Neutral Citation Number: [2015] EWHC 1000 (Comm)

Case No: 2010 Folio 1045

IN THE HIGH COURT OF JUSTICE
QUEEN'S BENCH DIVISION
COMMERCIAL COURT

Royal Courts of Justice, Rolls Building
Fetter Lane, London, EC4A 1NL

Date: 23 April 2015

Before :

MR JUSTICE EDER

- -

Between :

TEAL ASSURANCE CO LTD

Claimant

- and -

(1) W R BERKLEY INSURANCE EUROPE LTD
(2) ASPEN INSURANCE UK LTD

Defendants

- -
- -

Mr Christopher Butcher QC and Miss Rebecca Sabben-Clare QC (instructed by **DAC Beachcroft LLP**) for the **Claimant**
Mr Colin Edelman QC and Ms Alison Padfield (instructed by **Clyde & Co LLP**) for the **Defendant**

Hearing dates: 4 March 2015
Further written submissions received: 6, 10 & 12 March 2015

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Approved Judgment

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MR JUSTICE EDER

Mr Justice Eder:

Introduction

1. This is a trial of certain preliminary issues in relation to disputes arising between the claimant ("Teal") and its defendant reinsurers (the "Reinsurers"). In essence, the questions concern the time at which, and therefore the order in which, insured losses were suffered for the purpose of a programme of professional indemnity insurance and reinsurance.

2. For the purpose of these preliminary issues, the parties have agreed a Statement of Facts. The following summary is taken largely from that document.

3. Teal is an insurance company incorporated in the Cayman Islands. It is wholly owned by the Black and Veatch Holding Company and is one of the Black & Veatch group of companies. The Reinsurers are reinsurers of the Top & Drop layer of Black and Veatch's professional indemnity insurance as further described below.

4. Black and Veatch Corporation ("BVC") is another corporation in the same group of corporations and is incorporated in Delaware. BVC is a major engineering company providing professional advice and services and carrying out engineering, procurement and construction contracts in various parts of the world either by itself or through subsidiary or associate companies and either on its own or in joint venture with others. All references below to "BVC" are to all Black & Veatch group companies, as the context requires.

5. Teal is a captive insurer i.e. its sole business is the insurance and reinsurance of the interests of members of the Black & Veatch group of corporations.

6. During the relevant period i.e. 1 November 2007 to 1 November 2008 (the "policy period"), BVC's professional indemnity insurance programme for the policy period comprised of 5 layers, as follows.

The Lexington policy

7. The bottom layer of the programme was a contract of insurance of BVC underwritten by Lexington Insurance Corporation and contained in or evidenced by policy no. 0101085 (the "Lexington policy" or "Primary policy"). The Lexington policy provided professional indemnity insurance to BVC subject to a per claim deductible of US$100,000, a per claim self-insured retention of US$10 million and an aggregate self-insured retention per policy period of US$20 million. The limit under the Lexington policy was US$5 million per claim and in the aggregate.

8. The Lexington policy provided in material part as follows:

> "…
>
> *1. INSURING AGREEMENT - COVERAGE*
>
> …

The Company will indemnify the Insured all sums up to the Limits stated in the Declarations, in excess of the Insured's Deductible and/or Self-Insured Retention, which the Insured shall become legally obligated to pay as Damages if such legal liability arises out of the performance of professional services in the Insured's capacity as an architect or engineer and as stated in the Application provided:

…

V. SETTLEMENT

The Insured shall not settle any Claim without the informed consent of the Company, such consent not to be unreasonably withheld.

…

VI. ACTION AGAINST THE COMPANY

No action shall lie against the Company unless, as a condition precedent thereto, the Insured shall have fully complied with all the terms of this Policy, nor until the amount of the Insured's obligation to pay shall have been finally determined either by judgment against the Insured at the actual trial, arbitration or by written agreement of the Insured and the claimant, to which agreement the Company has consented.

…

ENDORSEMENT # 008

…

DESIGN BUILDER'S INDEMNITY ENDORSEMENT

Endorsement Specific Deductible: $250,000.00

In consideration of the premium charged, it is hereby understood and agreed that the coverage provided under this policy is modified as follows:

In addition to the coverage granted under this Policy, but subject to the same Self-Insured Retention and limits of liability, we agree to indemnify the Named Insured for the Named Insured's Actual and Necessary Costs and Expenses incurred in rectifying a Design Defect in any part of the construction works or engineering works for any project upon which you are providing design/build services provided …"

The upper layers of insurance

9. The next 3 layers were contracts of insurance of BVC underwritten by Teal (together the "tower policies"). The 3 layers were as follows:

    i) By policy No. 2007-009, a contract of insurance subject to a limit of US$5 million in aggregate, excess of US$15 million in aggregate (i.e. excess of the Lexington policy).

    ii) By policy No. 2007-010, a contract of insurance subject to a limit of US$30 million in aggregate, excess of US$20 million in aggregate (i.e. excess of the first tower policy).

    iii) By policy No. 2007-011, a contract of insurance subject to a limit of US$20 million per in aggregate, excess of US$50 million in aggregate (i.e. excess of the second tower policy).

10. The 5th layer comprised a contract of "top and drop" insurance, which was underwritten by Teal (the "Top and Drop policy"). The Top and Drop policy was contained in or evidenced by policy document no. 2007-012. In essence, it provided insurance to BVC subject to (i) a limit of GB£10 million or its equivalent in other currencies, excess of the Lexington policy and the tower policies; and (ii) an exclusion in respect of claims emanating from or brought in the USA or Canada.

11. All these upper layers i.e. the tower policies and the Top and Drop policy were, in effect, on terms substantially similar to the terms of the Lexington policy.

