INSURANCE WARRANTIES: SOME CRITICISMS AND PROPOSALS FOR REFORM

If insurance is to be an indispensable shield against the uncertainties of the modern age, the law should ensure that the insured is given the cushion he bargained for so long as he has not breached a material term of the contract or misled the insurer into issuing the policy. There is a need for a fair balance to be struck between insurer and insured and the policy must reflect this balance. This need for a balance was clearly in Lord St. Leonard's mind when, in *Anderson* v. *Fitzgerald,* he stressed:

> 'A policy ought to be framed that he who runs can read. It ought to be framed with such deliberate care that no form of expression by which, on the one hand, the party assured can be caught, or by which, on the other, the company can be cheated, shall be found upon the face of it'.[1]

Alas, the law has not played its part. While some efforts are being made in other branches of contract law to redress imbalances in bargaining power between contracting parties, little or nothing is being done in the field of insurance law where much needs to be done. Foremost among the sores for which legislative poultice is required is the law on insurance warranties which is, to many an unsuspecting insured, his Sword of Damocles.

An insurance warranty differs radically from the usual contractual warranty. It is a term which must be exactly and literally complied with, failing which the insurer may repudiate the entire contract.[2] That a breach is immaterial, is unconnected with the loss or has been remedied before loss is irrelevant.[3] For rigidity and harshness, this rule has no peer. It is inevitable, then, that some judges would over-

1 (1853) 4 H.L.C. 484, 510.

2 Use of the term 'warranty' sometimes leads to confusion. Strictly speaking, it is a term which must be exactly and literally complied with. A non-promissory warranty is one that is outside the rule on exact and literal compliance. Donaldson J. explains the position rather succinctly in *de Maurier (Jewels), Ltd.* v. *Bastion Insurance Co., Ltd.* [1967] 2 Lloyd's Rep. 550, 558 as follows:—

> "The warranty (here) delimits and is part of the description of the risk and is not of a promissory character. By a warranty of a promissory character, I mean a warranty by the assured that a particular state of affairs will exist, breach of which destroys a substratum of the contract and entitles the underwriter to decline to come on risk or, as the case may be, to terminate the risk as from the date of breach. In the marine field, 'warranted free from capture and seizure' is a warranty of the former character leaving the contract effective in respect of loss by other perils. 'Warranted to sail on or before a particular date' is, however, of a promissory character, breach of which renders the contract voidable."

Throughout this article, unless the context otherwise requires, an insurance warranty refers to the type which must be exactly and literally complied with,

3 In regard to marine insurance, s. 34(2) of the Marine Insurance Act 1909 states that the assured cannot avail himself of the defence that the breach has been remedied and the warranty complied with, before loss. See *Quebec Marine Insurance Co.* v. *Commercial Bank of Canada* (1870) L.R. 3 P.C. 234.

strain canons of construction, to the chagrin of insurers, to achieve just results. This, of course, has led to confusion. Far too often, the state the law is in has been attributed to the tussle between humane judges and stubborn insurers. This is an oversimplification of the matter. Insurers, in their zeal to inundate their policies with warranties so as to avoid the difficulties of pleading misrepresentation, did create problems but much of the confusion that exists is the result of the tussle between those judges who would strain canons of construction, those who would not and those who did not know what to do.

Before prescribing reforms, it would be instructive to review the history of the development of the insurance warranty.[4] What can be unravelled is a woeful tale of judicial myopia which resulted in the creation of the insurance warranty followed by judicial ineptitude at either reining in or obliterating what had become an embarassment to the law. There is no more convenient point to begin than with the views of Lord Mansfield, the 'father' of the insurance warranty. Lord Mansfield was determined that some descriptive statements of the risk should have greater effect than other statements. Statements that a ship was seaworthy, was neutral or was sailing in a convoy ought not to be taken lightly. No one can quarrel with the need for such a distinction. However, the existing classification of contractual terms was more than adequate for this purpose. For instance, a statement that a ship would be part of a convoy could be treated as a condition precedent of the contract. For no sound reason, the label 'insurance warranty' was brought into the picture. To ensure that such warranties were not confused with the usual contractual warranties, Lord Mansfield defined an insurance warranty in the following broad terms in *De Hahn* v. *Hartley:*

