinion of every rule which has been applied in insurance law is this, namely that the contract of insurance contained in a marine or fire policy is a contract of indemnity and of indemnity only and this contract means that the insured in the event of a loss against which the policy has been made shall be fully indemnified but never shall be more than fully indemnified”.⁶⁶

It is clear from the case that to allow the insured to keep both the indemnity payments and the third-party

⁶³ In reality, no doctrine of insurance law can be isolated for discussion in this context. All the principles are intrinsically linked to ensure that the insured does not make a profit or a business out of insurance. Indeed, the related concepts of under-insurance, double insurance *uberrimaefidei* and contribution are all relevant to prevent unjust enrichment of one party at the expense of another.

⁶⁴ This sentence relates to the obligation imposed on the insured to hold windfall in trust for the insured as created by s.32(2)(d) of the Marine Insurance Act 1906. The text of the section is reproduced just above paragraph 5(3) of the article. What the sentence in question refers to is that the obligation should remain to govern the insurance contract in order to avoid unjust enrichment. The only other way to achieve the same objective would be to introduce the concept of quasi(semi) contracts or collateral contract on the insured to hand over the windfall. Unfortunately the concepts of quasi contracts and collateral contracts are both alien to insurance contracts. Thus, employment of both quasi contracts and collateral contracts are although not mentioned directly are nevertheless implied

⁶⁵ *Castellain v Preston* (1883) 11 QBD 380.

⁶⁶ *Ibid.*, at p. 387. See the case of *Darrell v Tibbitts* (1880) 5 QBD 560 where similar circumstances existed.

payment would result in his unjust enrichment by virtue of double compensation for the loss.

Another often-repeated goal of subrogation is that it is necessary for the survival of the insurance industry by reimbursing the insurance company for its payments (Hasson, 1985, 421; Greenblatt, 1997) itself a reverse extension of unjust enrichment. However, *unjust enrichment* is a general common law and equity principle, which was only later imported into contract generally, and/or insurance in particular. It is a cause of action developed at common law and equity whereby a person who is unjustly enriched (either by receipt of value from the plaintiff in circumstances where they ought to return it, or by profiting from a wrong done to the plaintiff) is required to pay over the value of that enrichment to the plaintiff (Mozley Whiteley, 2001, 375). Unjust enrichment is often referred to as the law of restitution, whereby the defendant is not entitled to retain the value of the gain but must hand it over to the rightful owner. On the other hand, subrogation is often given as an example of a situation which attracts the unjust enrichment remedy. This, however, does not apply to the insurer.⁶⁷ Although the insurer must indemnify the insured for his loss, he is subsequently entitled to pursue any action that the insured has against a third party. If this were not the case, the insured would be able to claim for his loss from the insurer. He would also be entitled to claim from the wrongdoer and, in such a situation, he could be said to be doubly compensated for his injury or unjustly enriched at the insurer's expense. Despite this clear position, why is the insured entitled to windfall retention (albeit in only in some cases)? This is exactly the unforeseen and unintended consequence of subrogation.

If the insurer could not exercise this right it would undoubtedly mean that they could not continue to carry on business. Therefore, the doctrine of subrogation recognises that upon payment under the terms of the policy the insurer is entitled to protect himself from unjust enrichment by taking action against the third party to recoup the amount he has had to pay out. However, courts have tended to bypass this unjust enrichment rationale for subrogation in certain situations, particularly where the insured has received windfall. These situations where the insured is entitled to retain the benefit of such monies to the disadvantage of the insurer is cited as a clear example of the insured becoming unjustly enriched at the expense of the

⁶⁷ Insured's retention of windfall cannot be an unjust enrichment; see *Barclays Bank PLC v Hammersmith and Fulham LBC* (1991) *The Times* 27 Nov; for the principle of restitution see *Boissevain v Weil* [1950] AC 327.

insurer.⁶⁸ Nevertheless, it is questionable whether the insured's retention of windfall necessarily leads to unjust enrichment. Not in the real sense of that word. First, unjust enrichment is the retention of a benefit conferred by another without offering compensation, in circumstances where compensation is reasonably expected (Curzon, 1993, 395).⁶⁹ On the contrary, the insured unquestionably pays a premium and, in any case, windfall comes not from the insurer but a third party.⁷⁰ Second, windfall is alternatively a benefit obtained from another, not intended as a gift and not legally justifiable, for which the beneficiary must make restitution or recompense. In these circumstances, the insured does not have to make any restitution or recompense. In the absence of any solution, an inconvenient truth persists; windfall is being allowed to co-exist side-by-side with indemnity, subrogation and unjust enrichment.⁷¹ If not a contravention of unjust enrichment, does it contravene the alternative equitable doctrine of injurious behaviour?

5.4. Windfall Waiver and the Contractual Principle of 'Injurious Behaviour'

Another rationale for rebuff of windfall in favour of strict subrogation is that it deters injurious behaviour by placing the primary burden of compensation on the wrongdoer.⁷² Is there any merit in this proposition in insurance and contract law? Is it a legal or equitable principle? The answer to these questions are in the negative. This is because responsibility for injurious behaviour should relate to the wrongdoer, not the insured. The most frequently cited English law manifestation of this justification for subrogation was put by Viscount Simonds in *Lister v Romford Ice and Cold Storage*,⁷³ that,

⁶⁸ See under Part II Section 5(3) ahead for a discussion of this limitation on an insurer's subrogation rights.

⁶⁹ *Barclays Bank plc v Hammersmith and Fulham LBC* (1991) *The Times* 27 Nov; *Boisservain v Weil* [1950] AC327 (equitable restitution).

⁷⁰ For American decisions see *Tulaip Shores, Inc. v Mortland*, 9 Wash. App. 271, 511 P.2d 1402, 1404; *L&A Drywall, Inc. v Whitmore Construction Co., Inc.*, Utah, 608 P.2d 626, 630; *Everhart v Miles*, 47 Mid. App. 131, 136,136, 422 A.2d 28.

⁷¹ For a proper use of the doctrine of unjust enrichment in the US see *Fair Wind v Dempster*, 2015 AMC 585 (use of another's trading rights) and *Cal Drive v Schmidt* 2015 AMC 959 (WDLA).