The Reinsurance of the Top and Drop policy

12. By a contract of reinsurance contained in or evidenced by a slip policy No. Y0050790U (the "contract of reinsurance" or the "Excess Policy"), the Reinsurers agreed to reinsure Teal in respect of its liability under the Top and Drop policy. Like the Top and Drop policy, the contract of reinsurance was subject to a per claim limit of GB£10 million or its equivalent in other currencies. The contract of reinsurance was subject to the same terms and conditions as the Top and Drop policy in relation to coverage, including the exclusion in respect of claims emanating from or brought in the USA or Canada.

Summary of claims faced by BVC during the Policy Period

13. During the policy period, BVC faced a number of claims, as follows:

    i) PPGPL: This is a substantial non-USA claim arising from BVC's design, procurement and construction of an expansion project at a gas processing plant in Trinidad.

    ii) Providence, Water One and City of Clovis: These are small US based claims.

    iii) FRP: This is one of two US based claims that arise from contracts between BVC and a company known as AEP or its subsidiaries to design, procure and install wet flue gas desulphurisation systems at AEP's power stations. Fibre Reinforced Thermostat Plastic failed as a result of a design defect, namely a lack of support.

iv) Ajman: This is the second non-USA claim and arises out of the failure of a waste water treatment plant to process sewage to its contractual specification.

v) JBR Internals: This is the second AEP, and therefore US based, claim and the largest of the claims, arising out of failure of jet bubble reactors in the USA.

14. Thereafter, BVC paid out various sums on remedial works in respect of these claims details of which were summarised in a Schedule attached to the Statement of Facts setting out the amount of such payments and the month in which they were incurred. At this stage, the Reinsurers make no admissions as to the accuracy of this Schedule but it is to be presumed accurate for the purposes of these preliminary issues.

History of proceedings

15. These proceedings were originally commenced in 2010. At that time, Teal contended as its primary case that it was entitled, under the insurances, so to order its claims as to enable the non-USA claims, namely PPGPL and Ajman, to fall within the Top and Drop policy.

16. That question was tried by Andrew Smith J as long ago as 2011 as the First Preliminary Issue. In essence, he found for the Reinsurers and held that the contracts of insurance within BVC's professional indemnity insurance programme responded to claims by reference to the order in which the original assured (i.e. BVC) suffered insured loss: see [2011] EWHC 91(Comm). The Order made by the Judge following that Judgment and dated 31 January 2011 is in material part in the following terms:

> "*On the true construction of the Excess Policy, the Excess Policy responds by reference to the order and timing of the establishment and ascertainment of an original Insured's liability or of the incurring of costs and expenses falling within the ambit of Endorsement 008 to the Primary Policy by an original insured to provide indemnity only upon exhaustion of the limits of liability of the underlying p.i.tower and an original insured thereafter becoming liable to make any payments in respect of any claims against it or incurring such costs and expenses, subject to the exclusion of US and Canadian claims and losses and subject to all other applicable policy terms and conditions.*"

17. The decision of Andrew Smith J was upheld by the Court of Appeal: see [2011] EWCA Civ 1570; and the Supreme Court: see [2013] UKSC 57.

18. In light of those judgments, Teal revised its case. As already noted, the Schedule sets out BVC's expenditure on remedial works as it occurred on a monthly basis. The left-hand columns of the Schedule set out the claims and the amounts paid out by BVC by month. The right hand columns show the resulting exhaustion of the deductibles, self-insured retention, the tower policies and finally the Top & Drop policy on the basis that exhaustion of the insurances occurs as BVC incurs expenditure.

Ajman

19. BVC were part of a consortium which constructed a sewage system for the emirate of Ajman. BVC were responsible for process, design and construction of the waste water treatment plant (less the civil engineering work). The plant was required by the construction contract to achieve a standard of effluent known as 10/10. It did not achieve that standard. Ajman alleged breach of this standard.

20. BVC reached a settlement with its contracting party i.e. Ajman Sewerage (Private) Company Limited ("ASPCL") in December 2010. Part of that settlement required BVC to place a net amount of US$13,460,531 (i.e. US$14 million less US$539,469) into escrow (the "escrow payment") on terms set out in an Escrow Agreement dated 10 December 2010 which provided in material part as follows:

> "*Payment Deed*
>
> …
>
> *Recitals*
>
> …
>
> *D. Under the terms of the MOA, BVGL has agreed to pay ASPCL the Payment.*
>
> …
>
> *It is agreed:*
>
> *1. Definitions and Interpretation*
>
> …
>
> *(g) Payment means an amount not to exceed in aggregate USD 13,460,531 (…) to be paid by the Escrow Agent on behalf of BVGL to ASPCL under the terms of this Payment Deed and the Escrow Agreement.*
>
> …
>
> *2 Payment terms*
>
> *2.1 The Payment or parts thereof are due at the times and in the amounts set out in Appendix 1 and Payments shall be made by the Escrow Agent on behalf of BVGL pursuant to the Escrow Agreement.*
>
> …
>
> *3 Escrow Account*
>
> *3.1 BVGL and ASPCL agree that upon the execution of this Payment Deed they will designate and appoint BNP Paribas*

Securities Services, London Branch as escrow agent upon the terms and in the form of the Escrow Agreement.

3.2 Before the Effective Date, BVGL shall deposit USD13,460,531 in cleared funds (the Escrow Amount) into the Escrow Account.

3.3 BVGL and ASPCL agree that:

(a) any interest accruing in the Escrow Account shall be for BVGL's account and shall be paid by the Escrow Agent to BVGL as set forth in the Escrow Agreement; and

(b) the Escrow Amount shall be held on deposit and not used for making any investments by the Escrow Agent;

and neither BVGL nor ASPCL shall instruct the Escrow Agent otherwise.