> 'A warranty in a policy of insurance is a condition or a contingency and unless that be performed, there is no contract. It is perfectly immaterial for what purpose a warranty is introduced; but being inserted, the contract does not exist unless it be literally complied with'.[5]

Lord Mansfield's approach opened Pandora's box. As it was immaterial for what purpose a warranty was introduced, insurers were free to make trivia the subject matter of their warranties. As for material subjects, immaterial breaches could not be overlooked for

[4] For an interesting account on the historical aspects of the insurance warranty, see Vance, 'The History of the Development of the Warranty in Insurance Law', (1911) 20 Yale L.J., p. 523. Vance blames the confusion in the law on the struggle between judges and insurers. He observed:-

> "The unseemly struggle that ensued between the unwise insurers who sought to frame their policies as to compel the courts to allow them the dishonest benefit of forfeitures unsuspected by the insured, and the courts who sought by liberal construction, and sometimes, distortion of the language of the policies, to do justice in spite of the warranties, resulted in a mass of litigation and confused precedent, the like of which cannot be found in any other field of our law."

[5] 1 T.R. 343. Lord Mansfield's approach has not been fully accepted. It is inaccurate to say that the contract does not exist unless the warranty is literally complied with. The insurer can, if he so desires, waive a breach. Indeed, if he fails to act to repudiate the contract, he may, under certain circumstances, be estopped from repudiating liability. In regard to marine insurance, s. 33(3) of the Marine Insurance Act 1906 makes it clear that the insurer is discharged as from the date of the breach of warranty but *without prejudice to liability incurred by him before that date.*

there had to be exact literal compliance.[6] A warranty that there were 450 men on board a ship would be breached if in fact there were only 449 men. An additional man, be he sick, wounded, blind or even dying would save the day. On the other hand, a warranty that there were 20 guns on board will be complied with if there were 20 guns on board even though no one knew how to work them.[7] Logic was lost in a web of formality.

Such bad law had best been confined to marine insurance but this was not to be for it was extended to all branches of insurance law and for the poorest of reasons. It was thought that contract law would be subverted if parties were not free to introduce the type of term they so wished.[8] Nothing could be more reasonable than for the parties themselves to decide what was not open to judicial scrutiny. This line of reasoning is symptomatic of judicial myopia. Freedom of contract has never been without limits. It is equally subversive of contract law to have one of its branches out of line in regard to so fundamental a concept as classification of contractual terms. Apart from the fact that the insurance warranty is, in the context of contract law, an anomaly, it should be borne in mind that it is not the parties themselves but the insurer himself who, in the main, decides what warranties to incorporate into the contract.

If the introduction of the insurance warranty was the first mistake, the second lay in the development of the law relating to mode of creation of such warranties. In view of their lethal nature, there ought to have been stringent control over the mode of creation. On this, there seemed to have been full agreement for courts have consistently stressed that clear and unambiguous words are required for the creation of such a term. As Lord Buckmaster explains, 'it is at least essential that the bargain should be plain in order that it may be clear that a man has contracted on the faith of something which may rob the insurance of the greater part of its value'.[9] Zealousness did not bring desired results for it is evident that the mode of creating warranties in the field of non-marine insurance leaves much to be desired.[10]

Non-marine insurance warranties may be created in one of two ways. Firstly, as a general rule, a term is only regarded as a warranty if it has been unquestionably expressed as such or when, as a matter of business sense, it was intended to be one. Secondly, answers to questions in a proposal form incorporating the basis clause are usually

6 In *De Hahn* v. *Hartley* (1786) 1 Term Rep. 343, Ashhurst J. declared "The very meaning of a warranty is to preclude all questions whether it has been substantially complied with; it must be literally so."

7 *Hide* v. *Bruce* (1783) 3 Doug. 213. This was a decision by Lord Mansfield. Situations in which the insured benefits from the rule of exact compliance are, of course, rather rare. Where they do occur, they often illustrate the ridiculousness of the rule.

8 *Per* Lord Watson in *Thomson* v. *Weems* (1884) 9 App. Cas. 671, 689.

9 *Provincial Insurance Co., Ltd.* v. *Morgan* [1933] A.C. 240, 247.