⁷² *Cousins & Co. Ltd. v D. & C. Carriers Ltd.* [1971] Q.B. 230, 243 (Davies L.J.).

⁷³ *Lister v Romford Ice and Cold Storage* [1957] AC 555.

"...to grant the servant immunity from such an action would tend to create a feeling of irresponsibility in a class of persons from whom, perhaps more than any other, constant vigilance is owed to the community".⁷⁴

The underlying basis for this justification appears to be that if the insurer could not exercise these subrogation rights, it would give the impression to the world at large that if a person caused injury to another individual who is insured, then they would be immune from liability as the insurer would be ultimately responsible for the injured party's loss. This rationale appears to highlight the moral and class-based public policy justifications that necessitate the doctrine. Hence one of this article's theses is that windfall decisions are sometimes based on policy rather than purely law. However, the above decision has been much criticised⁷⁵ and, in particular, the criticisms highlight the usefulness of the doctrine, which enables the insurer to pursue an action against a third party who is also insured. American law, however, takes a different view from the English and other common law jurisdictions on waivers which insurers can technically commit. For instance, in the recent landmark case of *Deepwater Horizon*,⁷⁶ the 5th Circuit Court in Louisiana decided that when an insurer breaches the policy by wrongfully denying coverage based on an erroneous interpretation of the policy, the insurer has waived its rights to subrogation and therefore windfall.

It is perhaps in response to these criticisms that further limitations and modifications on the doctrine such as the "knock for knock agreements"⁷⁷ and the "gentleman's agreement" (Birds, 1978, 201) were developed. In the former, insurers may voluntarily waive their rights to subrogation against an insured third party, instead preferring to enter into an arrangement with the third party's insurer. According to the "gentleman's agreement", insurers have voluntarily agreed to resist taking subrogation actions against the employee of an insured employer except in specified situations. The effect of both agreements can be said to have the salutary consequences of eliminating wasteful and costly subrogation actions. However, despite the weight of the above arguments in favour of the doctrine, one must address the question as to why it has been

⁷⁴ *Ibid.*, at 579.

⁷⁵ Note the criticisms of Hasson of this approach: Hasson, 1985, 423-424.

⁷⁶ *The Deepwater Horizon*, 2015 AMC 2969 (5 Cir - also involving double insurance).

⁷⁷ See *Hobbs v Marlowe* [1977] 2 All ER 241; see also *Morley v Moore* [1906] 2KB, 359 at 361 per Sir Boyd Merriman P; Birds, 1978, 201.

necessary to limit and/or modify⁷⁸ its application. It has also been suggested that windfall should constitute an American-type waiver to subrogation. However, this suggestion ignores that waiver by the insurer does not apply to, or affect, windfall. It is these limitations and modifications that will be addressed next in the context of windfall. Does the existence of such modifications and limitations outweigh the arguments in favour of the doctrine's continued use and render it obsolete in the context of insurance? Surely the insurer will only waive when proceeding would diminish their commercial interest (and certainly where windfall prospects are not involved). These considerations lead to further questions of whether or not windfall should be added as a limitation to indemnity and subrogation. Besides, are these rights limited to only the subject matter of the case?

5.5. Effect of Implied and Express Assignments on Windfall

Re Miller Gibb,⁷⁹ in Part I of this article, demonstrated that entitlement to windfall may be affected by express assignment of the ECGD contract and its proceeds. The precedent arguably extends to all insurance contracts, including implied assignments. It is recognised that subrogation does not confer a right of action on the insurer. As a general rule, the rights to which the insurer are subrogated to must be enforced in the name of the insured, as well as the fact that subrogation does not entitle them to enforce actions in their own name. Indeed, in *London Assurance v Sainsbury*,⁸⁰ Lord Mansfield opined that, "I take it as a maxim that as against the person sued the action cannot be transferred".⁸¹ Hardy (Hardy, 1986, 475), however, put forward an exception to this established principle, in which the insurer can sue in his own name. For example, the insured can make a formal assignment to the insurers of their rights in respect of the subject matter. This operates as a limitation or an alternative to traditional subrogation. The operation of such an exception is illustrated by *Compania Colombiana de Seguros v Pacific Stream Navigation Company*.⁸² In

⁷⁸ Although the article treats limitations and modifications of the doctrines separately, there is not much difference between them. The separation of the two in this respect is only for convenience as the effects of either is probably the same.

⁷⁹ *Re Miller, Gibb & Co. Ltd.* [1957] 2 All ER 266; [1957] 1 WLR 703; discussed under Notes 122-127 in Part I).

⁸⁰ *London Assurance v Sainsbury* (1783) 3 Doug KB 245 at 253.

⁸¹ *Ibid.*

⁸² *Compania Colombiana de Seguros v Pacific Stream Navigation Company* [1965] 1 Q.B. 101.

this case, Justice Roskill held that once the insured had assigned their rights in the subject matter to their insurers, and satisfied the requirements of s.136⁸³ of the *Law of Property Act 1925*,⁸⁴ the insurer was entitled to bring an action in their own name.

Nevertheless, Birds is of the view that such assignments are rare and that insurers prefer to sue in the name of the insured because of the subsequent lack of publicity (Black, 2007, 312).⁸⁵ There is also an advantage to such an approach: the principle as established in *Yorkshire Insurance*⁸⁶ will not apply as the action is entirely the insurers', because the insured has forfeited all their interest in it.⁸⁷ The situation or alteration of the traditional subrogation referred to in the scenario here is the case where the insured has expressly assigned his rights and interests in the subject matter. In such cases, the insured ceases to be part of the picture and will have divested himself totally of any rights he may have in the subject matter. This must be contrasted to the operation of the doctrine of subrogation in its unmodified form. In such a situation, following full indemnification of the insured under the policy, there will be an implied assignment to the insurer of such rights. These enable the insurer to recoup the amount he has paid out to the insured. The insurer usually achieves this by "stepping into the shoes of the insured" and in his name pursuing his right and remedies against a third party.⁸⁸ Unlike the express assignment, as was the situation in *Compania Colombiana de Seguros*, the insured retains an interest

⁸³ S.136 provides: "Any absolute assignment by writing under the hand of the assignor (not purporting to be by way of charge only) of any debt or other legal thing in action, of which express notice in writing has been given to the debtor, trustee or other person from whom the assignor would have been entitled to claim such debt or tiling in action, is effectual in law (subject to equities having priority over the right of the assignee) to pass and transfer from the date of such notice:

(a) the legal right to such debt or tiling in action;

(b) all legal and other remedies for the same; and

(c) the power to give a good discharge for the same without concurrence of the assignor". See www.statutelaw.gov.uk for the full version of the relevant Act.

