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The undermining of the indemnity principle - a plea for a return to basics and the rediscovery of full indemnity in insurance law - a case study of Vietnam

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THE UNDERMINING OF THE INDEMNITY PRINCIPLE – A PLEA FOR A RETURN TO BASICS AND THE REDISCOVERY OF FULL INDEMNITY IN INSURANCE LAW – A CASE STUDY OF VIETNAM

CHAPTER 1: INTRODUCTION

This research concerns, as the title indicates, the fundamental principle of indemnity and related doctrines. The principle of indemnity is well established and stands in an unchallengeable position. However, some doctrines derived from the fundamental principle, such as subrogation and insurable interest, cause problems, and the rules of subrogation and insurable interest to some extent depart from the nature of the principle of indemnity.¹ The rules vary from one jurisdiction to the next.

The Vietnamese Insurance Business Law was enacted in 2000. The Law adopts the principle of indemnity² and the doctrines of insurable interest³ and subrogation.⁴ However, the rules of the two doctrines are not consistent with the principle of indemnity. As to the principle of insurable interest, under Vietnamese insurance laws, the insureds must have a legal relation to the subject matter of insurance.⁵ Strict interpretation of this principle may deprive the insureds of the right to be compensated for their actual economic loss.⁶ An insured, for example, who has an economic interest in the insured property and may gain economic advantage from the existence of the insured property, but whose interest is not recognised by law, is not allowed to take out insurance.

In some situations, the insurable interest principle may cause even worse consequences for the insured. For instance, if the insured's insurable interest is not legally recognised, the insurers may allow the insured to take out insurance when the contract is concluded but reject

¹ See Chapter 4: Insurable interest and Chapter 5: Subrogation

² Article 46 and 47 of Vietnam's Law on Insurance Business 2000

³ Article 3(9) of Vietnam's Law on Insurance Business 2000

⁴ Article 49 of Vietnam's Law on Insurance Business 2000

⁵ Article 3(9) of Law on Insurance Business 2000: "Insurable interest means a right of ownership, right of possession, right of use, or property right; maintenance rights and obligations to the person insured against."; Article 226 of Maritime Code 2005: "*Identification of insurable interests*: (1) A person with an insurable interest is a person who is interested in a subject-matter of insurance in a sea voyage. (2) A person is interested in a sea voyage when he/she has grounds to prove that he/she has any relation to the voyage or to any subject-matter of insurance at risk in it, in consequence of which such person may benefit by the safety and due arrival of the subject of insurance, or may not benefit by its loss or by damage to it or by the detention of it, or may incur liability in respect of it..."

⁶ See section 4 of Chapter 4: Insurable interest

his claim when the loss occurs, on the ground that the insured has no legal insurable interest.⁷ In this situation, the provisions governing insurable interest under Vietnamese insurance laws actually put the insurers into an “all to gain, nothing to lose” position.⁸

Regarding the subrogation principle, there is confusion between the principle of subrogation and the principle of assignment under Vietnamese insurance laws. After having been indemnified by the insurers, the insureds must transfer all of their rights and remedies against a third party to the insurers.⁹ The insurers and the insureds have separate rights to bring an action against the third party. This confusion creates a burden for the third party.¹⁰ He may be taken to court twice due to the same cause of action. In addition, the insurers are entitled to have priority claim to recoup their payment from the subrogation recoveries from the third party, regardless of the fact that the insureds are not fully compensated for their actual loss.¹¹ This is not consistent with the nature of the indemnity principle.

⁷ See section 5.3 and 6 of Chapter 4: Insurable interest

⁸ In principle, an insurance contract in which the insured has no insurable interest shall be void. The insurer must refund the premiums to the insured, see article 23 of Vietnam’s Law on Insurance Business 2000 and article 137 of Vietnam’s Civil Code 2005. However, in practice, Vietnamese insurers may sometimes use technical legal instruments in order to refuse to refund the premiums. For example, they may apply article 19(2) of Vietnam’s Law on Insurance Business 2000 or article 230 of Vietnam’s Maritime Code 2005. According to article 19 of the Law, an insurer has the right to unilaterally suspend contracts and collect insurance premiums up to the time of contract suspension when a policyholder has intentionally provided false information in order to enter an insurance contract to make an unfair profit. According to article 230 of Vietnam’s Maritime Code 2005, a contract of marine insurance is automatically invalidated if the peril covered by the policy has already occurred or where the possibility of its occurrence does not exist in reality; in this case, the insurer retains the right to the premiums, and need not indemnify.

⁹ Article 49 of Vietnam’s Law on Insurance Business 2000: “*Right of subrogation*: (1) Where the wrongful act or omission of a third party causes damage to an insured and the insurer has already indemnified the insured, the insured must pass to the insurer the right to claim recovery of such sum of indemnity from the third party. (2) If the insured person refuses to pass such right to the insurer or does not reserve or abandons the right to make a claim against the third party, then the insurer shall have the right to deduct an amount of indemnity depending on the level of fault of the insured...”; Article 577 of Vietnam’s Civil Code 2005: “*Transfers of claims for indemnity*: (1) Where a third party is at fault for causing damage to the insured, and the insurer has paid insurance benefits to the insured, the insurer has the right to demand the third party indemnify the insurer for the insurance benefits already paid. The insured must provide the insurer with all necessary information, documentation and evidence of which the insured has knowledge in order to enable the insurer to exercise its right to demand the third party [to indemnify]. (2) Where an insured has received monetary compensation for damage from a third party which is less than the amount payable by the insurer, the insurer is only required to pay the difference between the [total] insurance benefits [otherwise payable] and the amount paid by the third party, unless otherwise agreed. If the insured has received insurance benefits but the insurance benefits are less than the damage caused by the third party, the insured has the right to demand the third party indemnify [the insured] for the difference between the insurance benefits and the monetary compensation for the damage. An insurer has the right to demand the third party indemnify fully [the insurer] for the amount it has paid to the insured”;

¹⁰ See section 5 of Chapter 5: Subrogation

¹¹ See section 3.2 and 4.1 of Chapter 5: Subrogation

The principle of indemnity is a root of indemnity insurance.¹² Many doctrines of insurance contract law are derived from the principle of indemnity, such as insurable interest, subrogation, double insurance and contribution, reinstatement, and abandonment. These established doctrines are based on the fundamental principle. The purpose of the principle of indemnity and these doctrines are to prevent the unjust enrichment of the insureds and ensure that the insureds cannot get more than their loss in the event of the occurrence of the insured perils. In essence, the purpose of the principle of indemnity is to put the insureds or policyholders into the position in which they would have been if the loss had not occurred.¹³ The principle is aimed at giving insureds full compensation but no more. The recovery of the insureds is limited to the actual economic losses they have suffered as the result of the insured events, no more no less.¹⁴

This study examines Vietnamese insurance laws relating to the doctrines of subrogation and insurable interest and the rules of these two doctrines with reference to English law and, where necessary, other countries' law such as American, Australian and Canadian law.

Many other doctrines, such as double insurance, abandonment and so on, are also based on the principle of indemnity, but this research focuses on the doctrines of subrogation and insurable interest only. The reason for choosing these two doctrines as the subject of the study is that, on the one hand, they are the corollary of the principle of indemnity and, on the other, some of the rules of these two doctrines in Vietnamese law depart from the nature of the indemnity principle and have caused and will continue to cause problems, and therefore their reform is necessary.

1. BACKGROUND FOR THE RESEARCH:

Vietnam is a developing country. To accelerate its development, the country launched economic reform in 1986. Since then its economy has grown rapidly, with an average growth

¹² Such as property insurance, fire insurance, marine insurance and liability insurance and so on.

