Case No: A3/2005/1022

Neutral Citation Number: [2006] EWCA Civ 378
IN THE SUPREME COURT OF JUDICATURE
COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM THE HIGH COURT OF JUSTICE
QUEENS BENCH DIVISION
COMMERCIAL COURT
Mr Justice Colman
1996FOLIO644
[2005] EWHC 665 (Comm)

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: Friday, 7th April 2006

Before :

LORD JUSTICE WALLER
LORD JUSTICE LONGMORE
and
LORD JUSTICE LLOYD

- -

Between :

North Star Shipping Ltd & Ors	**Appellants**
- and -	
Sphere Drake Insurance plc & Ors	**Respondents**

- -

(Transcript of the Handed Down Judgment of
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Official Shorthand Writers to the Court)

- -

David Goldstone (instructed by **Davies Johnson & Co, Solicitors**) for the **Appellants**
Nicholas Hamblen QC and Graham Charkham (instructed by **Richards Butler, Solicitors**) for the **Respondents**

- -

Judgment

Lord Justice Waller :-

Introduction

1. The appellants were the owners of the North Star. That vessel was insured on a total loss only basis by the respondents under a war risks policy placed on 27th April 1994. On 6th July 1994 the North Star was damaged by an explosion and so badly damaged as to be a constructive total loss. The insurers refused to pay on two bases – first on the basis that the owners had been complicit in the bombing of the vessel, and second on the basis that they were entitled to avoid the policy on the grounds of non-disclosure. Colman J, by a judgment handed down on 22nd April 2005, found in favour of the insurers on both grounds. He refused permission to appeal but the owners obtained permission to appeal in relation to both aspects with limitations relating to certain findings of fact by the judge. For reasons which it is unnecessary to enter into, directions were given that the non-disclosure aspect of the appeal should be heard first. In the context of that appeal the relevant limitation placed on the owners obtaining permission was that they should not be entitled to challenge the judge's finding that, if material facts were not disclosed, the underwriters were induced to write the policy by the non-disclosure of those facts.

2. This part of the appeal, argued before us over two days, thus raises only the following point – was the judge right to find that certain facts, which it is common ground were not disclosed by the owners to the underwriters, were material i.e. were they facts which would have influenced the judgment of a prudent underwriter. The facts with which this part of the appeal are concerned are put shortly the following:-

(1) Pending criminal proceedings in the Greek courts charging fraud, namely

(a) the Sotiriadis proceedings;

(b) the Angelopoulos proceedings;

(c) the Overseas Agency proceedings;

(d) the Alliance Trust proceedings.

Harry Petrakakos was a defendant in all the proceedings and Michael Petrakakos was a defendant in the Sotiriadis proceedings only. The basic allegation against the Petrakakos brothers who owned and managed the company owning the vessel, itself part of a group of companies known as 'The Kent Group', was that they had dishonestly misappropriated clients' money.

(2) Civil proceedings by Atlantic Light Corporation in Panama against Kent Group companies claiming damages for a fraud on a business associate.

(3) The valuation of the North Star under the War Risks policy at US $4 million exceeded, by a considerable margin, the actual value of approximately US$ 1.3 million.

(4) That the insurance of the Kent fleet was cancelled by hull and machinery underwriters with effect from 6 March 1994 for non-payment of the premium.

Argument relating to a further fact alleged not to have been disclosed related to the owner's financial position has sensibly been agreed to be adjourned to be dealt with, if necessary, with the other aspect of the appeal on the basis that the owners' own financial position is controversial and inextricably linked with the evidence in relation to the owners' complicity in the loss.

3. For reasons which I will explain later facts (3) to (4) are in my view individually very arguably not material, and I have doubts whether it is legitimate to add them together in order to make them more arguably material. Unsurprisingly they never loomed large in the insurers' arguments, at least before us. Although some reliance was placed on fact (2), the Panamanian proceedings, it is the charges in the Greek criminal proceedings, fact (1), on which greatest reliance has been placed. They are alleged to be material as going to moral hazard, and the material fact relied on is "the allegations", not the dishonesty itself because, although the charges had been made prior to the placement, the charges were dismissed by the Greek courts in 1995 and 1996. The insurers have never asserted that they could establish the truth of the allegations. Even as regards fact (2), the allegations in the Panamanian proceedings, the insurers did not seek to establish the truth of the allegations made in those proceedings; it was the allegations themselves that they asserted were material. This aspect of the appeal raises for consideration accordingly what is the correct approach to an allegation of dishonesty which at the time of placement the insured would maintain was false, and ultimately after placement of the insurance turns out to be false, or an allegation that the insurers do not seek to establish as true.

