Sir, you may not step into my shoes: Insurers do not always have a right of subrogation

The Court of Appeal in Rathbone Brothers Plc v Novae Corporate Underwriting Ltd has set out some useful guidance on the issue of when Insurers do not enjoy the right of subrogation.

The decision is very fact specific and should not be taken to mean that the Court will often and readily imply a non-subrogation term into a contract of insurance. However, the judgment is of interest and demonstrates that such a term will be implied in certain circumstances.

In essence, the principle of subrogation enables insurers, who have paid out an indemnity under a policy, to 'step into the shoes' of the insured party that received the indemnity for the purposes of bringing a recovery action against a third party (in the name of the insured). This is a very long established legal right of insurers to "make such claim for damages as the insured himself could have made, and it is for this reason they would have to make it in his name."

Insurers’ right of subrogation can be excluded in two ways. Firstly, there may be a waiver of the right in the insurance policy itself, either express or implied. This is common, for example, under Contractor’s All Risk ('CAR') insurance policies, where there are a number of co-insured parties. CAR policies will often include an express waiver of insurers’ rights to subrogate against any of the co-insureds. Secondly, even if a right of subrogation exists under the insurance policy, the terms of an underlying contract between the insured and a third party may preclude the exercise of subrogation.

In the present case, the appellants sought to advance both of these arguments in order to prevent insurers bringing a subrogated action. At first instance, the Court had found that insurers did in fact benefit from the right of subrogation. This was challenged on appeal.
There was no express waiver of subrogation rights in the insurance policy. Rathbone Brothers plc and PEV argued that there was an implied waiver of the right of subrogation. They also argued that, in any event, on a proper construction of the underlying contract (the Rathbone indemnity provision) it was plain that the parties intended to treat the insurance as the primary indemnity such that there was no right of subrogation. In his leading Court of Appeal judgment Lord Justice Elias found in the appellant’s favour on both counts.

In the circumstances, a waiver of insurers’ rights of subrogation was to be implied into the insurance policy by virtue of the intention of the parties. The key passage stated:

“I am satisfied that it could not have been the intention of the parties that the insurers should be able to enforce rights of indemnity against a co-insured where the co-insured was indemnifying the very same risk as the insurers. I believe that implying the term is simply making express what the parties must have intended.”

In addition, under the terms of the Rathbone indemnity itself it was clearly not intended by the parties that the indemnity should be treated as the primary source of protection. As such, one could readily imply a term into the Rathbone indemnity contract to the effect that it was intended to provide supplemental protection only once the claim against the insurance company had been exhausted. The subrogated right which insurers were arguing for (unsuccessfully) related to an indemnity which was providing the same protection as the insurance itself. That cannot have been the intention of the parties.

Therefore, insurers were held to have no right of subrogation on the facts of the case. However, the Court made it clear that it would not be swift to imply terms into insurance contracts, or contracts generally. It was doing so in this case because the intention of the parties cannot sensibly have permitted any another outcome. In consequence, one must be cautious in drawing general lessons about the right of subrogation from this judgment. Possibly the only absolutely failsafe method of precluding insurers’ right of subrogation is for an express provision to that effect to be included in the policy wording, as it often is in CAR policies.

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