⁸⁴ As noted, *Ibid.*, this section deals largely with giving notice of the assignment to the defendant.

⁸⁵ The only publication to devote a whole chapter to windfall-related coverage.

⁸⁶ *Infra* under Section III(f).

⁸⁷ For a critique of cases where there is both an assignment and surplus see *Re Miller, Gibb and Co.*

⁸⁸ Cf. the American decision of *Hyywiack Lim* 2008 AMC 2669 decided under Louisiana legislation which provides for lots of freedom to both parties. The case decided that the insured's contractual assignment of rights to the insurer is valid regardless of whether or not the insurer is subrogated to it.

in the case as it is taken in his name and has the added advantage of retaining any benefits such as windfall that may be received from a third party.⁸⁹

6. REASSESSMENT OF AND SUGGESTIONS FOR WINDFALL SOLUTIONS

6.1. Reassessment in Common Law Jurisdictions

With regard to windfall, full indemnity and full compensation remain areas of criticism that need addressing as issues of priority between the insured and insurer in relation to *third party monies*. This is especially so in Anglo-Irish situations, where the amount received under the policy has not fully compensated the insured for his loss. The position is no different in other common law countries. Irish jurisdiction⁹⁰ appears to have accepted that the insured is entitled to be *fully compensated* as opposed to being *merely indemnified* for any uninsured loss before the insurer's subrogation rights arise. This is in line with ss.79-81 of the MIA which was transplanted to Ireland.⁹¹ The recent English *Napier* case is also followed in Ireland. A major source of criticism, however, lies in the approach of the House of Lords, which was at odds with both the Irish jurisdiction and other common law jurisdictions' approaches to the issue of priorities in subrogation actions.

The US position seems ambivalent.⁹² Greenblatt (Greenblatt, 1997, 1338) remarks that the question of priorities has generated considerable confusion in the American courts and that the only unanimity in the

⁸⁹ Cf. US case of *SDNY Sampo v Norfolk* 2014 AMC 579 which held at an underwriter, acting an assignee of VOCC's claim, may recover the claim from the performing railroad according to the terms of the railroad contract with the VOCC.

⁹⁰ Of course, it should be emphasised that this Irish case was decided well before the UK *Napier* case. As to whether the court would reach the same conclusion in light of recent UK developments is a matter of speculation. This paper, however, proceeds on the basis that Irish Law on this issue stands as enunciated in *Driscoll v Driscoll* [1918] 1 I.R. 152; see also IBA Report, *supra*, pp.67-71.

⁹¹ See also *In Re 19th Limited* [1989] ILRM 652 in which Lynch, J. noted that the right of subrogation arose from the equitable doctrine seeking to do justice between the parties; Law Reform Commission Consumer Insurance Contracts (LRC 113-2015) at p.141 exceptions and limitations to subrogation; Art. 10.101(2) *Principles of European Insurance Contract Law* on waivers.

⁹² See IBA Report, *supra*, at 137-156 especially the four criteria at p.137. Since insurance is not a federal matter, the Report covers California (137-139), Connecticut (140-142), Illinois (141-146) and Massachusetts (151-156).

courts is a categorical rejection of the insurer's claim first as a default rule. Thus, in *Rimes v State Farm Mutual Automobile Insurance Co.*,⁹³ the Wisconsin Supreme Court⁹⁴ held that, under both legal and conventional subrogation, the insured must be fully compensated before the insurer can share in the recovery for two reasons. Firstly, the insured cannot be accused of being unjustly enriched until he has been fully compensated for his actual as opposed to his insured loss (as the purpose of subrogation is to prevent double recovery by the insured). A second reason for giving the insured priority is based on the idea that, "Where either the insurer or insured must to some extent go unpaid the loss should be borne by the insurer for that is a risk that the insured has paid it to assume" (Greenblatt, 1997, 1355). It will be recalled that the same position was adopted by the US Federal Court in *Livingstone*.⁹⁵ If the authority's claims were not limited to where the insured is under-indemnified, this would be tantamount to their license to profit from windfall.

This line of reasoning is also followed in Canada, where the courts confirm the proposition that the exercise of the insurer's subrogation rights do not usually affect the insured's recovery of a full indemnity.⁹⁶ It will be recalled that the decision was based on the Canadian subrogation legislation,⁹⁷ itself

⁹³ *Rimes v State Farm Mutual Automobile Insurance Co.* 106 Wis 2d 263, 316 NW2d 348, 353 (1982).

⁹⁴ Unlike the other common law jurisdictions, the US does not have Federal insurance or marine insurance legislation. Instead, insurance matters are left to state jurisdictions. Other than that, the same Common Law subrogation principles apply and English and other Common Law insurance decisions are cited, sometimes with persuasion.

⁹⁵ *Livingstone* 130 F 746 (2d Cir) (also that subrogation, as opposed to abandonment, can never entitle the insurer to recover more than he has paid the assured); see also *Federal Deposit Insurance Corp. v Wilhoit* 297 Ky. 339, 180 S.W.2d 72 (1943); *Urban Industries, Inc. v Thevis* No.C-75-0342 L (A) (W.D.Ky. July 13, 1978); *Carolina Casualty Insurance Co. v Local 612, International Brotherhood of Teamsters* 136 F. Supp. 941 (N.D.Ala. 1956); *The St Johns* 101 Fed Rep 469 (the insurer's right in equity can never extend beyond recoupment or indemnity for the actual payments to the assured). <http://www.exim.gov/>

⁹⁶ IBA Report pp.24-29.