¹³ J. Chuah, *Law of International Trade*, (3rd edition, Sweet & Maxwell, 2005), p365

¹⁴ In *Castellain v. Preston* (1883) 11 Q.B.D. 380, p387 Brett L.J. said: "The fundamental rule of insurance law is that the contract of insurance contained in a marine or fire policy is a contract of indemnity, and of indemnity only, and this contract means that the assured, in the case of a loss against which the policy has been made, shall be fully indemnified, but shall never be more than fully indemnified." See also: ALRC Discussion Paper 63, para. 7.3; R. Keeton, *Basic text on insurance law*, (West Publishing Co., 1971), p88; SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p133-134

rate of 8% per year in terms of its GDP.¹⁵ Following the rapid development of its economy, the insurance market has expanded greatly. In 2007 Vietnam became a member of the World Trade Organization (WTO). To meet the commitments of joining the WTO, Vietnam has opened markets to foreign investors in most economic sectors, including insurance sector. Vietnam's insurance market, consisting of domestic and foreign insurance companies, has expanded rapidly since 2008.¹⁶ It is one of the fastest growing markets in the world. However, the history of Vietnam's insurance industry is relatively short; the role of insurance in the national economy had not been properly appreciated until 1980s.¹⁷ Since the economic reform, Vietnam's insurance market and insurance industry, like other industries in the country, have grown rapidly.¹⁸ To govern the insurance activities, legislations relating to insurance were published in 1990s. In 1990, the Vietnamese Maritime Code was enacted under which marine insurance was, inter alia, governed.¹⁹ The Maritime Code 1990 was replaced by the Maritime Code 2005.²⁰ Marine insurance is now governed by Chapter XVI (consisting of 34 articles) of the Maritime Code 2005.²¹ Non-marine insurance is governed by the Law on Insurance Business 2000²² which replaced the Decree on Insurance Business 1993²³.

However, due to the fact that the insurance laws are new laws and the legislators are not competent in terms of insurance legislation, some provisions in Vietnamese insurance laws are ambiguous and confusing. These ambiguities and confusions in law have caused, or will cause, problems and disputes in practice.²⁴ Judges have different interpretations of the

¹⁵ Documentaries of the 11th National Congress of Vietnam's Communist Party, Communist Party of Vietnam Online Newspaper, available at http://123.30.190.43:8080/tiengviet/tulieuvankien/vankiendang/details.asp?topic=191&subtopic=8&leader_topic=989&id=BT531160752

¹⁶ Total direct premium written increasing by approximately 20% year-on-year; see Hiep hoi bao hiem Viet Nam, "Tong quan thi truong bao hiem Viet Nam nam 2012" [Trans: Association of Vietnamese Insurance, "Overview of Vietnamese insurance market 2012"] <<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013

¹⁷ In a historic shift in 1986, it was seen significant changes in Vietnam's economic reform (free market reforms known as "Doi moi", from the centrally planned economy to "market – oriented" economy.

¹⁸ This will be fully explained in chapter 2.

¹⁹ The contracts of marine insurance was governed by Chapter XVI with 41 articles (from Article 200 to Article 240 in the Vietnam's Maritime Code 1990)

²⁰ Article 261(2) of the Maritime Code 2005: "This Code supersedes the Vietnamese Maritime Code of 1990."

²¹ From article 224 to article 257

²² Article 1 to article 57 governs insurance contracts, and article 58 to article 129 on establishment and operation of insurance companies.

²³ The Decree is relatively short and is divided into six chapters which are subdivided into 37 articles only. It should be noted that a decree in respect of the classification of Vietnamese law is one type of delegated (or subordinate) legislation.

²⁴ See section 3 of Chapter 4: Insurable interest and section 5 of Chapter 5: Subrogation

provisions of the law; consequently, different decisions may be made by different judges in similar cases. Reform of some of the provisions is necessary.

The English insurance industry has a long history. The origins of modern insurance contract in England can be found in the sixteenth century²⁵ and English insurance law has been considered as a model to be followed by other countries in drafting their own laws. The rules of marine insurance in the Vietnam's Maritime Code 2005 were drafted by following the Marine Insurance Act 1906 (UK).²⁶ In addition, the English legal system is a common law system and the English law includes statutes²⁷ and case laws.²⁸ Thus, the English law could keep pace with rapid changes in the business environment, particularly in the insurance industry. Because the Vietnamese laws are drafted largely following the English law, most concepts and principles in the Vietnamese laws are of English origin.²⁹ In this research, therefore, when considering the reform of Vietnamese law, English law will be taken as a reference.

2. RESEARCH QUESTIONS

There are two research questions in this thesis. The first question is that, if insureds have suffered an actual economic loss caused by an insured risk, to what extent does the current Vietnamese insurance law on subrogation and insurable interest allow them to be compensated for their loss? It is hypothesised that Vietnamese insurance law does not allow the insureds to obtain full compensation for their actual economic loss, which is inconsistent with the nature of the principle of indemnity.³⁰

In indemnity insurance,³¹ in order to make a valid claim against the insurers, the insureds are required to have an insurable interest in the insured property.³² An insurable interest must be

²⁵ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p1

²⁶ Hereafter referred to as the MIA 1906.

²⁷ The statutes are made by codifying case laws and rules of practices.

²⁸ Case law has force of law under the doctrine of *stare decisis*.

²⁹ For example: marine insurance contract, maritime peril, insurable interest, constructive total loss, principle of subrogation, principle of double insurance and contribution, principle of assignment, principle of abandonment,...

³⁰ For analysis on the nature of the indemnity principle, see Chapter 3: The principle of indemnity

³¹ This thesis does not deal with the requirement of insurable interest in non-indemnity insurance. Property and liability insurance are examples of indemnity insurance. Life insurance, personal accident are examples of non-indemnity insurance

³² See section 3.2 of Chapter 4: Insurable interest

a legal interest.³³ In order to constitute an insurable interest, the relationship between the insureds and the insured property must be a legally recognised relationship. This requirement narrows down the situations in which the insureds may have an insurable interest in the insured property.³⁴ In a number of cases, the insureds actually suffered an economic loss, but the economic relationship between the insureds and the insured property was not recognised by law, and therefore the insurance contract was declared void and the insureds' claim was denied.³⁵

The provisions relating to subrogation allow the insurers to have priority to subrogation recoveries from a third party. The insurers' rights of subrogation arise immediately after they have indemnified the insureds according to the terms of the insurance policy, irrespective of the fact that the insureds are not fully compensated for their actual economic losses.³⁶ The insurers are entitled to bring an action against the third party wrongdoer in their own name in order to recoup the payment they have made to the insureds,³⁷ which is confusion between the doctrine of subrogation and the doctrine of assignment.³⁸ This confusion may harm the insureds' rights to sue the third party for their uninsured loss, if there is any.³⁹

The second question is: what reforms are necessary to protect the insureds' rights to obtain full compensation? This thesis argues that the following reforms are necessary.

First, the provisions governing insurable interest in indemnity insurance⁴⁰ should be abolished.⁴¹ The principle of indemnity already provides protection against moral hazard and against gambling in the guise of insurance, because the principle limits the insureds' recovery to their actual loss.⁴² If the insureds cannot prove their actual loss, the obligation of the insurers to make a payment does not arise. In addition, the insurers themselves can prevent moral hazard and gambling in the guise of insurance.⁴³

³³ Article 3(9) of Law on Insurance Business 2000; Article 226 of Maritime Code 2005; see also section 3.2 and 4.1 of Chapter 4: Insurable interest

³⁴ See section 4.1 of Chapter 4: Insurable interest

³⁵ See section 4.1 of Chapter 4: Insurable interest

³⁶ See section 3.2 and 4.1 of Chapter 5: Subrogation

³⁷ See Article 49 of Vietnam's Law on Insurance Business; article 577 of Vietnam's Civil Code 2005; article 247 and 248 of Vietnam's Maritime Code 2005

³⁸ See section 5 of Chapter 5: Subrogation

³⁹ *Ibid*

⁴⁰ The requirement of insurable interest in non-indemnity insurance is not discussed in this thesis.

⁴¹ See section 6 and 7 of Chapter 4: Insurable interest

⁴² See section 6 of Chapter 4: Insurable interest

⁴³ *Ibid*

Second, the provisions governing subrogation should be amended.⁴⁴ Where the insurers exercise their subrogation rights against a third party, they should sue in the insureds' name and claim for the amount of the whole loss the insureds have suffered.⁴⁵ The insureds should be given priority to subrogation recovery until full compensation for their actual loss is achieved.⁴⁶ Any amount in excess of the full compensation should go to the insurers.⁴⁷

3. OBJECTIVES OF THE RESEARCH

The main purpose of this study is to critically examine and analyse the doctrines of subrogation and insurable interest and rules relating to these two doctrines under Vietnamese insurance law in order to identify problems and to work out better solutions to the problems and make the rules consistent with the nature of the principle of indemnity.

