



*Fraudulent insurance
claims and collateral lies:
does fraud unravel all?©*

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The Law on Fraudulent Claims

- “Fraudulent claim” – a genuine claim, but amount fraudulently exaggerated.
- Genuine part of claim forfeited if claim partly fraudulent or fraudulently exaggerated: *Britton v Royal Insurance Company* (1866).
- Home burglary of £16,133.94 worth of goods. Fraudulent exaggeration by addition of £2,000 claim for computer forfeited entire claim: *Galloway v. Guardian Royal Exchange (UK) Ltd* (1999).

The “Fraudulent Device” Doctrine

- “Fraudulent device” – an irrelevant lie dishonestly intended to embellish a perfectly valid claim.
- “*Dearth of convincing authority*” before *Agapitos v. Agnew (“The Aegeon”)* (2003).
- Facts of *The Aegeon*: ship destroyed by fire; post-action, insured fraudulently misrepresented date of hot work.
- Held: No fraudulent device defence, as fraudulent claims rule ceases to apply upon commencement of litigation.

The Aegeon – Mance LJ’s dictum

- Mance LJ *obiter* and tentatively suggested extending the fraudulent claims doctrine to:

“the use of fraudulent devices or means which would, if believed, have tended, objectively but prior to any final determination at trial of the parties’ rights, to yield a not insignificant improvement in the insured’s prospects—whether they be prospects of obtaining a settlement, or a better settlement, or of winning at trial.”

- But no inducement requirement.

1st Instance Decisions applying The Aegeon

- *The Game Boy* (2004): claim forfeited by assured handing over documents to the insurer's solicitor after the loss which assured knew to be false.
- *Aviva Insurance Ltd v Brown* (2012): assured proposed mother's old home, which had passed to him, to insurer as rental accommodation during subsidence repairs. £235,000 subsidence and accommodation claim forfeited.

DC Merwestone – the Facts

- Loadport (Klaipeda) temperatures of -10°C to -35°C. Chipped ice cleared using emergency fire pump; Crew negligently failed to close the sea inlet valve and drain the system.
- Seawater in pump froze, cracking the pump and bending the restraining bar over its filter cap.
- Ice melted during voyage to Bilbao leading to seawater ingress into bowthruster room and through pipe tunnel to engine room bilges. ER flooded. Bowthruster alarm did not ring.

DC Merwestone-insurer's defences

- No peril of the seas as seawater ingress neither fortuitous nor “of the seas”;
- No crew negligence (“Inchmaree”) cover because Owners guilty of 7 separate instances of causative want of due diligence;
- Owners privy under s. 39(5) of the MIA to causative unseaworthiness; and
- Owners’ Managers’ CEO had deployed 9 separate fraudulent misrepresentations in support of the claim.

Popplewell J's Decision

- All insurers' defences failed, save for one fraudulent device:
- CEO genuinely believed as realistic claim in letter to insurers' solicitors that alarm had sounded at noon but crew ignored it.
- But CEO reckless as to (implied) representation in letter that crew had reported noon alarm and said it was not investigated as it was believed to have been caused by the rolling of the Vessel.
- €3.241 million claim forfeited.

Insured's Arguments before the CA

- Judge wrong on facts to find implied representation in letter and recklessness by CEO.
- Fraudulent claims doctrine should not be extended to fraudulent devices – Mance LJ's dictum in *The Aegeon* should not be followed, being disproportionate; "fraudulent devices" are conceptually distinct from claims.
- Doctrine would violate Article 1, Protocol 1 of the *European Convention of Human Rights* ("A1P1") protecting right to property.

The CA's Decision

- Insured's appeal dismissed.
- Policy favoured adopting Mance LJ's tentative suggestion as ratio; fraudulent devices are a sub-species of fraudulent claims.
- A1P1 engaged, but fraudulent device doctrine is proportionate as deterrence is a legitimate aim, and *"the fact that forfeiture is a harsh, in some circumstances very harsh, sanction does not mean that it is disproportionate to that aim"*.

The Supreme Court's Decision

- Insured advanced same legal points before SC.
- Held, “collateral lies” (fraudulent devices) in support of a valid claim do not forfeit the claim:
 - 1) Since insurance claim arises at time of loss, the rule would effect retrospective forfeiture.
 - 2) Important difference between fraudulent claims and collateral lies.
 - 3) No other area of civil law effects forfeiture for a fraud that has no impact on its target.
 - 4) Materiality test cannot apply absent inducement requirement.

The Effect of the SC's Decision

- Proposed extension “*disproportionately harsh to the insured and goes further than any legitimate commercial interest of the insurer can justify.*” (Per Lord Sumption)
- 3 types of fraud:
 - Whole claim false/fabricated - no rule required.
 - Valid claim dishonestly exaggerated – valid part forfeited under fraudulent claims doctrine (now § 12 Insurance Act 2015).
 - Valid claim embellished by collateral lies ultimately found to be irrelevant to insured's right to recover – no forfeiture.

The effect of the Insurance Act 2015

- §12 gives the insurer remedies in respect of “fraudulent claims”.
- Insurer not liable to pay fraudulent claim, can recover sums already paid for that claim and can terminate cover from the time of fraud.
- Obligations accrued before the fraudulent act are not affected.
- “Fraudulent claims” deliberately not defined and left to the courts to sort out.
- Previously unclear whether fraudulent devices included. Now clear due to SC’s decision.

Express Fraudulent Device Term?

- Lord Mance (dissenting) suggested getting around the majority's decision by inserting an express fraudulent device clauses. But:
- Any term in a consumer insurance contract "*which would put the consumer in a worse position as respects any of the matters provided for in Part 3 or 4 of this Act*" is of no effect (§15 Insurance Act 2015).
- Such term in a non-consumer insurance contract must satisfy with §17's transparency requirements (§16 of 2015 Act).



Thank you for listening.

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