PRINCIPLES AND PRACTICE OF SUBROGATION IN RELATION TO MARINE INSURANCE CONTRACT

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INTRODUCTION

Mr. Chairman, distinguished guests, ladies and gentlemen. I am delighted to be presenting a paper at this 6th Practical Maritime Dispute Resolution Seminar and to have the opportunity of addressing you on “Principles and Practice of Subrogation in relation to Marine Insurance Contracts”.

We are all seated today as a people joined together by a singular variable, an item, a value system, first of all because of our passion to provide service to whom that service is due. To provide cutting-edge solution to post-compensatory challenges in marine insurance as a contract of indemnity.

There is no gainsaying the fact that, the duty to compensate the insured after a loss or damage belong to the insurer due to its undertaking to do so and the consideration which the insured had been made to give as a result. In a corresponding manner, something is amiss, the insurer has been left with a hole in its pocket, surely the third party should be made to pay for its negligence or lack of due care which has led to losses for the insured. Whereas, the insured has undeniable right to move against either the insurer or the third party who can lead to double recovery, the doctrine of ‘subrogation’ with its array of case law provides lasting solution to the issues which has agitated the minds of all interested parties.

FOUNDED ON PRINCIPLE OF INDEMNITY

An individual, corporate body or government with interest in maritime adventure have the right to be indemnified or have the subject matter restored to the pre-loss state on the occurrence of the insured event which may bring about loss or damage to cargo or vessels. Having paid under the legal obligation to do so, the insurer is expressly and impliedly empowered to move against the third party to make good its outlay. The marine insurance being a contract of indemnity thus forms the basis upon which insurers’ subrogation right operates. In Castellian v Preston in (1883)1. His Lordship Sir, Briet (as he then was) summed up the ratio in that case ‘that upon indemnification of the insured the insurer must be subrogated to his rights.

INSURER CAN ONLY PURSUE A CLAIM IN INSURED’S NAME AFTER PAYMENT

The real meaning of the principle of subrogation is much further than transferring of rights. The relationship between the insured and the third party concerning the subject matter of insurance is to the effect that the third party is bound to make good the loss or damage of a cargo or vessel, where this has been achieved, there is no subrogation right for the insurers under this circumstance. Section 79(1)2 of the Marine Insurance Act i.e ‘Right of Subrogation’ states inter alia that, the principle will only operate in the event of full payment of the total loss of the subject matter. The insurer is thereupon become entitled to take over the interest of the insured in whatever may remain of the subject matter. That was the situation in the Castellian case cited earlier.

1. “As between the underwriter and the assured the underwriter is entitled to the advantage of every right of the assured, whether such right consists in contract, fulfilled or unfulfilled, or in remedy for tort capable of being insisted on or already insisted on, or in any other right…”

2. 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…”
THEORIES UNDER THE PRINCIPLE

I. Contractual theory

The insurance policy purchased by the insured is a contract between the parties subject to which the insured will be compensated upon the occurrence of the perils insured against. In the policy are terms, provisions and conditions underlying the contract one of which is that the insured should not jeopardize subrogation rights of the insurer, which the parties to the contract must adhere to so that the provisions of the policy can operate. For this to be realized, the insured pays premium. It is therefore incumbent on the insurer to fulfill its obligation in the event of a loss and it is on this basis will the insurer be subrogated to the rights of the insured.

II. Tort

We all have rights which impose obligations on us as individuals while enjoying our lives and properties. We also owe our neighbour a duty to take care not to injure, or cause accident to them and their property. Where our misdemeanor interferes negligently, a tort has been committed. A tort is therefore, a civil wrong, which unfairly causes someone else to suffer loss or harm resulting in legal liability for the person who commits the tortuous act. In this case, the victim is legally able to recover his loss as damages in a law suit against the tortfeasor. Thus, even in the absence of an insurance contract, the injured party is legally able to recover from the wrongdoer. This theory operates whether or not insurance is in place, it will at all time occur however that the injured party who also has an insurance policy is able to decide who to pursue. Most of the time, it is the insurer that meets this purpose due to its financial capability, while the insurer will also look to the wrongdoer for reimbursement upon payment of the insured claim.