⁹⁷ S.81 of the *Marine Insurance Act 1993*. Although the section reproduces s.79 (1) of the MIA 1906, the former is better presented and a lot clearer: for instance, s.81(1) relates to subrogation in total loss while s.81 (2) to partial loss. Other than that, the Canadian Act is in many respects a departure from the MIA 1906, although some changes appear to be purely linguistic, do not affect subrogation and are not aimed at the substance. However, reasonable research has not revealed any windfall and subrogation decisions under the equivalent Export Development Canadian (EDC) <http://www.edc.ca/> established under the *Export Credits Insurance Act 1974* (as amended), although it

based on its origin, s.79 of the MIA 1906. However, the Canadian Supreme Court's decision of *Ledingham v Ontario Hospital Services Commission*,⁹⁸ based on the Canadian legislation, is a departure from the English ones made from the equivalent to s.79 (1) of the MIA 1906.⁹⁹ Here the question was whether the Commission was entitled to share *pro rata* in the third party funds or whether the plaintiff was entitled to recover in full to the exclusion of the Commission. The Supreme Court held that, under ordinary subrogation principles, the plaintiff was entitled to exclusive recovery. The court cited with approval the description and purpose of subrogation advanced in *National Fire Insurance Co v McLaren*,¹⁰⁰ to the effect that:

"The primary consideration is to see that the insured gets full compensation for the property destroyed and the expenses incurred in making good his loss. The next thing is to see that he holds any surplus for the benefit of the insurance company".¹⁰¹

This would appear to be a more logical conclusion than that reached by the English court in *Napier v Hunter*.¹⁰² Since the primary function of the doctrine of subrogation is to prevent the insured becoming unjustly enriched at the insurer's expense, there is certainly room for the argument that an insured cannot be accused of being unjustly enriched until he has been fully compensated for his loss, thus denying subrogation to be exercised until this can be said to have occurred for the insured's benefit.

6.2. Variation of Subrogation and Windfall in Common Law Jurisdictions

Unlike other common law countries, Australia has made efforts to vary subrogation provisions¹⁰³ from

would safe to assume English ECGD cases be persuasive as they are in Anglo-American and other Common Law countries.

⁹⁸ *Ledingham v Ontario Hospital Services Commission* (1974) 46 DLR (3d) 699.

⁹⁹ S.81 *Canadian Marine Insurance Act 1993*.

¹⁰⁰ See *National Fire Insurance Co. v McLaren* (1886) 12 OR 682, 687.

¹⁰¹ For more Canadian decisions and further analysis of the Canadian law on windfalls see 'Subrogation: basic principles, emerging trends and practical considerations' prepared by J.M. Moshonas, J.A. Vamplew and S.R. Lerner, February 2006 <http://www.whitelawtwining.com/documents/article-pdfs/Subrogation.pdf> at pp.5-7 (Subrogation Agreements) (accessed on 28/02/2018); see also generally IBA Report, *supra*, at pp.26-29.

¹⁰² *Napier v Hunter* [1993] 2 W.L.R. 42.

¹⁰³ IBA Report, *supra*, pp.8-11 at p.8 on the insurer's rights of recovery after indemnity; Part VIII of the *Insurance Contracts*

those inherited from English law, although with little effect on windfall. This was achieved by ss.64-68 of *Insurance Contract Act 1984*'s amendments to the MIA 1906's equivalent provision in s.79 of the original *Marine Insurance Act 1909*. The first amendment forbids the insurer from suing a co-insurer in subrogation, and has now had judicial interpretation in *Woodside Petroleum Development Pty Ltd v H&R-E&W Pty Ltd*.¹⁰⁴ The second item was addressed in *The Iceberg*,¹⁰⁵ which confirmed dispensing with the requirements for disclosure, for subrogation purposes, by inland carriers. However, these insubstantial amendments to subrogation did not affect windfall. Otherwise, the remaining Australian situation is almost similar to those discussed above, as is its subrogation provision.¹⁰⁶ Apart from the amendment,¹⁰⁷ the Australian subrogation provision is still based on the received law embodied in s.79 (1) of the MIA 1906. Of the remaining leading common law jurisdictions, Hong Kong¹⁰⁸ has probably remained the most faithful to the received s.79(1) of the MIA 1906.

Act 1984, ss.65 and 67; *Johnson v Endeavour Energy* [2015] NSWSC 1117 (New South Wales Supreme Court decision).

¹⁰⁴ *Woodside Petroleum Development Pty Ltd. v H&R-E&W Pty Ltd.* [1997] 10 ANZ Ins. Cas. para 61-395 (Anderson J); [1999] war 380.

¹⁰⁵ *Helicopter Resources Pty Ltd. v Sun Alliance Australia Ltd. (The Iceberg)* 26 March 1991; ss.65-68 of the *Australian Insurance Act. 1984*. Reasonable research has not revealed any reports on any windfall or subrogation cases of the Australian Export Credit Agency - the Export Finance and Insurance Corporation (EFIC) <http://www.efic.gov.au/>; established under the *Export Finance and Insurance Corporation Act 1991* (148/1991) as amended by the *Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Act 2015* <https://www.legislation.gov.au/Series/C2004A04223>. It would be a reasonable presumption that Anglo-American decisions would be persuasive.

¹⁰⁶ S.85 of the *Australian Marine Insurance Act 1909* is based on section s.79 MIA 1906 but with several additional sections at the beginning.

¹⁰⁷ *Insurance Contracts Act 1984*, especially sections 65-68.

¹⁰⁸ IBA Report, *supra*, pp.53-58; The Hong Kong *Marine Insurance Ordinance* (Cap. 329) is probably the more faithfully pp. ss.79-81 of the English MIA 1906, except for an additional section 92 on gambling policies, in retaining identical s.79 of the MIA 1906 (subrogation); see *Amoi Electronics Co. Ltd. v Kin Cheung Transportation (Hong Kong) Co. Ltd.* [2010] WL 7467(DC), [2010] HKE 235 and s.25 of the *Employee Compensation Ordinance* (Cap. 282). However, reasonable research has not revealed windfall and subrogation decisions under the Hong Kong Export Insurance Corporation <http://www.hkcec.com/en/index.aspx> established under the Hong Kong Export Credit Insurance Corporation Ordinance as amended (HECIC) http://www.hkcec.com/en/about_ordinance.aspx but ECGD cases above would be persuasive if not binding.