To achieve this purpose, the research will first examine the nature of the principle of indemnity, which is the fundamental principle in insurance law for indemnity insurance. Secondly, it will critically discuss the doctrine of insurable interest and doctrine of subrogation, which are the corollary of the principle of indemnity,⁴⁸ and the rules of these two doctrines in Vietnamese insurance law and English law and other jurisdictions (if necessary), and will discover to what extent the rules depart from the nature of the indemnity principle in these two countries' laws. Thirdly, this study will critically analyse the provisions of Vietnamese law relating to subrogation and insurable interest to explore problems such as ambiguities and confusions and disputes which have been caused and will be caused in practice. The research attempts to find better solutions to solve the problems by referring to English law and the Law Commission's reform proposals.⁴⁹ Approaches in other countries' insurance laws⁵⁰ will also be referred to in this thesis where necessary.

⁴⁴ See section 5 and 6 of Chapter 5: Subrogation

⁴⁵ See section 5 of Chapter 5: Subrogation

⁴⁶ See Chapter 5: Subrogation

⁴⁷ *Ibid*

⁴⁸ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p17; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p321

⁴⁹ The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008). The Issue Paper 4 has put forward a question as to whether there should be a requirement for insurable interest. In indemnity insurance, it has tentatively proposed that no requirement of insurable interest should apply to indemnity insurance contracts. It has also raised another question as to whether there should be a legal requirement on insurers to check that policyholders have an

As to the principle of insurable interest, under both Vietnamese and English insurance laws, the insured must have a legal relation to the subject matter of insurance, and must possess an insurable interest at the time of loss.⁵¹ This is a narrow and rigid approach. Unfairness to the insured may occur if the harsh approach is followed strictly. A sub-contractor, for example, may be allowed to take out policy for the whole project when the contract is concluded, but the insurer may refuse the payment later when the loss occurs on the ground that the sub-contractor has no insurable interest on the whole project.⁵² The Vietnamese courts, like English courts, may support the insurer's rejection. It is really unfair to the insured who has paid the premium but received nothing from the insurer. In contrast, the insurer, who has received the premium from the insured but is allowed to escape liability with the technical defence, would be unjust enriched. Rules derived from the doctrine of insurable interest will be fully discussed in chapter 4: "Insurable Interest".

So far as subrogation is concerned, according to its nature, where an insured event is caused by a third party, after the insurer has paid the insured under the policy, he is entitled to be subrogated to the insured's right to sue the third party wrongdoer by using the insured's name for the whole loss suffered by the insured for both his own benefit and the latter's benefit.⁵³ However, in Vietnamese insurance laws, there is confusion between the principle of

expectation or a chance of loss at the outset of an indemnity contract of insurance or should such matters be left to regulation? In the Issue Paper 4, it has set out examples of insurance policies that do not easily fit within the categorisations of insurable interest under the current English laws or where it is unclear how the indemnity principle applies. The examples relate to insurance of an honour payment and contents insurance. It has asked for any comments on those examples; UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012). The Consultation Paper has concluded that the basis of the requirement for insurable interest is uncertain for most indemnity insurance. It has proposed that the requirement of insurable interest should be imposed by statute alone. The statute should clarify that the requirement for insurable interest exists in all forms of insurance, including indemnity insurance. In indemnity insurance, to make a claim, the insured must show insurable interest at the time of the loss. It has also proposed that unless there is a real probability that a party would acquire some form of insurable interest at some stage, an insurance contract should be treated as void: the insurer may not sue for the premium, and the insured is entitled to a refund of premiums already paid. This is to guard against an insured being sold a policy that is, to all intents and purposes, worthless. As far as the definition of insurable interest is concerned, the Consultation Paper has asked for comments on two possible options: (1) Option 1 would not define what comprises a valid insurable interest for the purposes of indemnity insurance. Instead the matter would be left entirely to the courts, as it is now. (2) Option 2 would provide a partial codification of the common law, in much the same way as the Marine Insurance Act 1906. It would provide a non-exhaustive list of what does constitute insurable interest, while recognising that the concept is open-ended. The courts may develop it further as time goes on.

⁵⁰ Such as American laws, Australian laws, and Canadian laws

⁵¹ *Lucena v Craufurd* [1806] 2 Bos. & P.N.R. 269; *Macaura v Northern Assurance Co.* [1925] A.C. 619; section 5 of MIA 1906; section 1 to 3 of LAA 1774; article 3(9) of Vietnam's Law on Insurance Business 2000; article 225 and 226 of Vietnam's Maritime Code 2005

⁵² For more details, see section 3.2 and section 5.3 of Chapter 4: Insurable interest

⁵³ *Castellain v. Preston* [1883] 11 QBD 380; *Mason v Sainsbury* [1782] 3 Doug. K.B. 61; *London Assurance Co v Sainsbury* [1783] 3 Doug 245; section 79 of the MIA 1906

subrogation and the principle of assignment.⁵⁴ For example, the Vietnamese law allows the insurer to sue the third party in his own name for his own benefit.⁵⁵ This may harm the insured's right to sue the third party for his underinsured loss if there is any. The confusion may cause disputes in practice and a clarification for the confusion is necessary. Furthermore, under Vietnamese law, where the insured loss is caused by a third party, sometimes the insured cannot get full compensation if the insurance is an under-insurance or where there is an excess in the policy.⁵⁶ By the Vietnamese laws the insurer is allowed to be subrogated to the insured's rights to sue the third party wrongdoers for his own benefit irrespective of the fact that the insureds have not been fully compensated for their total loss.⁵⁷ The insurer, after payment to the insured, is allowed to sue the third party for what he has paid to the insured and the insured must bring a separate action against the third party for his uninsured loss which has not been paid by the insurer.⁵⁸ However, the law does not expressly stipulate who (whether the insurer or the insured) has the priority to be recouped by the recoveries from the third party. In practice, sometimes the insurer is allowed to be recouped before the insured being fully compensated. This is not consistent with the nature of the principle of indemnity.

This thesis attempts to find out to what extent the rules of subrogation and insurable interest depart from the principle of indemnity under Vietnamese insurance laws. Recommendations on how to amend the rules will be suggested in order to keep them in line with the nature of the principle of indemnity.

Similar problems are also found in English insurance laws. For instance, English law requires the insured to have a legal or equitable insurable interest.⁵⁹ As to subrogation, the current English law allows the insurer to be recouped first from the subrogation recoveries and leaves the insured behind in recovering for his loss within the excess according to the excess clause in the policy.⁶⁰ These approaches have received heavy criticism from academics, judges, legal practitioners and other commentators.⁶¹ The Law Commission and Scottish Law

⁵⁴ This confusion is critically analysed in section 5 of Chapter 5: Subrogation

⁵⁵ Article 577 of Vietnam's Civil Code 2005; article 49 of Vietnam's Law on Insurance Business 2000; article 247 and 248 of Vietnam's Maritime Code 2005.

⁵⁶ See section 4.1 of Chapter 5: Subrogation

⁵⁷ Article 577(2) of Vietnam's Civil Code 2005; article 49 of Vietnam's Law on Insurance Business 2000; article 248 (3) of Vietnam's Maritime Code 2005

⁵⁸ Article 577 of Vietnam's Civil Code 2005; article 49(1) of Vietnam's Law on Insurance Business 2000; article 247 and 248 of Vietnam's Maritime Code 2005

⁵⁹ S.5 of the MIA 1906 (UK); *Macaura v Northern Assurance Co.* [1925] A.C. 619

⁶⁰ *Napier v Hunter* [1993] A.C. 713

⁶¹ J Birds, "Insurance: subrogation in the House of Lords", (1993) J.B.L 294; M Hemsworth, "Subrogation: the problem of competing claims to recovery monies", (1998) J.B.L 111; M Luey, "Proprietary remedies in

Commission have, in recent years, published Issue Papers and Consultation Papers for insurance law reform, such as: the Issues Paper 4,⁶² and the Law Commissions' Joint Consultation Paper No 201.⁶³ In this study, the English current law and the Law Commissions' reform proposals will be considered to in order to find better solutions to improve Vietnamese laws.