10 The mode of creating marine insurance warranties is, by comparison, far more satisfactory. S. 35(2) of the Marine Insurance Act 1909 provides that an express warranty must be included in, or written upon, the policy, or must be contained in some document incorporated by reference into the policy.

regarded as warranties.[11] My quarrel is with the latter of the two modes. There is no reason why insurers should be given a *carte blanche* to create warranties *en masse* with the basis clause. If what amounts to a warranty is a matter of construction, each and every answer in the proposal form should be strictly construed to see whether, in the circumstances of the case, a warranty had been intended. As most people are perfectly capable of making at least one technical mistake while answering the deluge of questions in the usual proposal form, the present law allows the insurer to point to at least one warranty to avoid the policy if and when he so chooses. Obviously, our courts have been unnecessarily overawed by the fact that the basis clause purports to make every answer in the proposal form the foundation upon which the whole contract rests. This need not have been so for the basis clause could have been regarded as having done nothing more than making it clear that the proposal form initiated the transaction and it was in response to it that the insurance policy was issued.[12] Indeed, it is absurd that every answer in a proposal form should be a warranty merely because of the basis clause. Besides, if there is any ambiguity, the *contra preferentem* rule should be applied in favour of the insured.[13]

The common law has not quite come to terms with the basis clause. After holding that the basis clause created warranties *en masse,* it lacked the stomach to digest every consequence of this rule. Judges, without the slightest blush, soon began to decide which of the answers in the proposal form could be warranties and which could not. The original arguments which breathed life to the basis clause were conveniently side-lined.

Dawsons v. *Bonnin* [14] mirrors in its entirety judicial confusion in regard to this. In this case, the insurer repudiated liability because the insured did not garage his car at the place stated in the proposal form. The majority (Viscount Cave, Viscount Haldane and Lord Dunedin) in the House of Lords held that as this statement was made in a proposal form which incorporated the basis clause, the only issue left to be resolved was whether the vehicle was or was not garaged at the place warranted. Any other approach would derogate from the basis clause. The fact that the insurer benefitted because the car had been garaged in a safer place than that warranted in the proposal form was held to be irrelevant. Viscount Haldane explained:

> 'The result may be technical and harsh but if the parties have so stipulated we have no alternative, sitting as a Court of justice, but to give effect

11 The following is an example of a basis clause:—
"I hereby declare and warrant that the above questions are fully and truthfully answered and that I have not withheld or concealed any circumstance affecting in any way the proposed insurance. I agree that this declaration and the answers above given shall be the basis of the contract between me and the company."
For a criticism of such clauses, see R.A. Hasson (1971) 34 M.L.R. 29.

12 This approach was supported by Lord Wrenbury and Viscount Finlay in *Dawsons* v. *Bonnin* [1922] 2 A.C. 413, 437. Their Lordships regrettably failed to persuade the majority to adopt this sensible approach.

13 In *Dawsons* v. *Bonnin (ibid.),* Viscount Finlay argued "The policy is put forward by the underwriters and it must be construed *contra proferentes.* If its effect is ambiguous, it must be read in favour of the assured." How this simple principle was found inapplicable in the case itself is beyond comprehension.

14 [1923] 2 A.C. 413.

> to the words agreed on. Hard cases must not be allowed to make bad law'.[15]

However, Viscount Haldane himself undermined the supremacy of the basis clause when in his next breath, he conceded that it may well be that a mere slip in a Christian name, for instance, would not vitiate the answer given if the answer was in substance true and unambiguous.[16] This has been interpreted to mean that reasonable effect must be given to the terms of a warranty.[17] Such an interpretation is patently wrong for in the harsh world of the insurance warranty, reasonableness is apparently irrelevant. Viscount Haldane ought to have made up his mind. The basis clause must be taken for what it is. If it purports to make every answer the foundation of the contract, it must convert every answer into a warranty or it lacks sense. It is not the business of the courts to re-write the terms of the basis clause for the insurer.