A similar position loyal to s.79 of the MIA 1906 was adopted by New Zealand¹⁰⁹ and Singapore.¹¹⁰ However, South Africa has rather a unique common law jurisdiction, based on received dual legal systems: civil (Dutch-Roman) and common law.¹¹¹ Thus, in *Rand Mutual Assurance Co Ltd v Road Accident Fund*,¹¹² only after discussing South African legal history¹¹³ did Justice Harns conclude that the insurer replaces the assured in subrogation, which entitles the insurer to claim the loss from the wrongdoer. Referring to windfall, he countered that the assured may not be enriched at the expense of the insurer by receiving both the insurance indemnity and damages from the wrongdoer.¹¹⁴ However, this pro-insurer position was contradicted in *Somersall v Friedman*,¹¹⁵ in that if there is no danger of the assured being overcompensated, there are no reasons to invoke subrogation. The phrase “over compensated” in this case probably refers to the insured’s windfall gain.¹¹⁶ Other major common

¹⁰⁹ IBA Report, pp.8-11 at p.9; ss.268-270 *Property Law Act 2007* and Appeals Court case of *Holler & Rouse v Osake & Another* [2016] NZCA 130. Like the *Hong Kong Ordinance*, the *New Zealand Marine Insurance Act 1908* is mostly similar to the MIA 1906, retaining the same numbering of s.79 on subrogation. Other than that, there are some substantive changes, but these do not affect subrogation and therefore windfall. In addition, the grammar is substantially modified, but without alteration on subrogation; see also the case in Note 144 *op. cit.* for New Zealand decision on an ECGD equivalent. <http://www.nzeco.govt.nz/>

¹¹⁰ IBA Report, pp.108-111; Singapore has adopted the same principles as English subrogation law since the English MIA 1906 applies almost verbatim. However, there is no reported case law, the closest being the Malaysian Court of Appeal decision in *Kementerian Pertahanan Malaysia and Another v Malaysia International Shipping Corp Bhd and Others* [2007] 5MLJ 393 concerning general subrogation principles. Reasonable research has not revealed windfall and subrogation decisions under the Singapore Trade Credit Insurance Scheme (TCIS), but ECGD cases would be persuasive.

¹¹¹ IBA Report, supra, pp.112-14.

¹¹² *Rand Mutual Assurance Co. Ltd. v Road Accident Fund* [2008] ZASCA 114; 2008 (6) SA 511.

¹¹³ *Ackerman v Loubster* [1918] OPD 31 (Receipt of English law into South Africa); *Commercial Union Insurance Co. of SA Ltd. v Lotter* [1999 (2) SA 147 (SCA) (subrogation).

¹¹⁴ *Ibid.*, at 519; see also the South African decision in *Stearns v Village Main Reef Gold Mining Co.* (1905) 10 Com Cas 89 (voluntary gifts).

¹¹⁵ *Somersall v Friedman* [2002] (3) SCR 109.

¹¹⁶ These are decisions based on the equivalent of the received s.79 MIA 1906 as there are no equivalent cases on the Export Credit Insurance Corporation of South African (ECIC) <http://www.ecic.co.za/> established under the South African *Export Credit and Investment Act 2002*, https://www.thedti.gov.za/business_regulation/acts/export_credit_act.pdf

law jurisdictions following the MIA 1906 and ECGD approach on windfall in subrogation include India,¹¹⁷ Malaysia¹¹⁸ and Nigeria.¹¹⁹

6.3. Effect of Windfall on the Foundation of Subrogation and Indemnity

Before concluding, attention must be drawn to a number of aspects of this analysis in more detail with justification of, and with a view to reform, subrogation. It is generally accepted that there is some role for subrogation; however, the myriad of limitations, exceptions and modifications that exist casts doubt as to its justification. Perhaps the insured’s retention or rights in share of windfall should be formally added to those justifications. These issues aside, among the many critics of subrogation, Lowry and Rawlings (Lowry, Rawlings, 2011, 621) are of the view first, that subrogation is sometimes a means of both reducing losses, and, therefore, premiums, and determining wrongdoing by fixing liability on the wrongdoer. However, in the same breath they see the difficulty of these arguments and argue that insurers are unlikely to use their rights of subrogation unless they are able to enforce any judgment awarded. This means that such rights are likely to be exercised only where the wrongdoer is insured. On this assumption, they conclude that subrogation becomes merely a way of

¹¹⁷ IBA Report, supra, pp.60-63; s.79 of the *Marine Insurance Act 1963*; Indian authorities are not discussed but operating under the *Export Credit Guarantee Corporation of India Ltd.* (ECGC Ltd.) <http://www.ecgcindia.in/en/pages/ecgcaphome.aspx> established under the *Export-Import Bank of India Act 1981* (No.28/1981) <http://www.eximbankindia.in/sites/default/files/exim-bank-act.pdf>. There are numerous other Indian authorities dealing with subrogation of which the *Economic Transport Organisation v Charan Spinning Mills (P) Ltd. and Another* (2010 Civil Appeal No.5611 of 1999) decision is the most prominent. The case was decided in 2010 in the Supreme Court, India’s highest court. In the case, Justice Raveendran (Justice Jain, Justice Sathasivam and Justice Panch concurring), explained that subrogation is inherent, incidental and collateral to a contract of indemnity, which occurs automatically, when the insurer settles the claim under the policy, by reimbursing the entire loss suffered by the insured. The English case of *Napier v Hunter* [1993] 2 W.L.R 42 was cited and followed evidence of the convergence of the Common Law jurisdiction on this point.

¹¹⁸ Export-Import Bank of Malaysia (Eximbank Berd) <http://www.exim.com.my/index.php/en/> for legal position on subrogation and windfall see s.80 80 *Marine Insurance Act, 1961*, based on the UK’s MIA 1906; IBA Report, pp.82-85.

¹¹⁹ Nigerian Export-Import Bank (Nexim); see <http://www.neximbank.com.ng/> established by the *Nigerian Export-Import Bank Act 1991* (No.38/1991) <http://lawnigeria.com/LawsoftheFederation/NIGERIAN-EXPORT-IMPORT-BANK-ACT.html>

shifting losses from one insurer to another and does not fix liability on the wrongdoer. Windfall is probably coincidental to all this debate.