The law

4. Courts have previously wrestled with this problem, recognising first that there is something unjust in the notion that insurers can avoid a policy on the grounds of a suspicion as to the insured's probity flowing from an allegation which is in fact false, but second that it is difficult to gainsay an underwriter who gives evidence that an allegation of fraud would have an influence on his underwriting judgment if it was unknown at that time whether that allegation was true or false.

5. Different judges have come to different conclusions. Forbes J in *Reynolds and Anderson v Phoenix Assurance Co. Ltd* [1978] 2 Lloyd's Rep 440 at 460 recognised that the odd feature of a rule that required allegations to be disclosed was that it was in fact only false allegations to which such a rule had any relevance. If the allegation was true then the insured was bound to disclose that he had committed the fraud, and

disclosure of the allegation as such added nothing. As he put it "the only occasion on which the allegation as an allegation must be disclosed is when it is not true" - " a conclusion so devoid of any merit that I do not consider that a responsible insurer would adopt it and nor do I." However, May J had expressed a contrary view in *March Cabaret Club & Casino Ltd v The London Assurance* [1975] 1 Lloyd's Rep 169, and Phillips J in *The Dora* [1989] 1 Lloyd's Rep 69 said that he preferred the view of May J. Colman J then in *The Grecia Express* [2002] 1 Lloyd's Rep Insurance and Reinsurance 669 at 718 supported Phillips J, saying "if an allegation of criminal conduct has been made against an assured but is as yet unresolved at the time of placing the risk and the evidence is that the allegation would have influenced the judgment of a prudent insurer, the fact the allegation is unfounded cannot divest the circumstances of the allegation of the attribute of materiality." But Colman J, having found that the allegation was material, mitigated that finding by holding that for the insurers to persist at a trial in taking the point, in the face of evidence before the court that the suggested facts never existed, would be contrary to their obligation of good faith. In his words "Such a course would be so starkly unjust that I would hold that in such a case it would be unconscionable for the Court to permit the insurers to avoid the policy on the grounds of non-disclosure." [719R]

6. The view of Colman J was considered in the Court of Appeal in *Brotherton v Aseguradora Colseguros SA* [2003] 1 Lloyd's Insurance and Reinsurance Rep 746. The judgments of Mance LJ (as he then was) and Buxton LJ with which Ward LJ agreed confirmed Colman J's view as to the materiality of an allegation even if it turned out to be false. As Mance LJ said "it is difficult to see any reason why, if the evidence satisfies the court that a prudent underwriter would have regarded information suggesting the possibility of moral hazard as material in the sense identified by Lord Mustill [in *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd* [1995] 1 AC 501], that should not suffice. In my view that is the basic legal position."

7. However the Court of Appeal in *Brotherton* rejected Colman J's route for mitigating the possible injustice if the facts established at a trial demonstrated that the allegation was false. They held that Moore-Bick J had been right in refusing an application for disclosure relating to the issue whether an allegation was actually false or not. It was irrelevant, they held, to fight out at a trial the truth or otherwise of an allegation because it was the allegation that was material to be disclosed, and as Mance LJ put it "neither principle nor sound policy" supported the conclusion that a court could hold that an insurer should not be entitled to persist at trial in seeking a declaration that he had successfully avoided the policy as Colman J had suggested. As Mance LJ stated:-

> "It would be an unsound step to introduce into English Law a principle of law which would enable an insured either not to disclose intelligence which a prudent insurer would regard as material or subsequently resist avoidance by insisting on a trial, in circumstances where:
>
> > (i) if insurers never found out about the intelligence, the insured would face no problem in recovering for any losses which arose – however directly relevant the

> intelligence was to the perils insured and (quite possibly) to the losses actually occurring; and
>
> (ii) if insurers found out about the intelligence, then (a) they would in the interests of their syndicate members or shareholders have normally to investigate its correctness, and (b) the insured would be entitled to put its insurers to the trouble, expense and (using the word deliberately) risk of expensive litigation, and perhaps force a settlement, in circumstances when insurers would never have been exposed to any of this, had the insured performed its *prima facie* duty to make timely disclosure."

8. Mance LJ was clearly aware of what he termed "hard cases". Having referred to the view of Forbes J he referred to the views of May J and Phillips J in the following terms-

> "May J in *March Cabaret* and Phillips J as he was in *The Dora* held, after hearing underwriting evidence, that it could be, on the basis, as Phillips J put it, that:
>
> > "When accepting a risk underwriters are properly influenced not merely by facts which, with hindsight, can be shown to have actually affected the risk but with facts that raise doubts about the risk."
>
> I add however that, in this situation, the issues of both materiality and inducement would in all likelihood fall to be judged on the basis that, if there had been disclosure, it would have embraced *all* aspects of the insured's knowledge, including his own statement of his innocence and such independent evidence as he had to support that by the time of placing. This might itself throw a different light on the answer to one or both of the issues of materiality and inducement. That would of course be a matter of fact and evidence."