III. Doctrine of Unjust Enrichment

We must not forget that the main reason for subrogation is that the insured must not make profit by getting paid by the insurer as well as obtaining compensation from the third party. 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 irrespect of the subject-matter insured. If it is a total loss, the insurer is subrogated to all the rights and remedies of the insured and also acquires title to the subject matter. However, the insurers should not be able to recover more than they have paid out to the insured. In its broadest term, the intention of the doctrine is to see that no one benefit more than his equitable proportion and no one is made to bear more of misfortune than its equitable share.

CAUSES OF ACTION LEADING TO SUBROGATION

Whenever consideration is to be given to possibility of recovery against a third party, it is expedient to consider all possible cause of action which may include one of the following:

- Breach of contract
- Negligence
- Nuisance
- Defective Premises Act 1972
a) Breach of contract

There could be a breach of contract concerning the terms conditions applying as well as any relevant limitations and exclusions. For example, in a case for loss of cargo under an All Risks cargo policy the insured is obliged to prove that the vessel owner(s) or their manager(s) breached the agreed mode of handling and safe carriage of cargo to the port of destination.

b) Negligence

This is a case where the duty of care is owed, has been breached, the breach of which has caused the damage and the damage can be demonstrated as not being too remote. For example, a loss or damage to imported cargo during transit from the port to insured warehouse caused by negligence of the vehicle driver or that of his staff (motor boy).

c) Nuisance

This is the wrong done to a person or persons by unlawfully disturbing them in the enjoyment of their property. A case of pollution hazard will cause owners of property adjoining the sea loss or damage by users of the sea. The owner of those properties adjoining the sea duly has a cause of action against the seafarers (users of the sea) and is an occasion to be borne in mind for subrogation purposes.

d) The Defective Premises Act 1972

Section 4(1) of this act imposes duties on builders who work on dwellings and landlords having possession of the buildings to ensure that work is done in a professional manner with proper material and that landlords should not let out buildings in a dilapidated state or having buildings that are poorly maintained which can cause injury to their tenants and third parties. In this vein, the ports have been concessioned no doubt; the landlord still remains The Nigerian Ports. Losses emanating under the terminal operators may involve the state of repair of the premises, which may lead to subrogation issue.

FUNDAMENTAL PRINCIPLE OF EQUITABLE RESTITUTION

There are various situations where restitutionary duty has to be performed. In such cases, and whether or not the parties have previously agreed on the modus operandi concerning indemnity, the law generally recognizes restitutionary remedy. Depending on the proper distribution of the burden of liability between claimant and defendant, the claimant’s primary remedy is contribution or reimbursement. There are however limitations or drawbacks to the principle.

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3 Sec 4(1) “Where premises are let under a tenancy which puts on the landlord an obligation to the tenant for the maintenance or repair of the premises, the landlord owes to all persons who might reasonably be expected to be affected by defects in the state of the premises…”
i. **Recoupment**

As known, the basic and significant principle in insurance law is that the insured that faces loss or damage under a marine insurance policy shall be fully indemnified by his marine insurance policy. However, the insured should not receive more than full indemnification. Therefore, recoupment is a right usually exercised by an insurer claiming from the insured a sum equivalent to any sum of damages paid to the insured by a third party legally liable for the loss. Otherwise, it means that the insured is earning benefit from the insured risks. It does not matter that the benefit happens before or after the indemnification from the insurer, the insurer is entitled to substitute the position of the insured and get the benefit as well. When the benefit from the third party happens before the indemnification paid by the insurer, “the net effect is reducing the liability of the insured. Moreover, when the third party pays the benefit after the indemnification from the insurer, the insurer has the right to accept the benefit. However, it also brings some confused problems such as the voluntary payment and gifts the discussion of which will follow now.

ii. **Voluntary Payment**

Ordinary rule of reasonability would suggest that whatever payment is made and received from a third party or wrongdoer in excess of the claim from the insurer should be kept as a bailee for the insurer; however the line of case law and precedent disissently. The intention is to benefit the insured, which does not in any way exclude the insurer or diminish the loss.