Based on the above argument, Lowry and Rawlings¹²⁰ have a second criticism that insurers who recoup their losses today will be paying out tomorrow to cover the liabilities of wrongdoers whom they insure. Furthermore, doing so would presumably nullify any reduction in premiums that might be attributable to subrogation. Lowry and Rawlings are also curious that, while subrogation is meant to prevent the insured from profiting, the same principle does not seem to be applied to insurers who, if they recoup any money paid the insured, will have lost nothing and will instead have gained premiums. In other words, they call for an equitable solution to both parties. As noted, there seem to be tentative steps in this direction under other common law jurisdictions, in the hope of applying the indemnity and consequently the subrogation principles to limited aspects of personal insurances. This justification has no bearing on windfall. All these miss the point, which is that there is the need for a rationale in windfall just as there is one for subrogation (Hemsworth, 1998). Perhaps the solution lies elsewhere, as noted below.

6.4. Whether 'Co-sharing' as 'Co-insurers' is Part Solution to Windfall Problems

In view of the impasse, this article proffers a few solutions for a way forward that would satisfy both interests and also preserve indemnity and subrogation (Brownie, 1991; Mead, 1998).¹²¹ The preferred solution would be legislative intervention by way of reform or amendment of s.79 of the MIA 1906. The second suggestion would be maintaining judicial consistency and clarity in windfall decisions. Third, courts should not only establish clear guidelines, but should also indicate when decisions are based on legal or policy considerations. Fourth, parties should agree in advance on how to proceed in the event of windfall along the line of the ECGD practice. Matters should be made clear, as in *Standard Clause 17* of the old ECGD Policy. Although the new equivalent Article 9 is not explicit on windfall co-sharing,¹²² it is nevertheless implied in

¹²⁰ *Ibid.*

¹²¹ Mead discussing Australian decisions.

¹²² "SUBROGATION

9.1 Upon payment of any amount due to the Insured under this Policy, ECGD is subrogated to all rights, remedies, claims, guarantees and securities available to the Insured to mitigate the loss sustained by the Insured, including any rights against a guarantor or a surety, whether or not the exercise of such rights might, in addition, involve claims, rights or remedies concerning

Article 11.¹²³ In the absence of legislative inaction and judicial ambivalence, it is argued that allowing for common sharing of windfall might be a temporary, if not viable, solution.

Under this scheme, the parties would be treated as *co-insurers*¹²⁴ for the purposes of windfall, as participants in a *common adventure*. This would be more equitable to both parties and sustain the principles of indemnity and consequently the doctrine of subrogation. In other words, windfall recovery from the wrongdoer should be distributed on the principles of subrogation with equity and justice, and the equitable principles of subrogation should not be changed by valuations in the policies. Among other things, this would eliminate the criticism of unjust enrichment. This argument has gained grounds in American rather than English¹²⁵ or other common law jurisdictions. This was raised in *Aetna Insurance Co. v United Fruit Co.*¹²⁶ in response to *Yorkshire Insurance*. Counsel for the insured argued successfully that since the risks retained by the owners was in the same amount as that assumed by the

obligations other than those whose non-performance has created a loss under this Policy. These rights of subrogation shall be in addition and without prejudice to all rights and benefits to which ECGD is entitled under the general law of subrogation.

9.2 At all times after payment of any amount due to the Insured under this Policy, the Insured:

9.2.1 shall exercise or enforce or refrain from exercising or enforcing all such rights, remedies, claims, guarantees and securities solely in accordance with the directions of ECGD and take all steps for this purpose as ECGD may require;

9.2.2 will on request assign and transfer all such rights, remedies, guarantees and securities to ECGD, and execute and deliver to ECGD all such documents as ECGD may require for this purpose; and

9.2.3 will authorise and permit ECGD, in the name of the Insured, to settle or compromise any claim which the Insured may have against the Purchaser, the Surety or any other party in connection with any Insured Contract or institute and conduct legal or arbitral proceedings in respect of any such claim".

¹²³ "11 ALLOCATION OF RECOVERIES

11.1 If at any time the Insured receives a Recovery, it shall hold the Recovery on trust for ECGD and, as soon as practicable after receipt, notify ECGD of that receipt and pay that Recovery to ECGD.

11.2 ECGD shall retain the Specified Percentage of each Recovery received by it and shall pay the remainder to the Insured".

¹²⁴ A co-insurer can be either an insurer participating in a co-insurance with other insurers or the insured himself when he bears a part of a risk either as self-insured or by way of excess, deductible or other means (e.g., under-insurance leading to the application of average).

¹²⁵ That accounts for why, of the myriads of English law authors, only Birds, 2007, Chapter 15 and Lowry and Rawlings, Chapter 11) give the subject any meaningful treatments.

¹²⁶ Insured counsel's arguments in *Aetna Ins. Co. v United Fruit Co.* 1938 AMC 710.

insurers, they were entitled to an equal portion of the recovery from the wrongdoers causing the collision.¹²⁷ A similar position is adopted in cargo insurance. For instance, the New Jersey Supreme Court in *Standard Oil New Jersey v Universal Insurance Co.*¹²⁸ held that the assured should be considered a *co-insurer* in respect of the windfall (*excess*) over the actual cargo insured value. The insured is therefore entitled to share rateably with the underwriters in windfall recoveries obtained from third party wrongdoers. Canadian decisions are also sympathetic to the concept,¹²⁹ but not the English courts.¹³⁰

6.5. Windfall - Policy Considerations or Practical Realities?

Most windfall authorities cited in this paper have been pro-insured. That leads to the alternative view to windfall decisions, where windfall retention by the insured is a matter of practical reality. Even with the revised ECGD rules of 90%-10%, the insured still retains 10% of the windfall. There are a number of reasons for this position. First, despite their legal rights to subrogation under s.79 of the MIA 1906, few insurers actually claim directly from the wrongdoers or do so in person, choosing instead to let the insured do so and then reimburse them. It is normally the insured's contractual obligations to do so. Incidents cited in this analysis suggest it has sometimes worked to the insurer's detriment. That the insurers do not bother to do so means windfall anomalies do not rank that high in their priorities. Secondly, this article has demonstrated that retention of windfall by the insured seems both reality and practice. At least the share of it. It would explain why the common law judiciary, jurists and insurers themselves have taken such a blasé approach to the subject.

Thirdly, windfall does not seem to be a legislative pressing need. Otherwise something could have been done by now. There have been more pressing

¹²⁷ *Ibid.* However, reasonable search has not revealed any windfall or subrogation decisions on the US Export Credit Agency - the Export-Import Bank (Eximbank) <http://www.exim.gov/> established under the *Export-Import Act 1945* <http://www.state.gov/t/isn/exportimport/>

¹²⁸ *Standard Oil New Jersey v Universal Insurance Co.* 1933 AMC 675, 1644.