9. In another passage he said at 757L:-

> "It is true that English insurance law has been criticised in a number of respects (and in the area of private insurance, mitigated by convention and the activity of the Insurance Ombudsman). Lord Mustill in *Pan Atlantic* identified and considered certain main criticisms at pages 528-530. But they did not in that case, and do not seem to me in this case, to bear on the solution of the present appeal. Courts, which are the ultimate decision-makers on issues with respect to both materiality and inducement, will be able to take a realistic and

> even robust view about what constitutes "intelligence" which is material for disclosure as distinct from loose or idle rumours which are immaterial, and as to whether a particular underwriter would have been induced to act differently, had he known of an undisclosed circumstance. But, as I have shown, *Pan Atlantic* identifies a general test of materiality which is on the face of it inconsistent with Mr Millett's case. Further, I cannot see that the decision in *Pan Atlantic* that avoidance depends on inducement as well as materiality lends support to a conclusion that avoidance for non-disclosure of otherwise material information should depend upon the correctness of such information, to be ascertained if in issue by trial."

10. It was in the light of the decision in *Brotherton* that Mr Goldstone in the instant case before the trial judge made this concession. "It is accepted that as the law presently stands, it is open to underwriters to rely upon the fact that such allegations had been made and proceedings brought, notwithstanding that owners were subsequently (i.e. after the cover was placed) acquitted" referring to *Brotherton* and *Drake Insurance plc v Provident Insurance plc* [2004] 1 Lloyd's Insurance and Reinsurance Rep 277 [paragraph 172 of his written opening].

11. In *Drake* the circumstances were different from those in either *The Grecia Express* or *Brotherton*. It was noted in *Drake* that Mance LJ in *Brotherton* in paragraph 28, in referring to certain academic writing which had supported Colman J's approach in *The Grecia Express*, commented that the welcome in one commentary "appears to have been addressed to a case where, *by the time of the purported avoidance*, apparently material facts had proved to be untrue…which does not correspond with the facts of either the *The Grecia Express* or in the present case." One point taken in *Drake* was that Provident had acted in bad faith in avoiding; it was alleged that if it had made any investigation as to the true facts it would have discovered that the undisclosed accident would actually have made no difference to the premium to be charged. The judge acquitted Provident of any lack of good faith. Rix and Clarke LJJ were not prepared to go behind that finding, but expressed the view (echoing that of Colman J in *The Grecia Express* at page 719R) that the doctrine of good faith should be capable of limiting the insurer's right to avoid [see Rix LJ at 298L and Clarke LJ at 307]. Pill LJ would have found that there was a breach of good faith which prevented Provident being entitled to avoid.

12. Mr Goldstone for the owners did not at the trial seek to rely on *Drake* and allege that the insurers were in breach of their duty of good faith in avoiding the policy. In the Court of Appeal, by way of an amendment to the notice of appeal, the owners sought to argue that since by the date of avoidance the owners had been acquitted of all charges in the Greek proceedings, the insurers should not have been entitled to treat the allegations as material at that time. The amendment did not refer to any lack of good faith in the insurers, but in developing his submissions as to why the owners should be allowed to pursue this case in the Court of Appeal, Mr Goldstone made clear that his case would be based on a lack of good faith as recognised (he submitted) in *Drake*. The amendment was resisted by Mr Hamblen QC on the basis that whether

or not the point ever had any chance of success, it could not be fair to run the point in the Court of Appeal for the first time since further evidence would have been required in relation to insurers' knowledge as at the time of avoidance. Indeed if the point had been run, the insurers would have been entitled to disclosure of material in order to enable them to test whether the allegations were in fact true, which in the light of the concession made in the court below and *Brotherton* they had not done. Mr Goldstone was prepared to be put on terms that all assumptions should be made in favour of the insurers in order to meet points on evidence or, he suggested, if further evidence was necessary the matter could be sent back to the judge.

13. It would take quite exceptional circumstances to contemplate an amendment in the Court of Appeal, which might entail the matter being returned to the judge to hear further evidence. As for putting the owners on terms, it was impossible to identify what presumptions could be made against the owners to prevent further evidence being necessary which did not leave the owners without an argument. We accordingly disallowed the amendment.

Arguments on the appeal

14. Mr Goldstone, accordingly, when opening his appeal felt constrained to accept that his argument could not depend on whether the allegations of dishonesty with which the case was concerned turned out to be false or were ones which the insurers did not seek to establish were true. He sought to argue that there was something about a war risks policy which led to the conclusion that the allegations of dishonesty, asserted not to have been disclosed in this case, were not material. I will return to the details of that argument in a moment, but first I should mention how, with some encouragement from the court, Mr Goldstone ultimately sought to broaden his argument on the appeal.