Research on Vietnamese insurance laws has been limited to the statutes directly governing insurance activities, such as the Law on Insurance Business 2000, the Maritime Code 2005, and the Civil Code 2005. Of these three statutory documents, the first two are specific law and the last is general law and is only referred to when the former has no provision governing the issue in question.⁶⁴ This thesis does not examine delegated legislation because all of the legal principles on insurance are laid down in the statutes, and the delegated legislation only describes in detail the practices of insurance activities.⁶⁵

4. METHODOLOGY:

4.1. Comparative method:

This study adopts a comparative method. Comparative study of laws between two or more legal systems is a better way to improve one's own nation's law. The method may not only reveal similarities and differences between different legal systems, but may also identify problems that exist in each system.⁶⁶ As societies frequently face similar problems, comparative study can work as a tool to assess how different legal systems deal with similar issues. Through comparing different countries' laws, better solutions could be found which

insurance subrogation", (1995) 25 Victoria.U.Wellington.L.Rev. 499; C Mitchell, "Subrogation and insurance law: proprietary claims and excess clauses", (1993) L.M.C.L.Q 192; Z Jing, "The Confusion between Subrogation and Assignment in the Insurance Law of the People's Republic of China 1995-A Critical Analysis on Article 44 of the Insurance Law", (2002) J.B.L. 608; J Parker, "The made whole doctrine: Unraveling the enigma wrapped in the mystery of insurance subrogation", (2005) 70 Mo.L.Rev 723; A Tar, "Subrogation and the Ash Wednesday bushfire disaster", (1987-1988) 11 Adel. L. Rev. 232; G Veal, "Subrogation: The duties and obligations of the insured and rights of the insurer revisited", (1992) 28 Tort & Ins.L.J 69; SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985)

⁶² The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008)

⁶³ Chapter 3: Insurable interest in the UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012)

⁶⁴ For more details, see section 3.1 of Chapter 2: Vietnam's insurance industry and insurance law

⁶⁵ See section 3 and 4 of Chapter 2: Vietnam's insurance industry and insurance law

⁶⁶ M. Van Hoeke and M. Warrington, "Legal cultures, legal paradigms and legal doctrine: towards a new model for comparative law", (1998) 47 Int'l & Comp. L.Q 495, p497; J. Gillespie, "Transplanted company law: an ideological and cultural analysis of market-entry in Vietnam", (2002) 51 Int'l & Comp. L.Q 641, p642

can be introduced to solve problems in one's own country's laws. In this study the similarities and differences between Vietnamese law and English law relating to the principle of indemnity and doctrines of subrogation and insurable interest will be thoroughly evaluated and compared. Other countries' laws will also be considered if necessary. The purpose of comparing these countries' laws is to find better approaches to improve Vietnamese law.

Judicial practice in terms of insurance law will also be considered. In the Vietnamese legal system, unlike in the English system, precedent or case law has a trivial role.⁶⁷ The decisions of a higher court, according to the hierarchy of Vietnamese court system, are not binding on a lower court in dealing with disputes with similar facts.⁶⁸ Judges make decisions based on their own understanding and interpretation of the statutory laws.⁶⁹ So it is not uncommon that different judgements are given to similar cases. This problem could be reduced or avoided if the rules of law are clearly stipulated.

4.2. Literature Survey

The second method in this research is to carry out a literature survey of primary and secondary sources. The primary source includes statutes and case law, such as the Vietnamese statutory laws of the Civil Code 2005, the Maritime Code 2005, the Law on Insurance Business 2000, and English statutes and case law. Relevant provisions of these laws will be critically examined and analysed throughout the work.

The secondary source consists of books, journal articles and internet materials on indemnity principle, insurable interest and subrogation. These materials give a comprehensive view of the principle of indemnity and its relation to other doctrines derived from the indemnity principle.

⁶⁷ Pham Duy Nghia, *Chuyen khao luat kinh te*, (NXB Dai hoc Quoc gia, 2004), p211 [Trans: Pham Duy Nghia, *Vietnamese Business Laws*, (Publisher of National University, 2004)]

⁶⁸ Do Van Dai, "Toa an nhan dan toi cao voi van de giai thich phap luat dan su o Viet Nam" (2008) 6 *Tap chi Toa an nhan dan* 25, p25 [Trans: Do Van Dai, "The Supreme People's Court with its civil law interpretation in Vietnam", (2008) 6 *Journal of People's Court* 25]; Pham Duy Nghia, *Chuyen khao luat kinh te*, (NXB Dai hoc Quoc gia, 2004), p219 [Trans: Pham Duy Nghia, *Vietnamese Business Laws*, (Publisher of National University, 2004)]

⁶⁹ Do Van Dai, "Toa an nhan dan toi cao voi van de giai thich phap luat dan su o Viet Nam" (2008) 6 *Tap chi Toa an nhan dan* 25, p26 [Trans: Do Van Dai, "The Supreme People's Court with its civil law interpretation in Vietnam", (2008) 6 *Journal of People's Court* 25]

4.3. The analysis of judicial and industrial practices:

Sometimes laws exist but are not well implemented. The practical issue will be discussed to explore what are the gaps between law and practice in the Vietnam insurance market. This can be illustrated by examining some insurance companies' policy clauses.

Vietnamese judicial practice is also an issue in this thesis (Courts' decisions). The analysis of courts' decisions is very helpful in understanding how Vietnamese judges or arbitrators interpret the provisions relating to the principle of indemnity and the doctrines of subrogation and insurable interest in Vietnam's insurance laws.

4.4. Doctrinal legal analysis

Doctrinal analysis plays a very important part in this research. This method allows the thesis to inherit from previously existing materials and research.⁷⁰ It will also be used to examine different secondary sources (textbooks and articles, and so on) with the aim of discovering different opinions from different academic writers⁷¹ on the principle of indemnity and other principles deriving from the principle of indemnity under Vietnamese and English insurance laws. Those different opinions reflect all aspects of the hypothetical question to which this thesis attempts to find answers. For instance, under the subrogation principle, there are several approaches to allocation of subrogation recovery from a third party wrongdoer between the insurers and the insureds. Some of them are in favour of the insurers, and some in favour of the insureds. Each approach is based on different legal grounds. This thesis will examine and critically analyse those approaches in order to find out the most suitable approach for Vietnam's insurance market.

5. STRUCTURE OF THE STUDY

The study comprises six chapters:

Chapter One is a general introduction to the research. It explains the reasons for choosing to study the indemnity principle, the aims and objectives, the methodology, the outcomes and the structure of the research.

⁷⁰ Dao Tri Uc, "Basic information of legal research- a case study of Vietnam" in the Project of "Doing legal research in Asian countries: China, India, Malaysia, Philippines, Thailand, and Vietnam" conducted by the Institute of Developing Economies (IDE-JETRO), Japan, 2003 (IDE Asian Law Series No. 23), p225

<<http://www.ide.go.jp/English/Publish/Download/Als/pdf/23.pdf>> accessed 09 June 2013

⁷¹ *Ibid*

Chapter Two gives a brief overview of Vietnam's insurance industry and insurance law. The recent development of Vietnam's insurance industry is represented, particularly in the context of Vietnam's current integration into international trade. The rapid growth of Vietnam's insurance industry creates an urgent need for reforming Vietnamese laws of insurance. Some current commercial practices in Vietnam's insurance market were introduced by foreign insurance companies, revealing some drawbacks in Vietnamese legislation on insurance. The description of the Vietnamese legal framework for insurance contracts shows how an insurance contract is governed by Vietnam's legislation and delegated legislation. A summary of Vietnamese legal method and judicial system is also given. The ways of interpretation of insurance law by judges are examined in detail, focusing on variation on judges' points of view and provisions applicable to similar issues.

Chapter Three examines the fundamental principle of indemnity in insurance law, and the nature of the indemnity principle is critically analysed. The history and development of the principle of indemnity in English insurance law are also examined. The latest developments of English case law and current practices in the London insurance market form the basis for discussion on sufficient solutions to the problems. Comparison of the similarities and differences in English and Vietnamese insurance laws and practices in the light of the indemnity principle is a vital part in this chapter. The comparison explains precisely different approaches in both legal systems. Underlying reasons for the differences and the consequences of the differences affecting Vietnam's insurance business are identified.