This occurred in *Burnand v Rodocanachi* (1881-82)\(^4\). The insured had already been paid by the underwriters for destruction of the cargo; in addition, the American Government paid the compensation to the cargo owners for the loss as well. The judgment suggested that the underwriters could not get the compensation, because the compensation from the American Government was a kind of voluntary payments but not the payment for reducing the loss. The government would not pay the money because of reducing the indemnified loss against the insurer.

iii. **Gift**

A gift from a third party, intended as extra compensation, will not be taken into consideration when accounting to insurers. Also, where an insured has made a return to the insurer he can retain any surplus sum received from a third party once it has accounted to insurers i.e. windfalls belong to the insured.

**RIGHT OF SUBROGATION BEFORE AND AFTER INDEMNITY**

As already known, it is difficult for the insurer to claim subrogation right before full indemnification but there are some implied and expressed obligation between the insurer and the insured, which the insured must observe:

\(^{4}\) Burnand v Rodocanachi (1882)“The general rule of law (and it is obvious justice) is that where there is a contract of indemnity (it matters not whether it is a marine policy, or a policy against fire on land, or any other contract of indemnity) and a loss happens, anything which reduces or diminishes that loss reduces or diminishes the amount which the indemnifier is bound to pay; and if the indemnifier has already paid it, then, if anything which diminishes the loss comes into the hands of the person to whom he has paid it, it becomes an equity that the person who has already paid the full indemnity is entitled to be recouped by having that amount back.”
RIGHT OF SUBROGATION BEFORE INDEMNITY

- At all times before any occurrence of loss, the insured is obliged to observe the terms and conditions under the policy and must be ready to preserve subrogation right of the insurer.

- The insured must be ready to provide necessary information and assistance to the insurer to enable the company assume the right of subrogation.

RIGHT OF SUBROGATION AFTER INDEMNITY

- Under the policy, the insured is obligated to make sure that nothing will diminish the subrogation right of the insurer even where there is settlement between the insured and the third party.

- It is important to remember that, following a loss, there can only be one claim made in the name of the insured, it is therefore important to ensure that all insured and uninsured losses are included. The reasons for this are based on public policy. There is a public interest in avoiding any possibility of two courts reaching inconsistent decisions on the same facts and issues, in there being finality in litigation and in protecting citizens from being “vexed” more than once by what is really the same claim.

- In reality, there is an expressed term in the insurance policy about the insured’s obligation before full indemnification. The Duty of Assured Clause in the Institute Time Clauses Hulls is an example of this express obligation, in the Institute Cargo Clauses ‘A’ the same duty is imposed on the insured. In these cases the insurer can compel the insured to action against the third party before expiry of time allotted in the Institute clauses. It however occurs that in reality, the insurer would normally pay full indemnity as soon as possible and then subrogate the rights object matter against the third party.

EXPRESS OBLIGATION OF THE ASSURED PRIOR TO FULL INDEMNIFICATION

In reality, there is an express term in the insurance policy about the insured’s obligations before full indemnification. The Clause 9(1) in the institute Time Clauses Hulls i.e. Duty of the Assured is an example of this express obligation for the insured. Under Marine Cargo Insurance Clause 16(2) named Duty of Assured is also an express obligation to be observed prior to payment.

LIMITATION OF SUBROGATION

These are empirical reasons why the prayers of the insurer to subrogate the legal rights of its insured may be restrained or flagrantly denied.

5 Clause 9(1) Institute Time in Clauses Hulls (2003) “In case or any loss or misfortune it is the duty of the Assured and their servants and agents to take such measures as may be reasonable for the purpose of averting or minimizing a loss which would be recoverable under this insurance”.