15. He suggested that there might be a distinction between allegations which related to the risk and allegations which bore no relation to the risk. He submitted that the court ought somehow to limit the extent to which allegations which ultimately turned out to be false should be held to be material to the risk and disclosable. His suggestion was that allegations that related to the risk itself were one thing but allegations of dishonesty, which had nothing to do with the risk and nothing to do with either the particular insurance or with insurance at all, were another. In relation to fact (1), the Greek criminal proceedings, or fact (2), the Panamanian civil proceedings, the allegations of dishonesty had nothing to do with the risks being insured and nothing to do with claims under an insurance policy. He suggested that, although he must accept that the decisions of May J in *March Cabaret* and Phillips J in *The Dora* related to allegations of dishonesty which was unconnected to the risk or insurance, the only decision binding on us, *Brotherton*, was in fact concerned with allegations relating to the risk. Thus he argued we were in a position to take a stand and prevent what he said had been recognised by others as an unjust result.

16. Mr Hamblen QC submitted it was not open to Mr Goldstone to go back on the concession he had made in the court below, on the basis of which the case had been fought. He submitted further that what we were being asked to do was to lay down some rule of law in an area where the law was clear and what was lacking as a basis for Mr Goldstone's submission was evidence. He submitted that in any event the principle being contended for was uncertain in ambit and could only give rise to difficult arguments about when an allegation was related to the risk or insurance and when it was not. The test which required disclosure of "material which would influence the judgment of a prudent insurer in fixing the premium, or determining whether he will take the risk" was not capable of being circumscribed by some rule of law that excluded facts which a prudent underwriter would take into account in forming his judgment, particularly as section 18(4) of the Marine Insurance Act 1906 says that "whether a particular circumstance, which is not disclosed, be material or not is in each case, a question of fact."

17. The law in this area is, as others have recognised, capable of producing serious injustice. If every false allegation of dishonesty must be disclosed in all types of insurance, that may place some insureds in the position of finding it difficult to obtain cover at all, and will certainly expose them to having the rates of premium increased unfairly. I do not myself see it as a practical answer to say that exculpatory material can be produced, because unless the material is such as to prove beyond peradventure that the allegation is false, in which event the allegation seems to me no longer material, an underwriter is not likely to be prepared to take time sorting out the strength or otherwise of the allegation. In many instances he would be likely to take the view there is no smoke without fire and turn the placement down or at the very least rate the policy to take account of the allegation. Furthermore the decision in *Drake* may provide an answer in some but very few cases, and in any event does not seem to provide a remedy for the increased premium that an insured may have had to pay on the basis of a false allegation.

18. All that said, it does not seem to me that what must be disclosed can be defined as a matter of law in the way that Mr Goldstone would have us do and in a way which I might have been tempted to follow. It is a matter of evidence what is a material circumstance and, as the head note in *Pan Atlantic v Pinetop* accurately records, a "material circumstance" is one that would have an effect on the mind of a prudent insurer in estimating the risk and it is not necessary that it should have a decisive effect on his acceptance of the risk or the amount of premium to be paid.

19. Expert evidence is called to guide the court as to what would influence the judgment of an underwriter. The only way that, under the present state of the law, the obligation of disclosure in this area of moral hazard can be confined is either by underwriters giving evidence that they would not be influenced and would not take into account an allegation of dishonesty, or by a robust judge rejecting an underwriter's evidence that he would take it into account. Spent convictions no longer have to be disclosed, and old allegations of dishonesty or allegations of not very serious dishonesty, one would hope, expert underwriters would not suggest would influence the judgment of prudent underwriters. But it is unreal to contemplate as a general proposition that underwriters as expert witnesses would ever give evidence that a prudent underwriter would not

take into account in assessing the risk or the terms of the insurance a recent allegation of serious dishonesty the truth or falsity of which has yet to be determined, even if it is quite unconnected with insurance or the risk being insured. Furthermore it is difficult to see a judge not accepting that evidence.

20. This is not the place to explore in any detail what change in the law might mitigate the possible injustice. It is, I accept, not easy. Should what is understood to be moral hazard be confined by law to facts which go to the risk of the insured destroying the subject of the insurance? Should there be some consideration of whether the obligation to disclose should be confined to what a reasonable insured would consider material? Should the absolute right to avoid be reconsidered? What would prevent the injustice which seems to me may result from the obligation to disclose a false allegation of serious dishonesty under the present law, but at the same time protect properly the underwriter who has to assess the risk? I am glad that the Law Commission is looking at this area once again.