3.4 BVGL and ASPCL agree that upon the earliest of (i) ASPCL's agreement that no further payment certificates will be issued under the New Contract; (ii) 2 May 2011 if the New Contract has not been awarded by ASPCL; or (iii) 31 July 2013, the Escrow Agent shall be immediately jointly instructed by BVGL and ASPCL to distribute any remaining funds in the Escrow Account to BVGL and the Escrow Agreement shall be terminated.

3.5 The escrow agent shall at all times be the Escrow Agent, provided that the Escrow Agent has the Required Rating. ASPCL shall monitor the credit rating of the Escrow Agent and shall notify BVGL of any downgrade in the long term financial strength of the Escrow Agent upon becoming aware of any such downgrade.

…

Appendix 1 – Payment Terms

ASPCL shall deliver claims for payment to the Escrow Agent and the Escrow Agent shall make payment on behalf of BVGL in accordance with the provisions of the Escrow Agreement, in the amounts and at the times set out herein, provided that:

(a) the New Contract is awarded on or before 2 May 2011, failing which BVGL shall have no obligation to pay the Payment or any part thereof and such obligation shall become null and void;

(b) in the event the New Contract is awarded on or before 2 May 2011, all claims for payment must be delivered to the Escrow Agent in accordance with the provisions of the Escrow

> *Agreement on or before 31 July 2013, failing which BVGL shall have no further obligation to pay any parts of the Payment in respect of which claims for payment have not already been delivered to the Escrow Agent by ASPCL; and*
>
> *(c) no claim for payment shall be made by or due to ASPCL before the execution of the New Contract or the Effective Date, whichever is the later.*
>
> *Payments shall consist of:*
>
> 1. *US$1,400,000 (…) less US$539,469 within 21 days of BVGL receiving written confirmation from ASPCL of the award of the New Contract.*
>
> 2. *US$1,262,000 (…) within 52 days of BVGL receiving written instructions from ASPCL for the new contractor to commence the works under the New Contract.*
>
> 3. *An amount not to exceed US$ 11,340,000, payable in instalments, such instalments to occur not more frequently than monthly, each instalment subject to independent certification by ASPCL's consulting engineer (Halcrow International Partnership) that the requested instalment amount does not exceed the value of the work performed in the instalment period; each such instalment due within 21 days of BVGL receiving the relevant certifications.*"

21. Pursuant to the Escrow Agreement, BVC paid into escrow on 15 December 2010, the sum of US$13,460,531, credit being given to BVC for US$539,469. Subject to the addition of some late allocations of minor project costs, the escrow monies were thereafter drawn down from time to time as set out in the far right-hand column of the Schedule.

JBR Internals

22. The JBR Internals claim is the second substantial US claim and the largest claim of all. The claim concerns the design specification of BVC's subcontractor of pultruded fibreglass known as "Composolite" to be used as decking material within the JBRs and the failure of that decking material. BVC's contracting party ("AEP") asserted that BVC was in breach of contract by reason of these failures. By a series of agreements made in writing dated 30 July 2010, which took the form of amendments to the underlying contracts for the procurement of the wet flue gas desulphurisation systems at the various plants, BVC agreed with AEP to settle the JBR claim on terms that BVC would replace at its expense the JBR Internals and certain other components. BVC's case is that it would have been obvious as at 30 July 2010 to any informed observer who sought to put a figure on the costs of the work promised by the 30 July 2010 agreement that this would greatly exceed the remaining cover available under the tower policies. To this end, BVC's case is that (i) by early 2010, a detailed estimate for repair had been prepared in the sum of US$231,678,275; (ii) by 30 July 2010 it had entered into sub-contracts which committed it to spending

US$65,881,367.96 in total, of which US$13,729,371.49 was already incurred liability and US$52,151,996.14 would fall due in the future; and (iii) in the event, after contribution from AEP for certain enhancements, the actual cost of the remedial work to BVC was in excess of US$111 million plus US$2.3 million of legal costs. None of these allegations is admitted by the Reinsurers but, as I understand, they are to be assumed to be correct for the purposes of the preliminary issues.

The preliminary issues

23. The preliminary issues are as follows:

i) Issue 1.1:

> "*In respect of the Ajman Claim, did BVC suffer a loss for the purposes of its entitlement to an indemnity under its professional indemnity insurance programme in respect of the sum of US$13,460,531, which was paid into an escrow account on 15 December 2010 pursuant to settlement agreements dated 15 December 2010 referred to in paragraph 60 of the Re-Amended Particulars of Claim:*
>
> *(a) On 15 December 2010; or*
>
> *(b) As and when ASPCL drew down the money paid into the escrow account.*"

It is Teal's case that the answer to this preliminary issue is (b) and that issues 1.2 and 1.3 (see below) do not arise. It is the Reinsurers' case that the answer to this preliminary issue is (a).

ii) Issue 1.2:

> "*If the answer to 1.1 is (a), is that:*
>
> *(a) Because BVC's liability was established and ascertained for the purposes of the primary insuring clause by virtue of it becoming legally liable, pursuant to settlement agreements dated 15 December 2010, to pay the specified sum into an escrow account in respect of the Ajman claim, notwithstanding that the sum paid was subject to repayment if certain conditions were not met; or*
>
> *(b) Because the settlement agreements accepted BVC's liability to pay for the costs of the remedial works to which the sum paid into an escrow account was referable, notwithstanding that the agreements did not specify the amount of that liability; or*
>
> *(c) Because of both 1.2(a) and (b).*"

As stated above, it is Teal's case that this issue does not arise. It is the Reinsurers' case that the answer is: (a).

iii) Issue 1.3:

> "*If the answer to 1.2 is (b), did the amendment orders dated 30 July 2010 to the contracts between BVC and AEP referred to in paragraph 38 of the Re-Amended Particulars of Claim establish and ascertain BVC's liability as at the date of those contracts for the purpose of the primary insuring clause or give rise to an entitlement to an indemnity under endorsement No. 8 as at the date of those contract amendments?*"

As stated above, it is Teal's case that this issue does not arise. It is the Reinsurers' case that in the light of the answer to issue 1.2, this issue also does not arise.