Implicit in Viscount Haldane's judgement is the view that only very inconsequential matters could avoid the suffocating hold of the basis clause. It is therefore highly disturbing that neither his Lordship nor any of the other Lords in *Dawsons* v. *Bonnin* chose to refer to, let alone comment on, *Farr* v. *Motor Traders' Mutual Insurance Society*[18] where the Court of Appeal circumscribed the limits of the basis clause in a manner which left no doubt that it had been undermined. In this case, the owner of two taxi-cabs stated in the proposal form that each cab was to be used for only one shift per day. While one cab was under repair, the other was used for two shifts. After the cab had been repaired, both cabs resumed their normal shift duties. Shortly thereafter, the cab which had been used for two shifts was damaged. The insurer, not surprisingly, denied liability on the ground that the warranty relating to shift duties had been breached. Although the jury agreed that running a cab for two shifts increased the risk run by the insurer and although the rate of premium would have been increased if more than one shift was to be involved; Rowlatt J. held that despite the presence of the basis clause, the answer relating to number of shifts was not a warranty. It merely described the risk run by the insurer. While the cab was run in one shift, the risk attached and while the cab was run in two shifts, the policy was ineffective. The insurer naturally appealed against this 'strange' decision but Rowlatt J.'s judgment was unanimously upheld by the Court of Appeal. Bankes LJ. made it quite clear that despite the presence of a basis clause in a proposal form, one was entitled to consider the *nature* of the question in order to determine whether a warranty had, in fact, been created.[19] While this determined effort to rein in the basis clause is to be welcomed, it cannot be denied that it mauled the oft-established meaning of the basis clause.

How this decision escaped the attention of the House of Lords in *Dawsons* v. *Bonnin*,[20] especially when it was referred to by counsel

15 *Ibid.,* 424.
16 *Ibid.,* 425.
17 See, for instance, *The South African Law of Insurance,* (2nd ed., Gordon, Juta & Co., Ltd., 1969).
18 [1920] 3 K.B. 669.
19 *Ibid.,* 674.
20 [1922] 2 A.C. 413.

in the course of argument, is beyond comprehension. The deafening silence of the House of Lords in the face of the Court of Appeal's decision could only encourage insurers to submit that in view of *Dawsons* v. *Bonnin, Farr* v. *Motor Traders Mutual Insurance Society*[21] could no longer stand. The opportunity for the House of Lords to sort things out came in *Provincial Insurance Co.* v. *Morgan*.[22] In this case, the insured stated in the proposal form that the purpose of his lorry was to deliver coal. One day, the lorry was loaded with both coal and timber. Fortuitously for the insured, the lorry was involved in an accident after the timber had been delivered. The material issues were clearly indistinguishable from those in *Farr* v. *Motor Traders Mutual Insurance Society.* Instead of over-ruling the Court of Appeal, the House of Lords chose to give its blessing to the lower court's approach. Despite the presence of the basis clause and the fact that a higher premium would have been charged had the lorry not been a mere coal cart, it was held that the answer in issue was not a warranty. It merely described the risk and the policy was to remain ineffective while the lorry was used for purposes other than the carting of coal. To their Lordships, *Dawsons* v. *Bonnin* was distinguishable. Lord Wright declared that the condition in *Dawsons* v. *Bonnin* was expressed in clear and unambiguous terms and was clearly broken whereas in this case, the contrary was the fact.[23] Lord Russel thought that if the answer here was to be regarded as a warranty, we would be condoning some form of commercial shorthand which he could not understand.[24] Lord Buckmaster suggested that *Dawsons* v. *Bonnin* presented a special state of facts whereas in this case, it could be seen that a statement that a vehicle was to be used for a particular purpose was not the same as one that it was to be used exclusively for that purpose.[25] Too many writers have accepted without question the distinction between *Dawsons* v. *Bonnin* and the so-called 'description of the risk' cases when in fact, the distinctions offered by the House of Lords in *Dawsons* v. *Bonnin* cannot be countenanced. There was nothing special about the facts in *Dawsons* v. *Bonnin* and the question and answer in that case were neither clearer nor more ambiguous that those in *Provincial Insurance Co* v. *Morgan.* Evidently, commercial shorthand was understood in one case but not in the other.

The House of Lords was clearly trying in *Provincial Insurance Co.* v. *Morgan* to manoeuvre a path for itself out of the morass of its earlier decisions. As a result of its welcomed reiteration of the fact that judges ought to be vigilant in applying the rule of construction so that warranties are not created out of ambiguous terminology, the basis clause undoubtedly suffered a measure of attrition. While it is gratifying that the effect of the basis clause has been pruned,[26] it is nonetheless preferable that having been freed of its earlier constraint that it cannot over-rule itself, the House of Lords would tackle the problem at the root and take the earliest opportunity to rule that the

21 [1920] 3 K.B. 669.
22 [1933] A.C. 240.
23 *Ibid*., 255.
24 *Ibid*., 250.
25 *Ibid.,* 247.
26 A more recent application of this approach may be seen in *de Maurier (Jewels) Ltd.* v. *Bastion Insurance Co., Ltd.* [1967] 2 Lloyd's Rep. 550.

basis clause is an ineffective mode of creating warranties. Until and unless it is accepted that the subject matter of insurance warranties ought to relate to material matters, this rule would allow the rule of construction an unfettered role in checking the proliferation of immaterial warranties through the medium of the basis clause.