6 Clause 16(2) Institute Cargo Clauses ‘A’ “It is the duty of the Assured to ensure that all rights against carriers, bailees or other third parties are properly preserved and exercised and the Underwriters will, in addition to any loss recoverable hereunder, reimburse the Assured for any charges properly and reasonably incurred in pursuance of their duties.”
A. Limitation Of Liability Or Limitation Of Compensation

The right of insurer against the third party is based upon the insured’s right. This might be affected if there is limitation of liability or compensation in the contract between the parties. Thus, in an action in which the insured could not have recovered damages, neither can the insurer, they have no independent right different from the insured.

B. Settlement between the Assured and Third Party Affects Subrogation

The deduction here is that in the absence of insurance contract the parties already subscribed to an agreement by which the contract shall operate. Settlement between the assured and the third party might affect the subrogation of insurer. The settlement whether it is a bona fide settlement or not, is already agreed before paying the full indemnity. The insurer can however claim the compensation from the assured if he could prove that such a bona fide settlement is not harmful.

C. Arbitration Clause

This is very interesting in that this is a very important clause in a marine insurance policy. Where the amount to be paid is referred to arbitration, the award of the arbitrator has to be given first and when what will become subrogation right for the insurer is notdetermined as easily as it would by an insurer. It may also be very difficult to subrogate to such right subsequently. The line of decided cases is such that there is no assumed or reliable precedent.

D. Bankruptcy Of The Insured

Insurers’ right against the third party is derived from that of the insured; therefore in the event of loss of financial capacity or lifeline called bankruptcy, the insurer may lose the right of subrogation before or during litigation unless the insurer is able and willing to restore the assured.

WAIVER OF SUBROGATION

This is a common feature in a marine insurance policy especially where an oil company or the subsidiaries are the owners of tankers (vessels) used in transporting oil while they also have interest in the cargo in the tank of the vessel. Therefore, it makes good commercial sense when negotiating cover to ask that a subrogation waiver clause which will prevent the insurer pursuing subrogation from the negligent party who happens to be the same insured by virtue of the interest in both vessel and the cargo.

WAIVER OF SUBROGATION AND COASSURED

From the above, it then follows that insurers cannot claim from a wrongdoer or liable vessel, which belong to the same shipowner or management after payment of indemnity. And where co-assured is involved, insurer cannot equally exercise the right of subrogation against a negligent co-assured. Otherwise, the insurer would in effect be causing the assured with whom he had settled to pursue proceedings which if successful would at once cause the co-assured to sustain a
loss arising from loss or damage to the very subject matter of the insurance in which that co-assured has an insurable interest and a right of indemnity under the policy. This is based on theory of circuitry of action.

There is however some qualifying factors:

- The policy must make it clear that the co-assured is intended to benefit from the provisions in the policy.

- The policy must make it clear that the main assured, in addition to contracting for the insurance provisions on his own behalf, is also contracting as agent for the sub-contract that these provisions should apply to the co-assured.

- The main assured must have authority from the co-assured to contract on his behalf, although perhaps later ratification by the co-assured would suffice.

- Decision on whether the co-assured pays part of the premium.

The exception is where a co-assured is guilty of willful misconduct or his misdemeanor is not covered by the policy.

**SUBCONTRACTORS AND SHORT PERIOD CONTRACTS**

In contrast with the above, there are contract works forming part of the whole contract but which are mainly supportive in nature and are for very short period. It is envisaged that it will be a stifling of process to beam light on the activity of such subcontract works in order to establish causation and negligence for the sake of subrogation right of insurer. As such, subcontract works for short periods are seldom a matter for consideration.

**CHALLENGES FACING RIGHT OF SUBROGATION**

**a. The Insured**

Whilst it is true that marine insurance is insurance of transportation, the insuring public and their agents either ignorantly or tacitly decide to confine themselves to indolence or deliberately failed to learn that their business is international trade and thus are based on various market agreements, protocols and rules. At the same time, there are scores of decided cases, which also forms precedent from which several of the terms, conditions and provisions have emanated.