Chapter Four is concerned with the principle of insurable interest. Insurable interest is a basic requirement for any insurance contract. In order for an insurance policy to be valid, the policyholder must have a sufficient interest in the subject matter of the insurance. The insurable interest doctrine requires that a policyholder must gain a benefit from the preservation of the subject matter of the insurance or suffer a disadvantage should it be lost. As far as the purpose of the indemnity principle is concerned, if the policyholder cannot show that he has an insurable interest in the subject matter of the insurance, he could not have a claims paid under the insurance policy. However, English law on insurable interest in indemnity contract is currently confusing because of the enactment of the English Gambling Act 2005. It seems that the Gambling Act removes the requirement of insurable interest in indemnity insurance contracts. This confusion creates difficulties for both insurers and policyholders in understanding and applying the English law on insurable interest. Insurable

interest is also a requirement for enforcement of an insurance policy in Vietnam's law of insurance. Nonetheless, there is no clear, detailed ruling on the issue in Vietnamese laws. Weaknesses of Vietnamese laws on insurable interest are thoroughly evaluated in this chapter.

Chapter Five deals with the legal issues arising from the principle of subrogation. This principle is only applicable to indemnity contracts. The insurer's right of subrogation is the fundamental correlative of the principle of indemnity. There are two aspects of subrogation doctrine. The first aspect is that the insured cannot make a profit from his loss. The second aspect is that the insurer who has indemnified his insured has a right to step into the shoes of the insured and in the insured's name pursue any right of action available to the insured which may diminish the loss insured against. All the aspects of the subrogation doctrine regarding the indemnity principle are critically analysed. Thorough evaluation of the priority of allocation of the compensation amount from the third party responsible for the loss among the insureds and the insurers will identify unfairness to the insureds in English law on subrogation. Part of this chapter is devoted to the comparison of subrogation doctrine in English and Vietnamese laws.

The concluding chapter focuses on possibilities of applying the present English indemnity frameworks to Vietnam's insurance law. The advantages and disadvantages of strict application of the English mechanism are discussed in details. Recommendations for amendment to the provisions relating to the indemnity regime in Vietnam's insurance law are considered in accordance with Vietnam's legal frameworks, level of economic development and culture. Proposals for amendment of Vietnam's insurance law will be put forward as a conclusion to the whole research.

CHAPTER 2: VIETNAM'S INSURANCE INDUSTRY AND INSURANCE LAW

The purpose of this chapter is to provide a short overview of the key aspects of Vietnam's economy and legal system in general and Vietnam's insurance industry and insurance law in particular. This overview will provide an essential framework for discussions in later chapters, putting recommendations for amendment to provisions relating to the indemnity regime in Vietnam's insurance law in accordance with Vietnam's legal system, level of economic development and culture.

Any attempt to describe the Vietnamese legal system merely in terms of recent legislation or legal institutions overlooks important elements of the system. The political, economic and social elements of the Vietnamese system, under which Vietnamese insurance laws emerged, are considered in this Chapter. Understanding those elements would help people to know the reasons for the problems in Vietnamese insurance laws. Vietnam as a whole has developed very rapidly over the last 25 years,⁷² as has its legal system. Since the current legal framework of Vietnamese insurance law has been formed in less than two decades, as compared with the century-long development of some mature Western insurance laws (such as English insurance law), it is inevitable that there are a number of shortcomings in the Vietnamese insurance laws.⁷³ Therefore, in order to understand Vietnamese insurance laws better, it would be helpful to consider the historical background before commencing detailed discussion of the indemnity principle and related doctrines in the Vietnamese insurance legal system.

1. OVERVIEW OF THE VIETNAMESE ECONOMY

1.1. Vietnamese economy before WTO entry

Economic reform was first addressed in the Sixth Committee of the Vietnamese Socialist Republic in December 1986, when the country was confronting a severe economic crisis. During that time, the economy experienced stagnating growth: a low growth rate (1 to 2%), a

⁷² Average GDP growth rate per annum is about 7%, see General Statistics Office <<http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=5690>>

⁷³ See section 3.2 of Chapter 4: Insurable interest and section 4.1 of Chapter 5: Subrogation

high inflation rate (above 700%) and a large budget deficit.⁷⁴ The Committee agreed on implementing absolute reform policies which concentrated on boosting the economy in order to achieve a macro-economic stabilization, to promote economic growth and to abolish poverty. The basic concept of economic reform was transformation from a centrally planned economy into a socialist-oriented market economy with the involvement of many participants under state control.⁷⁵

From the initiation of the reform until now, economic reform has had many positive effects on Vietnam's national economy. The country has escaped from social and economic crises which lasted for many years and has reached the stage of accelerating industrialization and modernization. Commercial and social life was markedly improved and poverty was reduced. A market-oriented economy associated with global economic integration has been formed and has worked effectively. The image of Vietnam has been improved in the world.

1.1.2 Economic modernization and structural reforms

1.1.2.1 The Vietnamese economy has been transformed into an industrialized and modernized economy with many new industries and advanced technology

Consumer goods and the manufacturing industry have developed to meet the need for high quality products for domestic consumption and export.⁷⁶ Textiles, garments, leather, chinaware, porcelain, glass, wood, rubber, plastic, metal consumer units and the electrical and electronics industries have developed remarkably in this period.⁷⁷ The automobile and motorcycle assembly industry became established.⁷⁸

⁷⁴ Hoang Duc Than & Dinh Quang Ty, *Tang truong kinh te va tien bo, cong bang xa hoi o Viet Nam*, (NXB Chinh tri quoc gia, 2010) [Trans: Hoang Duc Than & Dinh Quang Ty, *Economic growth and social justice in Vietnam* (National Politics Publishing House, 2010), p123; see also Documentaries of the 6th National Congress of Vietnam's Communist Party, available at

http://123.30.190.43:8080/tiengviet/tulieuvankien/vankiendang/details.asp?topic=191&subtopic=8&leader_topic=223&id=BT1260354904

⁷⁵ Documentaries of the 6th National Congress of Vietnam's Communist Party; see also: "Mười tám năm đổi mới" [translated: 18 years of economic renovation], accessed on 24/12/2012

<<http://www.chinhphu.vn/portal/page/portal/chinhphu/noidungchinhsachthanhtuu?categoryId=799&articleId=2957>>

⁷⁶ From 1992 to 2002, the Vietnam's export growth rate was about 24.69%, see also: International Monetary Fund, "Vietnam: selected issues and statistical appendix" (2002) available at

<<http://www.imf.org/external/pubs/ft/scr/2002/cr0205.pdf>>

⁷⁷ In 1999, garment exports to Japan and the EU were USD 500 million, and USD 640 million, respectively, see General Statistics Office <<http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=5692>>

⁷⁸ Industry and construction increased from 22.7% GDP during 1990s to 41% in 2005, see General Statistics Office at <<http://www.gso.gov.vn/default.aspx?tabid=393&idmid=3&ItemID=13170>>. In 1995, Toyota was the first company to build auto assembly joint-venture in Vietnam. In 2001, the first car assembly factory that was

Many important projects involving thermal power, hydropower and cement were exploited, contributing to an increase of production capacity for the economy. Several new industries with potential prospects such as oil and gas, construction and ship repair were initiated.

In agriculture, centralized production areas emerged for major products and goods, including long-term industrial plants (rubber, tea, coffee, cashew, etc.). Long term industrial plants emerged, as well as fishing and mariculture areas.⁷⁹

A transportation industry was initiated to develop sea transport, inland waterways, and to improve the capacity of sea and river ports. Railway transport has been improved. Several main roads connecting major cities has been renovated and upgraded.⁸⁰

Foreign trade activities have been gradually diversified and have made an impact on regional and world markets.⁸¹ Garments, footwear,⁸² electronic assembly products, fishery and agricultural products, rice, coffee, rubber and crude oil became major export products.⁸³ However, the main export products were still semi-processed goods and raw materials, since sophisticated processing and advanced technological products are in shortage.⁸⁴

invested by a Vietnamese company was built; see also: Documentaries of the 7th National Congress of Vietnam's Communist Party, Communist Party of Vietnam Online Newspaper, http://123.30.190.43:8080/tiengviet/tulieuvankien/vankiendang/details.asp?topic=191&subtopic=8&leader_topic=224&id=BT1260354741

⁷⁹ Documentaries of the 7th National Congress of Vietnam's Communist Party, Communist Party of Vietnam Online Newspaper, http://123.30.190.43:8080/tiengviet/tulieuvankien/vankiendang/details.asp?topic=191&subtopic=8&leader_topic=224&id=BT1260354741

⁸⁰ Documentaries of the 7th National Congress of Vietnam's Communist Party, Communist Party of Vietnam Online Newspaper, http://123.30.190.43:8080/tiengviet/tulieuvankien/vankiendang/details.asp?topic=191&subtopic=8&leader_topic=224&id=BT1260354741