21. In any event I must reject Mr Goldstone's invitation to go down the route which we at times gave him some encouragement to follow. His arguments must be more confined.

Mr Goldstone's arguments

22. It is convenient to deal with the Greek criminal proceedings first. The judge explains in some detail what the various proceedings were about but our concern is with what material fact should have been disclosed and what would have been a fair presentation of that material. We suggested to Mr Hamblen QC that he should reduce to a piece of paper how he suggested that it would have been fair to disclose the facts alleged to have been undisclosed. So far as the allegations of dishonesty the subject of the Greek criminal proceedings, he did so in this way:-

> "The Petrakakos brothers have asked that it be brought to insurers' attention that there are four sets of criminal proceedings which have been brought in Greece against Mr Harry Petrakakos alleging fraud, fraudulent representation and obtaining property by deception in connection with a UK investment business set up by a Mr Billington. One of the proceedings also includes allegations of fraud against Mr Michael Petrakakos, and in those proceedings bail conditions have been imposed. In another of the proceedings the authorities have decided that the case should not proceed to trial although this decision is being appealed. In the others no decision has yet been taken by the authorities as to whether there is sufficient evidence for the matter to proceed to trial. In all these proceedings the gist of the allegations made are that Harry Petrakakos persuaded people to part with their money by telling them that it would be invested in copper-bottomed investments whereas the money was used for other purposes

> and some of it was taken by Mr Petrakakos. The amount said to have been lost is about US$1.35 million.
>
> The Petrakakos brothers deny these allegations and are confident that all charges will be rejected. They were themselves victims of a fraud perpetrated by Mr Billington in relation to the UK investment business as is confirmed in the accompanying letter from the Serious Fraud Office. They have been assisting the SFO in relation to criminal proceedings brought against Mr Billington in this country, which have since led to his conviction for fraudulent trading and other offences of dishonesty."

23. What of course was unknown as at the date of the presentation of the risk was the fact, known by the date of trial, that by February 1996 the Greek court had dismissed all the Greek Criminal charges. Mr Goldstone did not suggest that if the facts were disclosable the above would not have been a fair presentation of the facts, save possibly he would suggest a greater emphasis on the denial of any dishonesty and a greater emphasis on the letter from the Serious Fraud Office, which stated that, from their perspective, Mr Petrakakos was a victim of the fraud.

24. Mr Goldstone divided his submissions into two parts, first as to whether the alleged dishonesty was material to be disclosed when placing a war risks policy at all, and second whether the effect of the SFO letter was to render the dishonesty alleged in the Greek criminal proceedings immaterial.

25. As to whether the allegations of dishonesty the subject of the Greek proceedings were material at all in placing a war risks policy, the insurers called Mr Hall and the owners had called Mr Posgate as their expert witnesses.

26. So far as Mr Hall was concerned the judge said this:-

> "178. The Insurers rely on the expert evidence of Mr Hall that the pending Greek proceedings and the allegations in the Panama civil proceedings would have caused a prudent war risks underwriter to decline the risk in any event but particularly having regard to the fact that the assured was a new client, the premium was extremely small – some US$2000 – and the market at the time was very firm. Mr Hall, who had forty years experience in underwriting, including marine war risks policies, was firmly of the view that moral hazard was as relevant to the writing of war risks as of hull and machinery risks."

27. As regards Mr Posgate, the judge was unimpressed. He quoted a number of passages from his evidence but two passages will suffice:-

"Q. Now presumably, you would also accept that, if an insured had recently been charged in criminal proceedings with fraud and had, in fact, committed that fraud, then that too would be a material matter for underwriters to know?

A. Not on the War policy; it would be on the Hull risk policy.

Q. Surely it would be relevant on any policy in relation to which you may have dealings with that insured?

A. I don't think so because the War policy is outside the control to 99% of the assured. So to me, it is irrelevant. His bank require it and I am happy to give it and the assured is not at risk of scuttling that boat to any reasonable amount.

. . . .

Q. So even though, as we have seen, there are various ways a dishonest assured could manufacture a total loss, could manufacture a partial loss, could manufacture exaggerated claims under his War policy, the fact that he is dishonest is of no interest to you whatsoever?

A. It is of no interest to me, but it is of interest to the primary policy; this is an exclusion policy. It is of interest to the leaders of the primary assurance and I would wish to satisfy myself that the primary assurance has gone into those points. I am not interested.

Q. So is what you are saying this: that provided the Hull and Machinery underwriters have been fully informed of the assured's dishonesty?

A. I would have assumed they had; I would not have asked. I can't go around each time I write a War Risk and say, "Look, old boy, did you ask any pertinent questions?" If it is a respectable Hull Risk underwriter, he would have done so.