Issue 1.1

24. Standing back, the primary issue for consideration is Issue 1.1 which is, in summary, whether BVC, as the insured, was entitled to an indemnity in respect of the escrow payment i.e. the net sum of US$13,460,531 (i.e. US$14 million less a credit of US$539,469) which was paid into the Escrow Account pursuant to the terms of the Escrow Agreement in respect of the Ajman claim. In essence, it is common ground that following the judgment of the Supreme Court on the First Preliminary Issue, the underlying policies respond as stipulated in the Order of Andrew Smith J set out above. However, it is Teal's case that pursuant to that Order, the establishment and ascertainment of liability arose not when the escrow payment was paid into the Escrow Account but only at a later stage i.e. as and when ASPCL, the employer in relation to the Ajman works, became entitled to draw down on the escrow account monies. Applying the various dates of drawdown out of the Escrow Account rather than the date of the payment into the Escrow Account is financially advantageous to Teal because it means that a total of US$11,386.706.25 in respect of the Ajman sewage claim is payable by Teal to BVC under the Top and Drop policy and that the Reinsurers are liable to indemnify Teal under the contract of reinsurance. However, if the Reinsurers are right i.e. the liability is established and ascertained when the money was paid into the Escrow Account, no payment is due to Teal.

25. In support of Teal's case, Mr Butcher QC submitted that liability is not "*established and ascertained*" unless and until (i) the insured is in fact liable for some wrongdoing and is held so liable by a judgment or award or compromises a dispute about such liability; (ii) the amount of the insured's liability is quantified by judgment or award or agreement; and (iii) the time for payment of the ascertained amount to the liability claimant has arisen.

26. As to (i), Mr Butcher referred to the general principles on proof of liability as summarised by Clarke LJ in *Astrazeneca Insurance v XL* [2014] Lloyd's Rep. 509 at paras 16-23. However, he accepted and it was, as I understood, common ground that (i) by the July 2010 JBR settlement, BVC compromised existing disputes on terms that it would carry out the remedial work; and (ii) by the December 2010 Ajman settlement, BVC's liability was established because, pursuant to the relevant agreements, ASPCL became entitled to draw down on the escrow payment on the basis that it entered into a contract for the remedial works and had those works carried

out on the terms set out. To this extent, there is (at least for the moment) no issue on actual liability.

27. As to (ii) and (iii), Mr Butcher relied upon the language used in the leading authorities. Thus, in *Post Office v. Norwich Union* [1967] 2 QB 363, Lord Denning MR held at p.375: "*the right to sue for these moneys does not arise until the liability of the wrongdoer is established and the amount ascertained*" (emphasis added); and in *Bradley v. Eagle Star* [1989] 2 AC 957, Lord Brandon held at p. 966: "*In my opinion the reasoning of Lord Denning M.R. and Salmon L.J. contained in the passages from their respective judgments in the Post Office case set out above, on the basis of which they concluded that, under a policy of insurance against liability to third parties the insured person cannot sue for an indemnity from the insurers unless and until the existence and amount of his liability to a third party has been established by action, arbitration or agreement, is unassailably correct*" (emphasis added). Further, Mr Butcher submitted that these words have been cited in many subsequent authorities including *Burns v. Shuttlehurst Ltd* [1999] 1 WLR 1449, in which the Court of Appeal held that a plaintiff who obtained judgment against an insolvent defendant for damages to be assessed had no cause of action against the defendant's insurers under the Third Party (Rights Against Insurers) Act 1930 until the claim was quantified: see paragraph 35 *per* Stuart Smith LJ; that this is clear authority for the proposition that no insured loss is suffered until liability is both: (i) established in principle; and (ii) quantified, i.e. ascertained as to its amount; and that these points are also supported by the prior Judgments in the present case:

    i) Andrew Smith J's judgment at paragraph 30(ii) [p62] cites the principle that: "*Subject to any relevant terms of the (re)insurance contract, the right of an insured to an indemnity arises when an insured loss is suffered. In the case of liability cover the application of this principle is that a loss is suffered when liability is established and the amount of liability has been ascertained, whether by action or arbitration or by settlement, and not earlier*" (emphasis added).

    ii) Longmore LJ held at paragraph 2 of the Court of Appeal's judgment that: "*In general terms in English law a liability insurer's liability only arises when (and does not arise until) the liability of the insured to the third party is established (whether by agreement, judgment or award) … Thus Lexington will be liable to Black and Veatch, subject to any express tem of the insurance contract to the contrary and any defence Lexington may have, when Black and Veatch agree to pay any sum to the third party to whom they are liable or when the third party obtains a judgment or award against them*" (emphasis added).

28. As to Issue 1.1, Mr Butcher submitted that the agreement to pay money into escrow under the Ajman settlement agreement did not meet these criteria for liability to be "established and ascertained", in particular because (i) the payment into escrow was not a payment to ASPCL; (ii) the money in escrow was subject to conditions which meant that it might never be paid to ASPCL; and (iii) the amount of BVC's liability was not ascertained until ASPCL submitted certificates which proved the cost of work which had been done, save for the first 2 instalments which were payable 21 days after signing a new contract and 52 days after commencing the work respectively.

No payment to ASPCL

29. As to (i), Mr Butcher relied on the terms of the Escrow Agreement, in particular Recital D and clauses 1.1, 2.1 and 3.2, as well as the Appendix containing the payment schedule (which I have already quoted above). In essence, he submitted that the Escrow Agreement provides for a two stage process: (i) payment of the US$13.46m into escrow; and (ii) payment to ASPCL out of this fund as and when and if the remedial work has been performed by a new contractor; and that ASPCL has no entitlement to anything, and BVC has no liability to make any payment to it, until stage (ii).