⁸¹ Vietnam experienced a rapid increase in economic integration with the rest of the world during the 1990s. The share of trade, as measured by the ratio of imports and exports to GDP more than doubled from 44 percent in 1990 to 94 percent in 2000. In 1990s, Vietnam's exports increased five folds, from about USD 3 billion in 1993 to over USD 14 billion in 2000, see General Statistics Office <http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=5692>

⁸² Exports of garments and footwear increased most rapidly in the period of 1993-1997. Their shares in total exports increased from 8% in 1993 to 15% in 1997, and from 2% in 1993 to 15% in 1997, respectively, replacing coffee and rice as major export earners, see General Statistics Office <http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=5692>

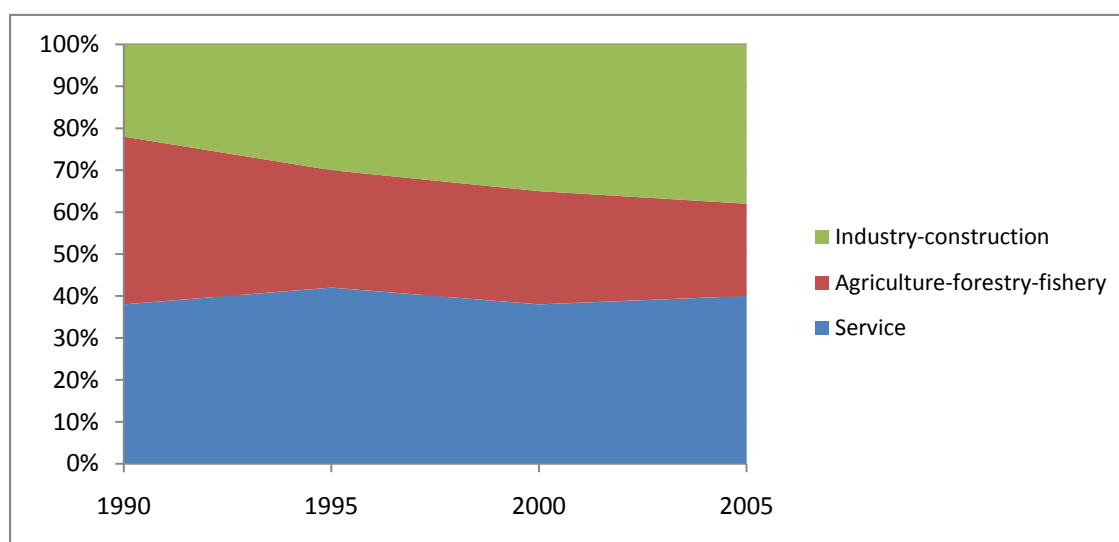
⁸³ From 1998 to 2000, oil revenue jumped by 2.5 percent of GDP to 6.75% in 2000, reflecting 28% increases in volume of crude oil exports, see General Statistics Office <http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=5692>

⁸⁴ Documentaries of the 7th National Congress of Vietnam's Communist Party, Communist Party of Vietnam Online Newspaper, http://123.30.190.43:8080/tiengviet/tulieuvankien/vankiendang/details.asp?topic=191&subtopic=8&leader_topic=224&id=BT1260354741

1.1.2.2 Vietnamese economic structure shifts in the direction of industrialization and modernization, decrease in the agriculture sector

During this period, the Vietnamese economy achieved a substantial growth rate. The structure of the economy shifted to modernization and industrialization, and promoted the construction, service industry, while demoting agriculture, forestry and fishery.⁸⁵ Industry and construction increased from 22,7% GDP during 1990s to 41% in 2005; while agriculture, forestry and fishery declined from 38.7% during 1990s to 20.9%, services remained at 38 to 48% GDP.⁸⁶ (See Chart 1 below)

Chart 1: The structure of Vietnamese economy from 1990 to 2005



Source: General Statistics Office (GSO)

The most noticeable thing is that, although the percentage of the agriculture sector in the Vietnamese economic structure went down, Vietnam shifted from being a rice importer before the 1990s to being the second largest rice exporter in the world from 2001 (standing slightly behind Thailand)⁸⁷ and became the second largest coffee exporter (just slightly behind Brazil).⁸⁸ Agricultural products are diverse and wide-ranging and meet the need of 85

⁸⁵ See Chart 1 The structure of Vietnamese economy from 1990 to 2005

⁸⁶ General Statistics Office <<http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=5694>>; see also IMF, “Economic diversification in LICs: stylized facts and macroeconomic implication”, (2012) available at <<http://www.imf.org/external/pubs/ft/sdn/2012/sdn1213.pdf>>

⁸⁷ Statistics of Organisation of Rice Exporting Countries (OREC) at <http://www.orecinternational.org/>

⁸⁸ Statistics of International Coffee Organisation at <http://www.ico.org/historical/2000-09/PDF/EXPORTSCALYR.pdf> ; see also: <http://vov.vn/Kinh-te/Viet-Nam-tro-thanh-nuoc-xuat-khau-ca-phe-lon-nhat-the-gioi/219913.vov>

million people, and are exported to other countries in the area such as China, Japan, Korea and ASEAN.

The service industries have achieved significant development; whereas they existed previously, as only basic services provided by state-owned companies they now provide a wide range of services to meet the needs of society.

1.1.3 Achievement of a high growth rate

The growth of the economy increased the demand for insurance, promoting the development of the insurance industry.⁸⁹ From 1986 to 2006, the Vietnamese economy obtained a stable high growth rate. The average GDP growth rate per annum over the period 1986-2005 remained at 7%,⁹⁰ with agriculture, forestry and fishery increasing by 3.7%.⁹¹ Construction and industry rose by 13.5%; and the service sector went up by 6.7%.⁹² In comparison with Asian countries, Vietnam had achieved a significant growth. For instance, the average GDP growth rate over the period 1987-2004 of China, Korea, Indonesia, Malaysia, Thailand and Singapore was 9.2%, 6.5%, 4.9%, 6.7%, 6.1% and 7.0% respectively.⁹³

Economic growth rescued the country from poverty and under-development so that income per capita was improved. The GDP per capita of Vietnam increased considerably, from 86 USD per annum in 1988 to 638 USD in 2005 and reached 720 USD in 2006.⁹⁴ Over the period 1986-2005, GDP per capita obtained a growth rate of 5.28%.⁹⁵ (*see Chart 2 below*)

⁸⁹ See section 2.3 of this Chapter

⁹⁰ General Statistics Office <<http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=5690>>

⁹¹ *Ibid*

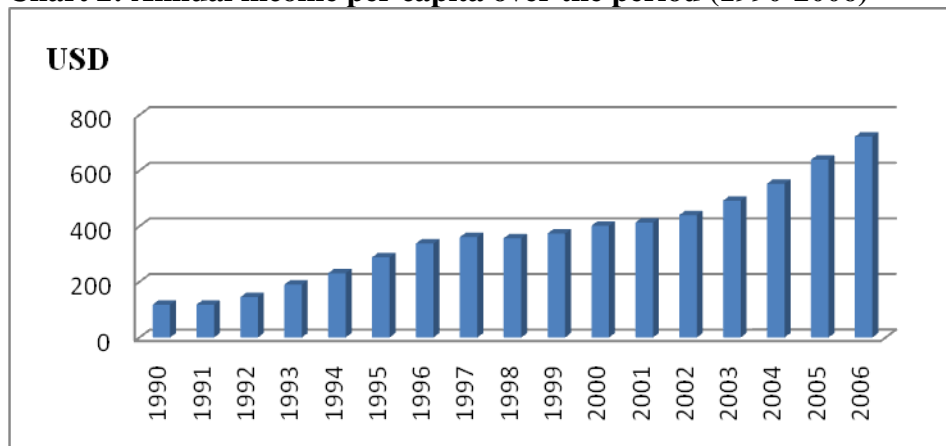
⁹² *Ibid*

⁹³ Documentaries of the 9th National Congress of Vietnam's Communist Party, Communist Party of Vietnam Online Newspaper, at <http://www.chinhphu.vn/portal/page/portal/chinhphu/NuocCHXHCNVietNam/ThongTinTongHop/noidungvankiendaihoidang?categoryId=10000714&articleId=10038377>; see also Ministry of Planning and Investment, *The domestic and international context of Vietnam, a research on development strategy 2011-2020*, (Finance Publishing House, 2008) p.13

⁹⁴ See Chart 2: Annual income per capita over the pperiod (1990-2006), source: General Statistics Office <<http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=5690>>

⁹⁵ Ministry of Planning and Investment, *The domestic and international context of Vietnam, a research on development strategy 2011-2020*, (Finance Publishing House, 2008) p.13

Chart 2: Annual income per capita over the period (1990-2006)



Source: General Statistics Office (GSO)

1.2. Vietnamese economy after WTO entry

Vietnam officially became the 150th member of the World Trade Organization (WTO) on 11 January 2007. This landmark commemorated a major progress of the Vietnamese economy. The next section provides several primary points of economic development since WTO entry.