Q. My question is: if the Hull and Machinery underwriter has not been told various facts relating to the assured's dishonesty, then in those circumstances you would regard those as matters which you should be told?

A. No, I would not.

Q. So your position remains that, however dishonest the insured may be, it is a matter of no concern to you as a War Risk underwriter. Is that right?

A. Put that way, yes."

28. The judge, against the background of other aspects of Mr Posgate's evidence including the fact that, as the judge found, he "appeared fundamentally to disapprove in principle of avoidance for non-disclosure" [see paragraph 214], and the fact that war risks cover had changed in form and substance in the period of 21 years since Mr Posgate had been an active underwriter [see paragraph 215], reached the conclusion that his evidence on the materiality of the fraud allegations in the pending criminal and civil proceedings could not be accepted [see paragraph 217].

29. The judge did however find the evidence of Mr Hall "entirely convincing" [see paragraph 217].

30. Mr Goldstone did not seek to support Mr Posgate's stance on moral hazard in the context of a war risks policy, but he did argue that there was something special about a war risks policy basing his argument on answers he had obtained from Mr Hall in cross-examination. He suggested that Mr Hall had conceded that so far as war risks were concerned there was only one "moral hazard", the bombing of the vessel.

31. Mr Hall accepted that under the terms of the war risks policy the only peril that could possibly be the subject of a simulation was clause 1.5 covering "any terrorist or any person acting maliciously from a political motive". Mr Goldstone then suggested that "realistically it is only really bombing that could be the subject of simulation under this clause. Can you think of any other examples?" to which Mr Hall responded "Not off-hand my lord". Mr Goldstone then suggested that even if there was a question mark over an assured's probity "it is a pretty far cry from that to a concern that the assured might blow his own ship up". Mr Hall's response was that it was "but I don't think it is out of the question". After being pressed further by Mr Goldstone to concede that the risk potential for fraudulent claims on a war risks policy was much lower, Mr Hall whilst accepting it was lower said "I can only reiterate . . . . that any moral hazard is moral hazard and, as such, a consideration for any prudent underwriter, whether it be under a Hull policy, War policy, as I said earlier, Cargo policy or any other policy." The judge asked him, at the end of his evidence, why he had said that it would have to be done by a bomb. His answer was: "I think it is the most likely. As I said, offhand I can't think of any other way that anything would do sufficient damage as to make the claim meaningful".

32. On the basis of these answers Mr Goldstone submitted that Mr Hall had accepted that in essence the moral hazard relevant to a war risks policy was a risk that the insured would bomb his vessel, and that thus dishonesty in relation to the taking of clients' money would not be something which an underwriter would take into account in writing a war risks policy.

33. Mr Hamblen pointed out in his submissions that he had explored with Mr Posgate other aspects of moral hazard e.g. exaggeration of a claim, production of false documents to support a claim, concealment of facts so as to avoid payment of additional premium etc. He, in any event, submitted that it would not be fair to construe Mr Hall's evidence as limited in some way.

34. In my view Mr Goldstone's cross-examination does not entitle him to say that the evidence of Mr Hall should in some way be limited, and the judge was right not to so construe it. Under skilful cross-examination Mr Hall had his attention directed to the moral hazard of an owner bombing his ship as being the most significant risk of a fraudulent claim. But the reality is that Mr Goldstone had an impossible task in seeking to persuade the judge, without any expert evidence of his own to support it, that Mr Hall's evidence should be rejected, and that allegations of serious dishonesty the subject of criminal charges in Greece should be found not to be material.

35. Does the SFO letter undermine that conclusion? The judge thought that there were difficulties in taking exculpatory material into account in considering materiality as opposed to considering inducement [see para 206 to 210]. His view was that serious allegations of fraud would always be material, and it would be for the underwriter then to assess the exculpatory material. I suspect as a practical matter there is force in the judge's view but it would seem to me that it must be possible to have a situation in which it is so clear that there is nothing in the allegation, such as an admission from the person who has made the allegation that he has made a terrible mistake as to identity, that the allegation no longer needs disclosing because it is no longer material.

36. The position in this case however is that the SFO letter does not get near to providing such a clear answer to the allegations. In my view one thing that shows clearly that the SFO letter was not the end of the matter is that, after receipt of that letter by the authorities in Greece, the Greek proceedings continued and the allegations and charges were considered to be of sufficient substance for the judge in Greece in the Sotiriadis proceedings to order in January 1994 the Petrakakos brothers to provide security or bail for their attendance at trial.