Conditionality

30. As to (ii), Mr Butcher submitted that under the terms of the Escrow Agreement, it was not automatic that all, or even any part, of the fund paid into escrow would ever be paid over to ASPCL. In particular, he relied upon the following points:

    i) The entire obligation to make the Payment (as defined) would become null and void if the New Contract (i.e. appointing a replacement contractor to carry out the remedial work) was not signed by 2 May 2011. In that event, all of the money in escrow would come back to BVC: Appendix 1 paragraph (a) and Clause 3.4(ii).

    ii) The agreement envisaged that the amount in escrow might be more than the sum required to carry out the remedial work. Clause 3.4(i) states that the remainder of the fund was to be distributed to BVC in these circumstances.

    iii) There was also a long stop date of 31 July 2013. Any money still in the Escrow Account then would also revert to BVC: Clause 3.4(ii).

31. For the avoidance of doubt, Mr Butcher accepted that the New Contract was signed shortly after the Escrow Agreement, that the 21 day and 52 day payments were triggered and that all of the money paid into escrow was drawn down on the dates shown in the Schedule as and when they were made. However, he submitted that it was wrong to treat these payments as made as at 15 December 2010, when BVC paid the US$13.46m into escrow: ASPCL did not receive, and was not entitled to receive, anything then.

Amount of liability to ASPCL not ascertained

32. Finally, Mr Butcher submitted that the Escrow Agreement did not determine that BVC was liable to pay US$13.46m to ASPCL. The only sums that were quantified by the agreement itself were the payments due 21 days after ASPCL confirmed the award of the New Contract and 52 days after BVC received written instructions from ASPCL for the new contractor to commence works under the New Contract: Appendix 1, payment terms 1 and 2. As to the balance, the effect of payment term 3 was that BVC had no liability to pay any sum to ASPCL unless and until work to that value had been performed and this was certified by Halcrow. For the avoidance of doubt, Mr Butcher accepted that BVC might eventually be liable to pay up to US$13.46m (as proved to be the case) but that was not determined by this agreement, a point which was, submitted Mr Butcher, underlined by the provision in clause 3.4

for the balance of funds to be returned to BVC if not exhausted by the cost of the remedial work or by the longstop date.

33. These submissions overlap to some extent. Taking these points in turn, I am unpersuaded that the first point i.e. no payment to ASPCL is of much, if any, weight. In truth, it rests upon the sentence quoted above from paragraph 2 of the Judgment of Longmore LJ in the Court of Appeal in the present case to the effect (as submitted by Mr Butcher) that there must be a liability to pay the liability claimant not to make some other payment. However, I am very doubtful that Longmore LJ had in mind at that time the particular question that now arises still less that he intended his words to be taken as creating a universal rule. However, the other two points (i.e. "conditionality" and amount of liability not ascertained) do, in my view, point strongly in favour of the case advanced by Mr Butcher in respect of issue 1.1 i.e. that BVC did not suffer a loss for the purpose of its entitlement to an indemnity on 15 December 2010 but only as and when ASPCL drew down the money paid into the escrow account. I turn then to consider the counter-arguments advanced by Mr Edelman QC on behalf of the Reinsurers.

34. First, Mr Edelman submitted that Teal's case involved the "startling proposition" that BVC were not entitled to any indemnity notwithstanding the fact that it had undertaken a legal obligation to make and duly did make the escrow payment; and that it is impossible to envisage any insured, without the ulterior motive that Teal and BVC have in this case, tolerating, let alone advocating, the withholding of an indemnity in these circumstances. I agree that the arguments which arise in the present context are unusual and possibly unique; but I am not sure I would agree that Teal's case involves any "startling proposition" given that the escrow payment was not made pursuant to any judgment or order but rather pursuant to the settlement agreement undertaken voluntarily with the characteristics referred to above. However, whether "startling" or not, it is necessary to consider the various arguments and counter-arguments on their merits.

35. Second, Mr Edelman emphasised that the arguments advanced by Mr Butcher were "new", the underlying suggestion being that they must necessarily lack merit for that reason alone. There is no doubt that these arguments are "new" but absent any estoppel (which is not raised), they must again be considered on their merits.

36. Third, in support of his general submission that the obligation to make the escrow payment pursuant to the December 2010 settlement rather than the later drawing down of moneys from the escrow account by ASPCL ascertained BVC's liability to ASPCL at the date of the agreement for the purposes of the response of the insurance programme and the Ajman claim therefore falls within the PI Tower and not to the Excess Policy, Mr Edelman relied heavily on (i) the Judgment of Phillips J in *Cox v Bankside Members Agency Ltd* [1995] 2 Lloyd's Rep 437 in relation to interim payment orders and (ii) the Judgment of Lord Mance in the Supreme Court on the First Preliminary Issue. I take these in turn.

Cox v Bankside

37. In *Cox v Bankside,* Phillips J had to consider a number of issues. For present purposes, of main interest is his conclusion that a Court order to make an interim payment to a claimant ascertained liability in the amount of, and at the time of, the

interim payment for the purpose of a liability policy. His reasoning appears at pp451-453. Given the importance of this passage, I quote the relevant part verbatim:

> *"Is an order for an interim payment a sum which the assured has "become legally liable to pay as damages"?*
>
> *If this question falls to be answered in the affirmative, then an order for interim payment will give rise to a right in the assured to claim an indemnity under the policy. Mr. Sumption submitted that the answer to the question was "No". He accepted that an order for interim payment was a sum which the assured had become legally liable to pay, but contended that the payment was not "as damages". He relied upon this passage in the judgment of Mr. Justice Chadwick in Maxwell v. Bishopsgate Investment Management (in liquidation), (Transcript Jan. 28, 1993) at p. 10:*
>
> > *"In my view, the true analysis is that the interim payment order does create a debt which is distinct from, but not independent of, the underlying liability to pay damages. The inter-dependence is this: in computing the final amount to be paid in respect of the underlying liability credit must be given for anything paid or to be paid under the interim payment order."*
>
> *Once judgment is given in respect of a claim for damages, subsequent enforcement is of the judgment debt. The sum that the judgment orders the defendant to pay is nonetheless properly and naturally described as "damages".*
>
> *In Maxwell v. Bishopsgate Mr. Justice Chadwick had to decide whether an interim payment order gave rise to a debt within the meaning of s. 267(b) of the Insolvency Act, 1986. I do not find that the passage relied upon by Mr. Sumption provides any assistance in determining whether the subject matter of an interim payment order falls within the meaning of "damages" in the context of the policies with which I am concerned. Mr. Sumption described the payment as "in effect, a loan on account of a liability". It was not, he said, an order that damages should be paid but an order that a sum should be paid which would fall to be taken into account when eventually damages were assessed and awarded.*
>
> *I was not impressed by these semantics. An interim payment ordered under O. 29, r. 11 is ordered on account of and in anticipation of an eventual award of damages. Where judgment for damages is subsequently entered, it will be for a sum that gives credit for the interim payment already made. In my judgment the subject matter of an interim payment ordered under O. 29, r. 11 can properly and naturally be described as*

> *damages and falls within the meaning of "damages" in the insuring clause of the policy.*
>
> *Ascertainment*
>
> *Does an interim payment order satisfy the requirement laid down by Post Office v. Norwich Union that no claim can be brought under a policy of insurance against third party liability until the existence and amount of that liability has been established by action, arbitration or agreement? Mr. Sumption argued that, because an interim payment order was provisional, it did not establish the amount of the assured's liability. Furthermore, the possibility that the order might be varied raised practical problems as to the operation of the cover. So far as these practical problems are concerned, it does not seem to me that they differ in principle from those inherent in the fact that a first instance judgment in favour of a claimant against the assured may be reversed or varied on appeal. So far as ascertainment is concerned, an interim payment order ascertains a quantified sum which is due and payable by way of damages - albeit on a provisional basis. Interim payment orders did not exist when Post Office v. Norwich Union was decided, but in my judgment an interim payment order satisfies the requirements there laid down.*
>
> *Had I any doubts on this question, they would be dispelled by the consequences that would flow were Mr. Sumption's submissions correct. An agent adequately protected by E & O insurance, would nonetheless be liable to be rendered insolvent by his inability to call upon his E & O underwriters to indemnify him against his liability to comply with an interim payment order. A liability policy which exposed the assured to such a possibility would provide an unsatisfactory cover and it is appropriate, where the wording permits, to adopt a construction that avoids this result. The terms of O. 29, r. 11(2)(a) indicate that those who drafted this order anticipated that liability insurers would be bound to respond to an interim payment order. In my judgment they were justified in so doing.*"

38. I derive the following five main points from this passage:

i) The subject matter of an interim payment ordered under what was then RSC O. 29, r. 11 can properly and naturally be described as damages and, in that case, fell within the meaning of "damages" in the insuring clause of the policy in that case ("… *all sums which the Assured shall become legally liable to pay as damages* …") because it was "… *ordered on account of and in anticipation of an eventual award of damages.*"

ii) An interim payment order satisfies the requirements laid down in *Post Office v Norwich Union* so far as ascertainment is concerned because it ascertains a

quantified sum which is due and payable by way of damages albeit on a "provisional basis".

iii) The fact that the interim payment order was "provisional" and did not finally establish the amount of the assured's liability is irrelevant.

iv) Whilst the possibility that the order might ultimately be varied raised practical problems as to the operation of the cover, such problems did not differ in principle from those inherent in the fact that a first instance judgment in favour of a claimant might be reversed or varied on appeal.

v) There are strong commercial reasons supporting the foregoing.

39. Mr Edelman submitted that there is no material difference between the policy wording in the present case and that which existed in *Cox v Bankside*; nor between the nature of an interim payment order that was considered in *Cox v Bankside* and the Ajman settlement agreement in the present case. Further, he submitted that a commercially sensible application of a liability policy requires the policy to respond in these circumstances; that the December 2010 settlement similarly quantifies the sum payable by BVC to ASPCL by way of damages albeit on a provisional basis; that the beneficiary of a pre-judgment interim payment order would still have to overcome the hurdles of proving liability and quantum before being entitled to retain the interim payment or withdraw it from Court if the interim payment was ordered to be paid into Court; and that in this case, the satisfaction of the conditions for drawdown was entirely under ASPCL's control and therefore presented far less of a hurdle than that faced by the beneficiary of an interim payment order.

40. For his part, Mr Butcher submitted that it was "questionable" whether Phillips J's characterisation of an interim payment was correct in light of *Bradley v Eagle Star* and *Post Office v Norwich Union*; and, insofar as may be necessary, he reserved the right to contend that it was wrong. However, in my judgment, the obligation to make an interim payment pursuant to Court order is distinguishable from BVC's obligation to pay money into escrow in the present case for the two main reasons which Mr Butcher summarised in his skeleton argument as follows.

41. First, the primary ground of Phillips J's reasoning was that an interim payment is a legal liability to pay "*damages*" (p452, applied at bottom p452 - top p453: "*an interim payment order ascertains a quantified sum which is due and payable by way of damages*"). However, as submitted by Mr Butcher, it seems to me that this is true (if at all) because, and only because, a Court will only order an interim payment if satisfied that the claimant will obtain judgment for substantial damages from the defendant. The amount of the interim payment must be less than the amount of damages which the Court holds is likely to be recovered at trial (RSC. Ord. 29, set out at p452 col.1, now CPR 25.7). Accordingly, an order for an interim payment involves a determination by the Court: (i) that the defendant is liable to pay damages to the claimant; and (ii) of the likely minimum amount of the liability. In contrast, the agreement to pay money into escrow was not an agreement to pay damages to ASPCL (the "damages" were payable only as ASPCL became entitled to draw down on the fund). Nor did the Escrow Agreement contain any equivalent assessment of the likely amount of BVC's liability. For the avoidance of doubt, I should emphasise that there

is nothing in the Agreed Statement of Facts to that effect or which might justify such inference.