¹²⁹ See the Supreme Court decision in *Commonwealth Construction Co. Ltd. v Imperial Oil Ltd.* (1977) 69 DLR 3d 558.

¹³⁰ E.g., *Petrofina Ltd. v Magnaload Ltd.* [1984] 1QB 127; *Stone Vickers Ltd. v Appledore Ferguson Shipbuilders Ltd.* [191] 2 Lloyds Rep 288; *Co-operative Retail Services Ltd. v Taylor Young Partners Ltd.* [2000] 2 All ER 865; see also [1983] JBL 497; *Birds*, 2007, 326-329.

insurance issues, such as duty to disclose, which deserve attention but which have not received the consideration they deserve. Fourth, in terms of the equitable judicial approach to the subject, judges seem keen to balance the interests of the parties rather than uphold subrogation, indemnity and insurance itself. The question seems to be: between the two (insurer and insured), who needs the money more? The judiciary, at least, seem to be of the view that insurers are not worse off by losing the windfall or their shares thereof. Given the retention of windfall, insurers will probably either add it to company profits or pass it on to shareholders or employees as bonuses.

Fifth, as to the supposed threat to insurance, maybe the pool system has taken care of the matter - so no need to worry about insurers. Would it be different if it went into the pool to reduce premiums or our taxes in the case of the ECGD? Whereas to the individuals or small businesses insured, it can mean a lot of difference. Besides, insurers seem to have a poor public image as greedy 'wealthy' money-grabbers. On the contrary, there seems to be a fairly positive and sympathetic attitude to the 'poor' insured. Sixth, as for policy, perhaps the courts should come clean and admit policy considerations do play a part in their windfall decisions. At least they should be consistent and should give reasons, rather than simply saying they are unaware of instances where the insurer has kept any windfall. Seventh, and finally, accepting now that it is a reality, maybe it should be included in the exceptions to subrogation and indemnity. Contractually, it could be avoided through assignment, express provisions, better subrogation clauses, etc.

7. OVERALL CONCLUDING REMARKS

Contrary to popular assumptions, windfall in subrogation is not synonymous with excess, profit nor surplus. The concept, now prevalent in export credit insurance, developed from marine and property insurance. Despite many years of experience, common law has failed to deal satisfactorily with the windfall issue. One of the problems being that windfall is only implied, but not expressly contained, in s.79 (1) of the MIA 1906. Where the insured's windfall retention has been permitted, it remains unclear whether they were treated as exceptions, limitations or modifications of indemnity and subrogation, or whether they were governed by subrogation, property or equitable rights. Furthermore, unjust enrichment is inapplicable in windfall due to the insured's lack of misconduct; otherwise, he/she would fall foul of the

anti-gaming legislation.¹³¹ To reiterate, with credit to the insurance authorities considered herein, windfalls are not products of fraudulent deception or insureds' active participation; rather they are freak functions of currency devaluations and other external financial factors within international trade relations. Although the ECGD insurance contract loophole is now closed by an express clause allowing for a share in the windfall in the ratio of 90/10, that still allows the insured to retain 10% of the windfall. Despite *Yorkshire Insurance* and the ECGD cases remaining good law, the decisions were heavily criticised. Since they are independent of the contract, voluntary third-party gifts intended for the insured's own use should not constitute windfalls.

That said, and to reiterate, windfall is probably of no practical consequence to insurance law and practice, otherwise either the judiciary, the legislature or the Law Commission would have acted. That probably explains the low-level take-up of the windfall debate. Furthermore, since the peak in the 1950s in the US, and 1960s and 1970s in England, case law on the subject seems to have evened out. It would, however, be better if the situation were clarified by a legislative amendment along the lines of the English *Insurance (Gambling Policies) Act 1909* and the Australian *Insurance Act 1984*. The latest English *Insurance Act 2015* never addressed it. Whereas courts seek to uphold the principle of indemnity and doctrine of subrogation, they seem unwilling to intervene in insureds' windfall gains where the insurer is not out of pocket. Is the judicial ambivalence to windfall dictated by the need to balance both parties' interests? Does it explain why courts have been unconcerned with whether windfalls are:

- (a) incompatible with subrogation and indemnity;
- (b) contractual or equitable;
- (c) arise from express or implied terms; or
- (d) displaceable by express provisions or assignments?

All these options have been either applied or left open. Neither have the courts given any policy reasons for their decisions. What can be gathered, however, is that windfall does not impinge on the insurer's undertaking to indemnify. It might make sense and be helpful if courts came clean and confirmed that, unless otherwise provided, so long as the insurer is not out of pocket, the insured might as well retain the windfall. It has been suggested that courts should adopt a flexible approach to the issue. Additionally, or alternatively, such parties should instead implement windfall sharing as co-insurers or co-participants in a venture. Unless

¹³¹ E.g., the *Marine Insurance (Gambling Policies) Act 1909* and the *Gaming Act 1857* as amended by the 1960 and 2005 Acts.

windfall is added to the list of exceptions to indemnity and subrogation, its retention by the insured not only undermines the indemnity principle but also makes a mockery of subrogation.

SUMMARY

This article examines the continuing and overall problems of indemnity and subrogation under common law (English law as practised in England and the countries where it has been adopted). It argues that it is untenable to grant the insured's retention of any windfall in contravention of indemnity and subrogation. Furthermore, that it is inconsistent to do so while trying to uphold indemnity and subrogation at the same time. Above all, it is disturbing to do so only in some cases and without providing any justification for the approach. If indemnity and subrogation are the bedrocks of insurance, then undermining them strikes at the very existence of insurance. This article uses decisions from marine, property and export credit insurances as examples to highlight the problem. It argues on five premises. First, that the terms 'profit', 'excess' and 'surplus' are used interchangeably and wrongly to describe windfall. This article opts for 'windfall' as the appropriate term. Second, the insured's retention or loss of the windfall is awarded inconsistently and as a 'rule of thumb' rather than following any logical approach. Third, and consequently, it is unclear whether legal decisions on windfall are based on law or policy. Fourth, it is also not clear whether the operation of windfall is automatic or based on law, tort or equity. Fifth, and finally, that to justify and protect subrogation and indemnity principles, and therefore the very basis of insurance, windfall should be added to the list of existing exceptions, limitations or modifications to indemnity and subrogation. As a way forward for reform, this article calls for: (a) judicial law making by adopting 'co-sharing', along with other windfall principles, between the insurer and the insured; or (b) additional agreements between the parties to do so along the lines of old *Clause 17* of the standard ECGD policies. Failing that, the Law Reform Commission should advise the legislator to enact reforms on this important aspect of insurance law.