1.2.1. Closer integration into the global economy

Despite late entry into the WTO in 2007, the policy of integration into the global economy has been gradually implemented over the past 25 years. Vietnam has signed bilateral and multilateral free trade agreements and set up trade relations with a number of countries,⁹⁶ for instance, joining the ASEAN Free Trade Area (AFTA) in 1997, and entering into the Bilateral Trade Agreement between Vietnam and USA in 2000.⁹⁷

Thanks to its WTO accession, Vietnam has had greater opportunities to access enormous markets of more than 150 member States. In addition, Vietnam has agreed to an open market and is deeply integrated into the world economy due to the commitments it made when joining the WTO.⁹⁸

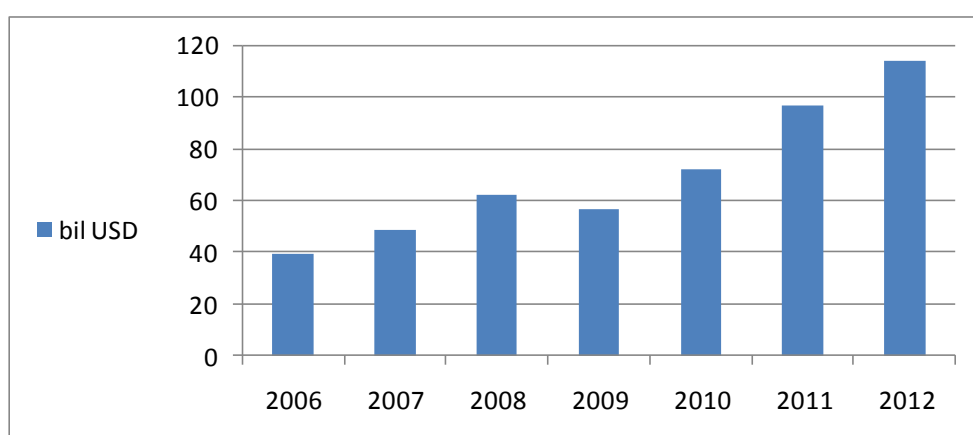
⁹⁶ Vu Nhu Thang, "Necessary reform of insurance business law in Vietnam after its accession to the WTO: prudential regulatory aspects" (2007) 12(6) *Fordham Journal of Corporate & Financial Law* 977, p977

⁹⁷ Vietnam's export to America increased from USD 95 million (2.3 percent of total exports) in 1995 to USD 770 million (6.7 percent of total exports) in 2000. The principal exports are seafood, textiles, footwear, and agricultural goods, see International Monetary Fund <<http://www.imf.org/external/pubs/ft/scr/2002/cr0205.pdf>>

⁹⁸ Vietnam has trade relations with over 140 countries, investment relations with about 70 countries and regions, attracting more foreign investment. See: Documentaries of the 9th National Congress of Vietnam's Communist Party, Communist Party of Vietnam Online Newspaper, at <http://www.chinhphu.vn/portal/page/portal/chinhphu/NuocCHXHCNVietNam/ThongTinTongHop/noidungvankiendaihoi dang?categoryId=10000714&articleId=10038377>

One of the most substantial impacts of world economic integration is that export capacity has improved significantly. The export turnover of Vietnam achieved a value of USD 48.6 billion in 2007,⁹⁹ which shows an increase of 21.9% compared with 2006. The following year 2008 witnessed a total value of USD 67.2 billion from export,¹⁰⁰ which rose by 29.1% compared with 2007. However, export value decreased to USD 57.1 billion due to the negative effects of the global economic downturn. In the following years, export turnover recovered and attained 114.6 billion on 2012.¹⁰¹ (see Chart 3 below)

Chart 3: Export turnover of Vietnam over the period of 2006 - 2012



Source: General Statistics Office (GSO)

Markets for export became more diversified, and Vietnam has integrated deeply into large markets such as the USA and Europe.¹⁰² Meanwhile, ASEAN, Japan, China and Korea are its largest trading partners in terms of export value, which account for 70% of the export turnover of Vietnam.¹⁰³

⁹⁹ Source: General Statistics Office at

<<http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=8555>>

¹⁰⁰ Source: General Statistics Office at

<<http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=10477>>

¹⁰¹ Source: General Statistics Office at

<<http://www.gso.gov.vn/default.aspx?tabid=393&idmid=3&ItemID=13170>>

¹⁰² Viện nghiên cứu quản lý kinh tế trung ương CIEM, *Tác động của hội nhập kinh tế quốc tế đối với nền kinh tế sau ba năm Việt Nam gia nhập WTO*, (2010) available at

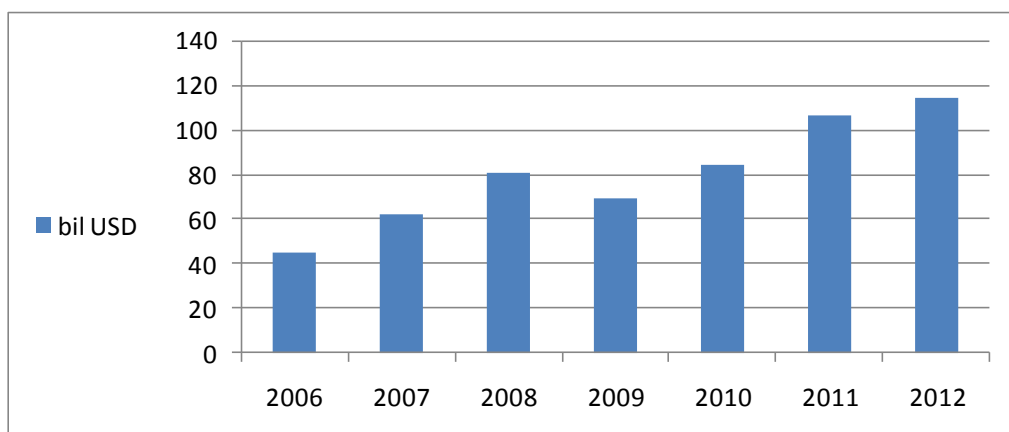
<<http://www.trungtamwto.vn/sites/default/files/Bao%20cao%20KT-XH%203%20nam%20WTO.pdf>> [Trans: Vietnam's Central Institute for Economic Management (CIEM), *The impact of international economic integration on Vietnam's national economy: 03 years after becoming a member of WTO*, (2010)] p26

¹⁰³ Source: General Statistics Office

<<http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=13492>>; see also: Viện nghiên cứu quản lý kinh tế trung ương CIEM, *Tác động của hội nhập kinh tế quốc tế đối với nền kinh tế sau ba năm Việt Nam gia nhập WTO*, (2010) available at <<http://www.trungtamwto.vn/sites/default/files/Bao%20cao%20KT->

Along with the growth of export, import value has experienced a significant growth. The total value of imports in 2007 reached 62.8 billion USD,¹⁰⁴ an increased of 39.8% compared to 2006. Import turnover declined considerably in 2009¹⁰⁵ under the impact of worldwide economic crises but showed a remarkable recovery over the next two-year. Specifically, the total amount of imports attained a level of 114.2 billion USD in 2012.¹⁰⁶ (see Chart 4 below)

Chart 4: Import turnover of Vietnam in the period 2006-2012



Source: General Statistics Office

1.2.2. Maintaining stable growth

Despite the financial crisis and the global economic downturn, Vietnam maintained relatively stable growth. Average growth rate in the period 2007-2012 was 6.3%.¹⁰⁷ The size of the gross domestic product (GDP) in 2010 reached USD 103.6 billion,¹⁰⁸ 3.26 times more than in 2000; GDP in 2012 was USD 136 billion.¹⁰⁹ Income per capita was USD 1,174 in 2010,¹¹⁰