42. In response and at the risk of repetition, the main point advanced by Mr Edelman in this context was that Mr Butcher's argument ignores the view expressed by Phillips J i.e. that an interim payment ordered under Order 29 r11 can properly and naturally be described as "damages" because it is "*on account of and in anticipation of an eventual award of damages*"; and that exactly the same can be said of the payment into the Escrow Account i.e. it was on account of and in anticipation of an award of damages. I was initially much impressed by this argument. However, as it seems to me, the main difficulty with such argument is the one already referred to above viz unlike the exercise that is performed when the Court is considering whether or not to make an order for an interim payment and, if so, in what amount, the agreed facts fall short of any finding of any minimum amount of likely liability.

43. In this context, Mr Butcher also raised a further point by reference to Clause 1 of the Lexington policy which provided for an indemnity for all sums "*which the Insured shall become legally obligated to pay as Damages*". "*Damages*" is defined in Clause IV.D as "*compensatory damages*" [Clause IV.D at p1]. On this basis, Mr Butcher submitted that the payment into escrow was certainly not a payment by way of "compensatory damages", since compensation necessarily involves a payment to, or to the order of, an injured party; that the payment into escrow was not such a payment; and that whereas an interim payment might well be regarded as an obligation to pay "*Damages*" within the meaning of Clause 1, the obligation voluntarily undertaken to pay money into escrow to await future events cannot be so characterized. At one stage, it seemed to me that this argument was similar to the one rejected by Phillips J as resting on "semantics" and that it should be rejected for that reason. However, for the reasons already stated, there is, in my view, a real and significant distinction between, on the one hand, the interim payment ordered by the Court and considered by Phillips J in *Cox v Bankside* and, on the other hand, the payment into the Escrow Agreement voluntarily undertaken by BVC in the present circumstances. By way of further elaboration, Mr Edelman emphasised the fact that an interim payment could also be made voluntarily without a court order: see RSC Order 29 r17 and, now, CPR25.8. That is true. However, it is, to say the least, far from clear to me that the decision of Phillips J in *Cox v Bankside* would necessarily have been the same if the interim payment had been made voluntarily rather than pursuant to Court order.

44. Second, Phillips J's secondary reason for his decision was one of policy viz that an insured would be liable to be rendered insolvent by an order for an interim payment if it could not call on its E&O underwriters to indemnify it (p.453, first full paragraph). As submitted by Mr Butcher, this point is of no application to the present case. The Escrow Agreement is a consensual arrangement for security for future payments to be provided by way of payment into escrow. BVC did not have to enter into this arrangement. An insolvent defendant could not have done so. It is quite different from a Court order compelling payment. There is no policy reason why BVC's insurance programme should indemnify it for the payment into escrow which it chose to agree to, rather than the draw downs from the escrow account. The latter, but not the former, were payments to ASPCL that BVC was legally liable to make.

45. I should mention that Mr Butcher also advanced a further third reason why, in his submission, the payment into escrow was distinguishable from an interim payment pursuant to Court order as in *Cox v Bankside* viz it was not a payment to ASPCL. In particular, he submitted that whereas an interim payment is made to the liability claimant, the funds in escrow remained BVC's funds; that this is why BVC received the interest on the account; and that the Reinsurers' contention depends on their mischaracterization of the payment into escrow as a payment to ASPCL which it was not. Mr Butcher is plainly right in saying that the payment of the money into escrow was not a payment to ASPCL. However, if this point stood alone, I am doubtful that it would be sufficient to determine Issue 1.1 in favour of Teal. As submitted by Mr Edelman: (i) whilst an interim payment made pursuant to a Court order would usually be made to the plaintiff, the Court could order that it be paid into Court rather than to the plaintiff (see RSC Order 29r13 and now CPR 3.1(3) and the White Book para 15-124 (Vol 2 p3446)); and (ii) that BVC was entitled to the interest on the account is equally consistent with the fact that ASPCL's entitlement to draw down the escrow payment was subject to conditions. As pointed out by Mr Edelman, I also accept that when the Court gives permission for money to be taken out of Court pursuant to CPR 37.3, it will generally include a direction for the payment of any money including accrued interest and that this may be a relevant consideration. At best, it seems to me that this further argument advanced by Mr Butcher may lend possible further support to his two main arguments as summarised above; but it is unnecessary to say more.

46. For all these reasons, I am unpersuaded that the decision of Phillips J in *Cox v Bankside* ultimately assists the Reinsurers in the present case.

The Judgment of Lord Mance on the First Preliminary Issue

47. Mr Edelman submitted that the Reinsurers' case was supported by the analysis of the Supreme Court on the First Preliminary Issue. In particular, he drew attention to the passage at paragraph 14 where, having referred at paragraph 13 to the conclusion in *Cox v Bankside* that an insurer's liability under the policy arose on the ascertainment of the insured's third party liability, Lord Mance stated:

> "*In Cox v Bankside itself, Phillips J held that the policy was called upon to respond in this way to a court order for interim payment; if this were not so, an insured 'adequately protected by E & O insurance, would nonetheless be liable to be rendered insolvent by his inability to call upon his E & O underwriters to indemnify him against his liability to comply with an interim payment order' (p 453, left).*"

Thus, Mr Edelman submitted that Lord Mance (with whom Lord Neuberger, Lord Clarke, Lord Sumption and Lord Toulson agreed) thereby implicitly approved Phillips J's decision in *Cox v Bankside* insofar as it related to interim payments. Further, he sought to rely upon what Lord Mance stated at [21] when he referred to the aim of the present liability insurance as being to "*provid[e] the insured with an indemnity to avoid the insolvency which third party claims would otherwise threaten – a consideration emphasised in the context of reinsurance in Charter Re and in the context of liability insurance by Phillips J in Cox v Bankside.*" In my judgment, these snippets are of no real assistance in the present context for reasons which I have

already set out above when considering Phillips J's Judgment in *Cox v Bankside* and which it is unnecessary to repeat.