REFERENCES

- Ademuni-Odeke, (2007). Insurance of FOB contracts under Anglo-American and other common law jurisdictions, *Tulane Maritime Review*, 31, 1-37.

- Bennett, C. (1992). *Dictionary of Insurance*, London: Pitman Publishing.
- Birds, J. (2013). *Birds' Modern Insurance Law*, London: Sweet & Maxwell.
- Birds, J. (2010). *Birds' Modern Insurance Law*, London: Sweet & Maxwell.
- Birds, J. (2007). *Birds' Modern Insurance Law*, London: Sweet & Maxwell.
- Birds, J. (1979). *Contractual subrogation in insurance law*, JBL.
- Birds, J. (1978). Motor insurance and the knock for knock agreements, *Modern Law Review*, 201.
- Black, H.C. (2001). *Black's Law Dictionary*, West Publication House, St. Paul, Minn.
- Black, H.C. (1990). *Black's Law Dictionary*, West Publishing House, St. Paul, Minn.
- Buckley, A.J. (2000). Subrogation - have insurers' rights been extended?, *Commercial Law Practitioner* 7(1), 22-26.
- Buckley, A.J. (2006). *Insurance Law*, Dublin: Thompson Round Hall.
- Burglass, L. (1991). *Marine Insurance and General Average in the United States*, Cornell Maritime Press.
- Bybee, J.S. (1979). *Profits in subrogation: an insurer's claim to be more than indemnified*. Scholarly Works. Paper 347. <http://scholars.law.unlv.edu/facpub/347>.
- Clark, M. Marine insurance system in common law countries, status and problems, https://www.bmla.org.uk/annual_report/rep_marine_clark.htm
- Corrigan, M., Campbell, J.A. (1995). *A Casebook on Irish Insurance Law*, Dublin: Oak Tree Press Dublin.
- Curzon, L. B. (1993). *Dictionary of Law*, London: Pitman Publishing.
- Derham, S.R. (1986). *Subrogation in Insurance*, Sydney: The Law Book Company.
- Greenblatt, J. (1997). Insurance and subrogation: when the pie isn't big enough, who eats last?, *University of Chicago Law Review*, 64(4), 1337-1366.
- Hardy, I. (1986). *General Principles of Insurance Law*. London: Butterworth.
- Halsbury's Laws of England*. (2011).
- Halsbury's Laws of England*. (2010). Trade and Industry.
- Halsbury's Laws of England*. (2008). Financial Services and Institutions.
- Hasson, R. (1985). Subrogation in insurance law - a critical evaluation, *Oxford Journal Legal Studies*, 5, 416.
- Hemsworth, M. C. (1998). Subrogation: the problem of competing claims to recovery monies, *Journal of Business Law*, 111-122
- Holdsworth, Sir W. (1966). *A History of English Law*, London: Methuen/Sweet & Maxwell.
- Horn, R. (1964). *Subrogation in Insurance Theory and Practice*, Homewood, Illinois.
- International Bar Association (IBA) Insurance Committee Subrogation Project. (2016). https://www.ibanet.org/LPD/Financial_Services_Section/Insurance/Subrogation.aspx; <https://www.ibanet.org/Document/Default.aspx?DocumentUid=9A6FD705-ABD7>.
- Kimball, S.L., Davis, D.A. (1962). The Extension of Insurance Subrogation, *Michigan Law Review*, 60 (7), 841-872.
- King, C.G. (1951). Subrogation under contracts insuring property, *Texas Law Review*, 30, 62.
- Lowry, J., Rawlings, P., Merkin, R. (2011). *Insurance Law Doctrines and Principles*, London: Hart Publishing.
- Macdonal, A.M. (1979). *Chambers Twentieth Century Dictionary*, London: Chambers.
- Mackay, L. (2011). *Halsbury's Laws of England*, Vol.60.
- Marasinghe, M.L. (1975). An historical introduction to the doctrine of subrogation, *Valparaiso University Law Review*, 10, 45.
- Marasinghe, M.L. (1975). An historic introduction to the doctrine of subrogation The Early History of the Doctrine I, *Valparaiso University Law Review*, 10 (1), 45-65.
- Mead, P. (1990). Co-Insurers and Subrogation, *Insurance Law Journal*, 3, 48-53
- Mitchell, C., Watterson, S. (2007). *Subrogation: Law and Practice*, Oxford: Oxford University Press.
- Mitchell, C. (1998). Subrogation, co-insurance and benefits of insurance clauses, *International Insurance Law Journal*, 6, 263.
- Mitchell, C. (1996). Defences to an insurer's subrogation action, *LMCLQ*, 343.
- Mitchell, C. (1994). *The Law of Subrogation*, Oxford, Oxford University Press.
- Mozley, H.N. and Whiteley, G.C. (2001). *Law Dictionary*, London: Butterworths.
- O'Regan-Cazabon, A. (1999). *Insurance Law in Ireland*, Dublin: Round Hall, Sweet & Maxwell.
- Procaccia, U. (1973). The effect and validity of subrogation clauses in insurance policies *Insurance Law Journal*, 573.
- Rawlings, P., Lowry, J. (2003). *Insurance Law, Cases and Materials*, Oxford: Hart Publishing.
- Sheldon, N.E. (2000). *The Law of Subrogation*, Frederick, M.D. Ed., Beard Books.
- Walmsley, R.M. (2007). *Subrogation and Contribution in Insurance Practice*, Oxford: Oxford University Press.
- William, L. et al. (1985). *The Shorter Oxford English Dictionary*, Vol. 1, Guild Publishing.
- William, L. et al. (1985). *The Shorter Oxford English Dictionary*, Vol. 2, Guild Publishing.