Versloot Dredging v HDI Gerling

Hindsight is a wonderful thing…

In Versloot Dredging BV and another v HDI Gerling Industrie Versicherung AG and others (the DC Merwestone), the vessel suffered catastrophic engine damage due to crew negligence in failing to close the sea suction valve and drain a pump. Owners claimed over €3.2m for a new engine under their hull and machinery policy. Their claim was supported by what was later found to be a fraudulent representation from their general manager that the crew had reported hearing a bilge alarm (which would have alerted the crew to the flooding) at noon on the day of the casualty but had failed to investigate the alarm on the basis that its sounding had been attributed to the rolling of the vessel.

At first instance, the statement was found to be irrelevant to the claim since the damage to the engine was found to have been caused by a peril of the seas. Popplewell J nonetheless held that the manager's lie was a "fraudulent device" entitling the insurers to reject the claim. The Court of Appeal agreed.

In short, the issue before the Supreme Court was whether insurers were entitled to avoid paying on the ground that the insured had told a lie in presenting the claim, if the lie later proved to be irrelevant to the insurer's liability. Deeming the expression "fraudulent device" to be archaic, Lord Sumption preferred to refer to "collateral lies". However the doctrine was renamed only to be immediately abolished. The Court allowed the owners' appeal by a majority of 4 to 1, holding that the "fraudulent claim" rule does not apply to collateral lies which are immaterial to the insured's right to recover. In other words, the answer to the question of whether the fraudulent claims rule applies to justified claims supported by collateral lies is – no. In so holding the Supreme Court overruled the (*obiter*) decision of the Court of Appeal in *Agapitos v Agnew* [2002] 2 Lloyd's Rep.42, which had been the leading authority on the point – and no doubt the foundation of numerous settlements.

The fraudulent claim rule is not wholly abolished. It still applies to entitle the underwriter to reject a fraudulently exaggerated claim in full. That is, if the assured presents a claim which is in principle justified, but deliberately exaggerates the quantum, then the whole claim is forfeit, not merely the exaggerated part.

In a dissenting judgment, Lord Mance (who, as Mance L.J. had given the leading judgment in *Agapitos v Agnew*) recognised that in relatively rare cases, like the present, where the insured pursues a claim to trial having told a lie in presenting the claim and is found after the event to have had a sound claim, it may seem harsh that the insured loses everything. However, the Judge went on to remind the Court that public policy must by definition look at the position overall, as the core fraudulent claim rule does. In his own words, abolishing the fraudulent devices rule "*is a charter for untruth*", which overlooks the imperative for integrity in an

insurance relationship and the reality that lies are almost always told to obtain an unmerited advantage.

This judgment has significant implications for insurers, not least for the reasons given by Lord Mance. Insurance policy wordings may need to be reviewed to ensure provision is made for the effect of collateral lies by the assured on the claims handling process.

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