The "hold harmless" principle

48. Further and in any event, Mr Edelman submitted that the Reinsurers' case based on *Cox v Bankside* and the decision of the Supreme Court on the First Preliminary Issue was supported by the "hold harmless" principle. In particular, he relied upon *Firma C-Trade SA v Newcastle Protection and Indemnity Association (The "Fanti")* [1991] 2 AC 1, HL, where Lord Goff said (at 35-36) that equity had intervened in relation to contracts of indemnity, the remedies available at law being inadequate, to give effect to the principle that indemnity means that the party being indemnified should never be called upon to pay; and where Lord Brandon, similarly, described (at 28) the remedies available at common law and in equity and said that in equity an ordinary contract of indemnity could be specifically performed by ordering that the indemnifier should pay the amount concerned directly to the third party to whom the liability was owed or in some cases to the party to be indemnified and that there was no doubt that, since the passing of the Supreme Court of Judicature Acts 1873 and 1875, the equitable remedy had prevailed over the remedy at law.

49. In addition, Mr Edelman relied on a passage from the Judgment of Hirst J in *Ventouris v Mountain (The "Italia Express") No 2* [1992] 2 Lloyd's Rep 281, at 291, col 2 to 292, col 1):

> "*While, of course, The Fanti was a liability insurance case, I consider that Lord Goff's statement of the law was of general application, extending to property insurance cases also, and I agree with Mr Clarke that it would be extraordinary if different principles applied to the two classes of insurance. The nature of the perils insured against in liability insurance enabled equity to intervene to prevent the loss which would otherwise have occurred under the common law. But this does not, in my judgment, render the two classes of contract different in their essential character, namely, as Lord Goff stated, that once the loss is suffered or the expense incurred, the indemnifier is in breach of contract for having failed to hold the indemnified person harmless against the relevant loss or expense; this phraseology is entirely appropriate to cover both the loss against which the insured is indemnified under property insurance, and the expense against which he is indemnified under liability insurance.*"

50. Further, Mr Edelman referred me to *Callaghan v Dominion Insurance Co Ltd* [1997] 2 Lloyd's Rep 541 where Sir Peter Webster re-visited *The "Italia Express"* and the authorities reviewed by Hirst J and, in relation to the observation by His Honour Judge Kershaw QC in *Transthene Packaging Co Ltd v Royal Insurance (UK) Ltd* [1996] LRLR 32 at 41, col 1 that what Lord Goff in *The Fanti* and Hirst J were saying was that the insurers under a policy of property insurance contract that the relevant contingencies will not occur, said (at 544, col 2):

> "*In my respectful view His Honour Judge Kershaw misunderstood or misread both the dictum of Lord Goff and the judgment of Mr Justice Hirst. In my view, neither of them were saying that the insurer in question had contracted that the contingencies would not occur; they were simply saying that immediately loss is suffered by the occurrence of the contingent event the insurer came under a liability to indemnify the insured against that loss, and I can see no good reason for differing from the judgment of Mr Justice Hirst or for declining to follow the dictum of Lord Goff.*"

51. The significance of these authorities in the context of liability insurance is, submitted Mr Edelman, that they show that the insurer is obliged to step in and make payment so that the insured is never called upon to pay; that applying these principles to the Ajman claim, BVC was entitled to be held harmless by Teal against its loss, that loss being the obligation to make the escrow payment under the December 2010 agreements; and that BVC was therefore entitled to call upon Teal under the policy to step in and to make the escrow payment in BVC's place. In broad terms, I accept, of course, the general thrust of the "hold harmless" principle. However, in my view, there are insufficient facts to enable Mr Edelman to say that there was any obligation on the insurers here to make any payment when the payment was made into the escrow account. The determination of that question turns on the proper resolution of the earlier questions which I have already considered. If I am right in the conclusions which I reached in relation to those earlier questions, I do not consider that the "hold harmless" principle provides the Reinsurers with a separate or discrete road to success.

52. I should mention that in the course of the hearing, Mr Butcher raised a new point for the first time seeking to rely (insofar as may be necessary) on Article VI of the Lexington policy which I have already quoted above. In particular, he submitted that as a matter of language the effect of Article VI is that there is no right of indemnity unless and until liability has been finally, rather than provisionally, established and ascertained. Following the hearing, I invited the parties to put in written submissions on this point. In essence, Mr Edelman submitted that Article VI was of no assistance in the circumstances of the present case in particular because (i) the issue was determined in favour of the Reinsurers by the Supreme Court on the First Preliminary Issue; and/or (ii) in any event, Article VI does not affect the accrual of the cause of action but, at most, only bars the right to sue which was, he submitted, irrelevant for present purposes. Both these points were disputed by Mr Butcher. However, given my earlier conclusions, it is unnecessary to engage in this further debate.

Conclusion

53. For all these reasons, I would answer Issue 1.1 by saying (b) i.e. that in respect of the Ajman claim, BVC suffered a loss for the purpose of its entitlement to an indemnity under its professional indemnity insurance programme in respect of the sum of US$13,460,531 as and when ASPCL drew down the money paid into the escrow account. In light of this answer, Issue 1.2 and Issue 1.3 do not arise. Accordingly, Counsel are requested to seek to agree a draft order for my approval. Failing agreement, I will deal with any outstanding issues.