37. Once one has formed the view that the allegations would have to be disclosed together with the SFO letter, materiality is established. The only remaining question would be whether the underwriter having taken the allegations and the exculpatory material into account would continue to write the risk on the same terms, but that relates to inducement on which permission to appeal has been refused.

38. In my view the judge's conclusion, based on the evidence of Mr Hall that the charges being made in the Greek criminal proceedings were disclosable, is unimpeachable.

39. The above being my conclusion the appeal must be dismissed on that basis alone. I can accordingly deal with the other matters shortly. The fair summary of the allegation relating to fact 2 produced by Mr Hamblen was as follows:

> "Allegations of fraud have also been made against the Petrakakos brothers' companies in civil proceedings in Panama brought by a disaffected former business associate, Mr Robayana, on the strength of which the Panama Court ordered the arrest of the "North Rock", another vessel in the Kent fleet as security for the claim which amounts to US$770,400. It is alleged that an insurance policy relating to one of Kent's ships,

("Ivory K") was endorsed to that business associate but that it was fraudulently concealed that the policy had previously been endorsed to a bank which had a prior claim. It is also alleged that the ownership of the "North Rock" was transferred in such a way as to defraud the business associate. The Petrakakos brothers deny the allegations and are confident that the claims will be thrown out. The vessel has recently been sold by the mortgagee bank to a company in which the Petrakakos brothers have a 50% interest and is no longer under arrest."

40. The judge quotes Mr Hall's evidence which was as follows:-

> "I believe that in this case the arrest and the underlying allegations ought to have been disclosed for two reasons.
>
> Firstly, I understand that in the Panama proceedings there were allegations of fraudulent behaviour, in particular an allegation that an insurance policy had been dishonestly assigned. I have to say that if I had learned of such an allegation of dishonesty, particularly relating to an insurance policy, I would have refused the risk without a second thought. I would not have wanted to do business with this client for the very reasons relating to moral hazard discussed above. I am confident that any prudent underwriter would do the same.
>
> Secondly, it would be relevant to the financial position of the beneficial owners of that vessel, who I believe were the same as the owners of the "North Star". A prudent underwriter, having been provided with this information would made further enquiries to establish whether this was a one-off arrest, which had no bearing on the financial position of the proposed insured, or whether it either signified an underlying financial problem or was likely to cause the insured financial difficulties. The outcome of these enquiries would certainly have influenced the judgment of that prudent underwriter.
>
> In reality, given the low premium, high turnover nature of war risk business, although he would ask the broker, I doubt that a prudent underwriter would wish to undertake his own detailed enquiries. I expect he would decide not to take the risk, particularly if the market was firm from the underwriter's point of view, which, as I recall, it was in 1994."

41. Having noted that Mr Hall had said nothing which detracted from that evidence in cross-examination the judge concluded:-

> "I accept this evidence. In my judgment the prudent underwriter would not have embarked on a detailed evaluation of the complicated facts underlying the arrest of the North Rock

> or the Panamanian proceedings in general. The kind of cursory consideration to be expected from underwriters of exculpatory information from the brokers with regard to those proceedings would not have led to the allegations of fraud being regarded as immaterial, particularly on the assumption, which has to be made, that there had been full disclosure of the Greek criminal proceedings."

42. I would have had some concern about Mr Hall's suggestion that because what had allegedly been fraudulently assigned was an insurance policy, that would have been more worrying than an alleged fraudulent assignment of any other instrument. I was also concerned as to the judge's reliance on the fact that some additional ground for the materiality of the allegations in the Panamanian proceedings followed from the fact that disclosure of the Greek criminal proceedings would have been made. But on reflection, first it seems to me that both Mr Hall and the judge had in mind allegations of fraudulent behaviour, which included not just a fraudulent assignment (or more accurately a dishonest concealment of an endorsement) but also alleged fraudulent transfer of the North Rock. Furthermore it seems to me that if one envisages disclosure of the allegations being made in the Greek criminal proceedings together with exculpatory material, plus a denial of dishonesty, in that context the judge is right in taking the view that a different allegation of dishonesty by another third party would become material, even if, arguably, it had not been material on its own.

43. It seems to me that the judge is finding both that the allegations of fraud in the Panamanian proceedings would be disclosable on their own, and the more so if one makes assumptions as to what would have been disclosed in relation to the allegations being made in the Greek criminal proceedings. That is a finding, it seems to me, that he was entitled to make on the evidence and I would dismiss the appeal on this aspect also.

44. As regards excessive overvaluation the summary of Mr Hamblen was as follows:-

> "Although the market value of the vessel is only about US$1.4 million there are good ship management reasons for the Owners valuing her at US$3 million, and they would like to insure her for US$4 million, her insured value under her expiring policy."