Moreover, the various rules, agreements and protocols are witnessing review in line with changing economic and trading realities across many frontiers. As such, we cannot live in isolation; experience has shown that when loss or damage occurs, our clients find themselves wedged between peaceful relationship and active hostility with their insurers. Verbal threats and letters tainted with disparaging innuendoes aimed at soiling the image of the insurers become the order of the day.
Whereas, all that is needed is seeking advice of experienced mariners, professionals with known pedigree. The main issue here is preservation of subrogation rights of insurers by the insured, which duty clients in our market find so alien and are unwilling to observe. Akin to that is the unwillingness to give subrogation receipt on time even in the face of one-year time bar on the bill of lading. This action of theirs negates the “Duty of the assured clause” under the policy as already mentioned in this paper.

**THE THIRD PARTY (The Shipowner/Managers)**

When you look into the past and a solemn giggle or smile does not adorn your face then you know those times were bad. Such is the history of attitude of shipowners and their managers concerning insurers’ interests as detailed below:

- Bill of lading unilaterally favours place of shipment and or principal place of business of the carrier.
- Claimants to surrender to foreign country’s law and jurisdiction.
- Claimants to surrender to Hague Visby Rules
- Extension of limitation period is at their discretion

**HAGUE VISBY RULES PERSPECTIVE VERSUS HAMBURG RULES PERSPECTIVES**

The United Nations Convention on the Carriage of goods by sea 1978 known as The Hague Visby Rule and the Hamburg rules are two cargo regimes operating in respect of cargo interest today. For the purpose of this paper the salient points worthy of note are that:

- Vessel owners’ favours application of The Hague rules because it gives control of which country’s legal system should operate in claim settlement.
- It gives only one-year limitation period.
- Shipowners are able to determine the quantum of settlement to the detriment of insured and the insurer and the right of subrogation is often rendered useless through offer of very negligible amount compared to claim paid by the insurer.

On the other hand the Hamburg Rules is more accommodating to cargo interests and underwriters for the reason that:

- It provides for two years time bar for cargo claim\(^7\).
- Cases may be brought in the contracting states or port belonging to the plaintiff or insured\(^8\).

\(^7\)Article 20(1) Hamburg rules
\(^8\)Article 21(1) Hamburg rules
It is worthy of note to comment that the use into which third parties i.e vessel owners put the HaugeVisby Rules have not been in the interest of other stakeholders especially the insurers. Having paid the claim, recovery effort is almost always long-tailed with attendant cost and management time.

ALTERNATIVE DISPUTE RESOLUTION

As an industry whose main focus is provision of service to the insuring public, there is need to visualize and vividly bring into the purview of risk management a generally acceptable alternative dispute resolution mechanism. Concerning this gesture, there is no need to look too far, there abound in general and marine insurance fields empirical alternative means of conflict resolution besides litigation and arbitration due to need for speed in settlement, escalation of costs and court calendars suffering from over-crowding, greater demand and budgetary constraints.

The establishment of the Customer Complaints Bureau by the Nigerian Insurers Association is a laudable option. Through this medium 32 cases had been brought and judiciously treated successfully. In the same vein, the Complaints and Bureau Unit of the Establishment and Compliance Department of the National Insurance Commission was set-up to have complaints resolved promptly and amicably.

There is also the investigative, mediatory and conflict resolution effort available through appointment of experienced professionals whose intervention and advice in disputed marine insurance related claims are respected. It will be more beneficial if stakeholders in the insurance industry and the insuring public eschew undue “winner-take-all attitude” embedded in litigation and the much avowed slowness often experienced with arbitration and give support to expanding the body of knowledge for more peaceful settlement of marine insurance claim.

CONCLUSION

Distinguished audience, Subrogation as a unique platform for restitution and equitable distribution of compensation among parties involved in maritime trade and of course marine insurance has evolved and being made use of in our market. It is however mind boggling to note that there are few professionals today in most underwriting firms and fewer mariners and recovery agents who are able to relate effectively with foreign shipowners or have international connections for the main purpose of securing subrogation rights of local insurers.

The principle of subrogation will continue to be a vanguard for insurers’ interests but in practice, there is need for more involvement of all interested parties whereby underwriters can reduce their claim outlays through timely and commensurate recoveries.

I thank you all for your rapt attention.

Thank you.

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