Proposals for reform

That the law on insurance warranties is in dire need of a thorough overhaul is hardly debatable. What is in issue is the direction and shape of reforms. There are no simple solutions. The diversity of approaches adopted by the jurisdictions which have dealt with the matter and the criticisms levelled at the approaches taken attest to this.

Any meaningful reform of this area of law should take into account the following principles:—

(a) *A warranty will be regarded as a term of the contract but it will be subject to the doctrine of substantial compliance.*

Much of the injustice encountered stems from the fact that a warranty must be exactly and literally complied with. As this rule is most open to abuse, it must be abolished. There are at least two ways of achieving this end. One way is to regard all statements made by or on behalf of the insured as representations. This would eliminate the insurance warranty as is presently understood and bring into play the rules on *uberrima fides.* This approach is regrettably defective in that it is manifestly unfair to insurers who should be entitled to regard certain statements of the insured as sufficiently important to be incorporated as terms of the contract. Besides, the law on *uberrima fides* is rather unsatisfactory and in urgent need of reform. This approach would thus create as many problems as it solves.

The better approach would be to treat the insurance warranty as a term of the contract but make it subject to the doctrine of substantial compliance. An insured who has substantially complied with a warranty will not be in breach. This sensible doctrine is succinctly summed up in an American decision, *Houghton* v. *Manufacturer's Mutual Fire Ins. Co.* by Shaw J. as follows:

> 'By a substantial compliance, we mean the adoption of precautions … intended to accomplish the same purpose and which may be considered equally or more efficacious. For instance, when it stated that ashes are taken up in iron rods, it would be a substantial compliance if brass or copper were substituted. So when it is represented that casks of water, with buckets are kept in each story, if a reservoir were placed above with pipes to convey water to each story, and found by skillful and experienced persons to be equally efficacious, it would be a substantial compliance'.[27]

(b) *An insurer can avoid a policy on the ground of breach of warranty only if that warranty prejudiced him.*

A major flaw in the present law is that trivial matters can be made the subject matter of insurance warranties. Some jurisdictions attempt to rectify this by making it clear that violation

[27] 49 Mass. 114, 122, 41 Am. Dec. 489 (1844).

of an immaterial warranty does not avoid the contract. One should go a step further by making it clear that a warranty is material only when the insurer has been prejudiced by it. In every case of increase of risk, the insurer will be protected. However, when there is an allegation of intent to deceive, it must be shown that the insurer has been prejudiced.

(c) *Breach of a warranty will not avoid a policy unless the breach exists at the time of avoidance.*

This rule will ensure that an insured who has rectified a breach of warranty will no longer be at the mercy of the insurer who at present can avoid the policy even though the breach has been rectified before loss.

Apart from the above, additional measures are required for life insurance contracts.[28]

The age of the life assured is of course a material factor in life insurance. However, as the insurer invariably requires the assured to have a medical examination before agreeing to accept the risk, a mis-statement of age need not avoid the policy. Adjustments can be made in regard to premiums payable by the assured and sums payable by the insurer under the policy. As for other mis-statements, there ought to be a limitation period for non-fraudulent statements, after which the insurer cannot avoid the policy. These proposals are no doubt weighed in favour of the assured but it is in life insurance that the common man requires the greatest measure of protection.

In the last analysis, law reform, and especially reform of insurance law, has never been easy. Anachronisms and anacoluthona have often been tolerated in insurance law because of judicial reluctance to tamper with terminology understood for centuries by judges and merchants. However, the injustice perpetuated by the insurance warranty has exacted too high a price. No one need regret the reining in of the insurance warranty. If anything, apologies are due for the decades of inaction.

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28 In regard to this, the Australian approach merits close scrutiny and attention. Its principles have been adopted in Malaysia. See s. 83 and s. 84 of the Australian Life Insurance Act.

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