45. That summary demonstrates what the allegation of non-disclosure came to on the judge's findings. The insurers could not ultimately make good a case that because the vessel was insured for $4 million, when its true value was US$ 1.35 million, an excessive over-evaluation was established.

46. I have doubts whether, taken on its own, I would have agreed with the judge on this aspect. I accept that the relevant test of materiality is whether the disparity between the insured value and the market value is consistent with prudent ship management [his paragraph 224]. Mr Hall's evidence was that there was nothing unusual in a

differential of 10-15% above market value; that an underwriter could be expected to know very roughly the market value of standard types of vessel such as the North Star; and further that an insured value of US$4 million would not have raised an underwriter's eyebrow.

47. The market value of the North Star as at April was agreed at $1,350,000. Mr Goldstone's simple point is that an underwriter knowing the market value roughly would appreciate the difference between $4 million and $1.35 million, and ask questions if he were interested in finding out what the reasons were for the differential. The judge indeed found that there were good management reasons for a value of $3 million, and it was the extra million "which went beyond that level and was effected only because it was the previous year's level and with regard to the Hull and Machinery level". [This last comment refers to the fact that the hull and machinery policy had an insured value of $4 million to pay $3 million.] So in essence (as Mr Hamblen's summary recognises) the judge was finding that the non-disclosure was of there not being good management reasons for $1 million.

48. The judge and Mr Hall seem to have placed some reliance on the fact that the vessel had been recently sold for $1.1 million as is and $1.4 million with Special Survey complete. The judge expresses his conclusion in these terms:-

> "227. Taken alone and alongside the contemporaneous sale of the vessel for US$1.1 million as is and US$ 1.4 million with Special Survey complete, this was therefore a material fact and certainly taken in conjunction with the Greek proceedings and the Panamanian proceedings it should have been disclosed."

49. I would have thought that the recent sale logically adds nothing to the knowledge that the underwriter has of the market value – the two are almost identical. If the sale has no relevance the underwriter can see for himself that the difference between $4 million and the vessel's market value would raise questions. The underwriter may prefer to take the extra premium rather than investigate whether the good management reasons establish $4 million as opposed to some lesser figure.

50. As regards non-payment of premium, it is not absolutely clear that the judge would have found this fact alone to be material. He seems to conclude it is material when taken with other factors. In so far as those other factors relate to the financial position of the owners, that is a matter which it has been agreed should not be dealt with by us at this stage. In so far as the judge following Mr Hall seeks to suggest the non-payment of premium could become material as a result of the other matters such as the Greek criminal proceedings, I doubt whether that is a legitimate approach. The non payment of premium is either material on its own or not, and since it seems to go to the owner's credit risk, and not to the risk insured, I would have thought it was not material.

51. My conclusion, accordingly, is that I have doubts about the judge's conclusions in relation to fact (3), overvaluation, and fact (4), non-payment of premium, but do not

feel it necessary to reach any concluded view in relation to those matters, having regard to the fact that I would uphold the judge in relation to his decisions on fact (1), the allegations made in the Greek criminal proceedings, and fact (2), the allegations made in the civil proceedings in Panama. For the reasons I have endeavoured to give, the appeal must be dismissed.

Lord Justice Longmore:

52. I agree with Waller LJ, for the reasons he gives, that this appeal must be dismissed.

53. This case does, however, bring into sharp focus the problems of the present state of the law about non-disclosure. We are compelled to conclude, as a result of the expert evidence given to Colman J, that false allegations of fraud made by third parties were material matters to be disclosed to underwriters at the time of placing. While the law remains as set out in section 18 of the Marine Insurance Act that is an almost inevitable conclusion since materiality is a question of fact on which the expert evidence of underwriters is admissible. Most expert underwriters will be likely to say that an allegation of fraud, not shown to be false at the time of placing, was material in the sense of being a circumstance which would influence the judgment of a prudent insurer (such as themselves) in fixing the premium or determining whether he will take the risk. Is it not time that the law was changed at least to the extent that an insured's disclosure obligation should be to disclose matters which the insured knows are relevant to the insurer's decision to accept the risk or which a reasonable assured could be expected to know are relevant to that decision?

54. In 2002 the British Insurance Law Association published a balanced and impressive report saying that reform was necessary and putting forward detailed proposals in the areas of non-disclosure and the draconian remedy of avoidance. It is gratifying to know that the Law Commission has published a Scoping Paper in preparation for a review of insurance contract law and it is much to be hoped that this area of the law will receive the Law Commission's detailed consideration and that proposals emerging from that consideration will be enacted. Australia with its Insurance Contracts Act 1984 is well ahead of the United Kingdom in this field.

Lord Justice Lloyd

55. For the reasons given in both judgments, I agree that the appeal should be dismissed.