[XH%203%20nam%20WTO.pdf](#)> [Trans: Vietnam’s Central Institute for Economic Management (CIEM), The impact of international economic integration on Vietnam’s national economy: 03 years after becoming a member of WTO, (2010)] p28

¹⁰⁴ Source: General Statistics Office at <http://www.gso.gov.vn/default.aspx?tabid=512&idmid=5&ItemID=8555>>

¹⁰⁵ See Chart 4: Import turnover of Vietnam in the period 2006-2012

¹⁰⁶ Source: General Statistics Office at <http://www.gso.gov.vn/default.aspx?tabid=393&idmid=3&ItemID=13170>>

¹⁰⁷ Source: General Statistics Office at <http://www.gso.gov.vn/default.aspx?tabid=388&idmid=3&ItemID=12959>>

¹⁰⁸ International Monetary Fund (IMF), “Vietnam: staff report for the 2012 article IV consultation”, (2012) available at <http://www.imf.org/external/pubs/ft/scr/2012/cr12165.pdf>>

¹⁰⁹ *Ibid*

¹¹⁰ *Ibid*

nearly 3 times higher than in 2000 (USD 401.5), and reached USD 1596 in 2012,¹¹¹ 11.43 times higher than in 1992 (USD 140).¹¹² Vietnam officially moved from the group of low-income countries to the group of middle-income countries in 2008,¹¹³ which is an encouraging achievement. In summary, although not having achieved such high growth rates as China, Vietnam has achieved relatively high and stable growth compared to other countries in the ASEAN region and the world. (see Table 1 below)

Table 1: GDP growth of some ASEAN countries in 2007-2011¹¹⁴

Unit: %

Year \ Country	2007	2008	2009	2010	2011	2012
Cambodia	10.2	6.7	0.1	6.0	7.1	-
Indonesia	6.3	6.0	4.6	6.2	6.5	-
Laos	7.6	7.8	7.5	8.5	8.0	-
Malaysia	6.3	4.8	-1.5	7.2	5.1	-
Philippines	6.6	4.2	1.1	7.6	3.9	-
Singapore	8.9	1.7	-1.0	14.8	4.9	-
Thailand	5.0	2.5	-2.3	7.8	0.1	-
Brunei	0.2	-1.9	-1.8	2.6	2.2	-
Vietnam	8.5	6.3	5.3	6.8	5.9	5.03

Source: World Bank

1.2.3. Ensuring macroeconomic stability

In the period from 2008 until the present, the world economy has witnessed complex volatility due to the impacts of the financial crisis and the economic recession. These

¹¹¹ World Bank, “Data GDP per capital (current dollars)”, accessed 29/12/2012, <<http://data.worldbank.org/indicator/NY.GDP.PCAP.CD>>

¹¹² Documentaries of the 11th National Congress of Vietnam’s Communist Party, Communist Party of Vietnam Online Newspaper, at http://123.30.190.43:8080/tiengviet/tulieuvankien/vankiendang/details.asp?topic=191&subtopic=8&leader_topic=989&id=BT531160752

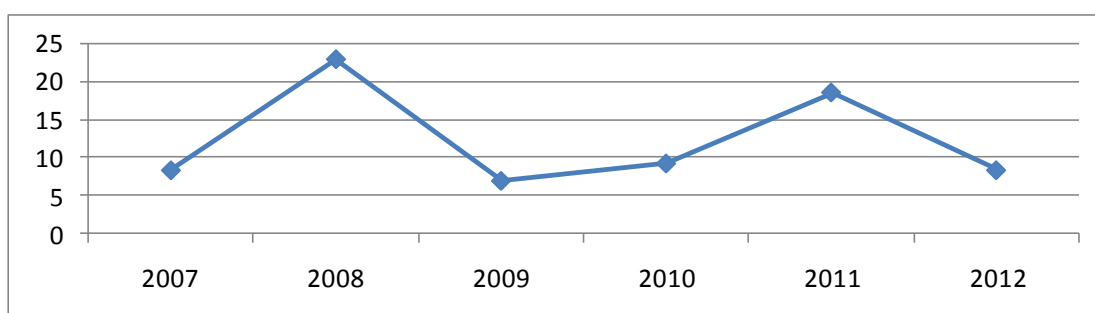
¹¹³ World Bank, “Data GDP per capital (current dollars)”, accessed 29/12/2012, <<http://data.worldbank.org/indicator/NY.GDP.PCAP.CD>>; see also International Monetary Fund (IMF), “Vietnam: staff report for the 2012 article IV consultation”, (2012) available at <<http://www.imf.org/external/pubs/ft/scr/2012/cr12165.pdf>>

¹¹⁴ Source: World Bank, Data GDP growth (annual%), accessed on 29/12/2012, at <<http://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?page=1>>

changes, to some extent, have had an influence on the macro-economic situation of Vietnam. However, Vietnam has successfully implemented macro-economic stabilization policies.

Due to thorough integration into the world economy, the volatility of the world economy imposed a fast and powerful impact on Vietnam. This is most evident in Vietnam's inflation. From 2008 until now, inflation was complicated, with differing trends. In the 2007-2008 period, inflation increased continuously, reaching 23% in 2008,¹¹⁵ the highest in the ASEAN countries. Two years later, inflation was brought down to less than 10%, before soaring back to 18.6% in 2011,¹¹⁶ and was under control again at 8.31% in 2012.¹¹⁷ Apart from external factors, high inflation was also caused by the intrinsic weakness of the Vietnamese economy. For a long time before 2012, Vietnam had adopted policies prioritizing economic growth and had pursued macroeconomic policies in the direction of expansion, rampant investment and excessive support for state-owned corporations. (*see Chart 5 below*)

Chart 5: Average annual inflation rate in Vietnam from 2007 to 2012



Source: General Statistics Office

To cope with the impact of the financial crisis and the global economic downturn and to ensure the sustainable growth of Vietnam, many macro-economic stabilizing measures have been implemented.¹¹⁸ These measures have made positive impacts. Inflation fell sharply to

¹¹⁵ Source: General Statistics Office <<http://www.gso.gov.vn/default.aspx?tabid=628&idmid=4>>

¹¹⁶ Source: General Statistics Office <<http://www.gso.gov.vn/default.aspx?tabid=628&idmid=4>>

¹¹⁷ Source: General Statistics Office <<http://www.gso.gov.vn/default.aspx?tabid=628&ItemID=13483>>

¹¹⁸ Resolution No. 11/NQ-CP on 24/2/2011 of the Government on the measures to curb inflation, stabilize the macro-economy and ensure social security. The measures are: (i) shift the focus from growth-boosting policy to inflation-curbing one; (ii) implement tight yet flexible monetary policy and at the same time tight and economical fiscal policy (restructuring and improving the efficiency of spending, especially investment); combine monetary policy with fiscal one, aiming to curb inflation and to stabilize the macro-economy. (iii) promote the production, business and export and use of efficient energy-saving methods, while curbing trade deficit; (iv) stabilize exchange rate; (v) restructure commercial banks ; (vi) restructure the real estate market.

8.31% in 2012.¹¹⁹ Foreign exchange reserves recovered, reaching USD 23 billion in 2012, up from USD 9 billion in late 2011. Bank lending rates decreased from 21% / year in 2011 to 15% / year in 2012. Relatively stable exchange rates have been maintained.¹²⁰

1.2.4. Attracting more foreign investment

Foreign investment has contributed significantly to facilitating Vietnam's deeper integration into international economic life. Foreign investment is an important source of additional capital, satisfying the needs of social development and economic growth and contributing to economic and labour restructuring and the upgrading of production capacity.¹²¹ Vietnam has implemented policies aimed at creating a legal environment which is more transparent, more equitable and more open, along with conditions and incentives to attract foreign investors.¹²²

FDI inflow to Vietnam increased sharply in the period 2006-2008. Registered capital was at USD 21 billion in 2007¹²³ (up 75% compared to 2006), and reached a peak of USD 71 billion in 2008¹²⁴ (an increase of 238% compared to 2007). From 2009 to 2012, FDI inflow decreased due to the impacts of the world economic crisis. Registered capital was at USD 23 billion, USD 20 billion, USD 15.5 billion and USD 13 billion in 2009, 2010, 2011 and 2012 respectively.¹²⁵ However, the implemented amount was maintained at USD 10-11 billion in this period.¹²⁶

Foreign-invested enterprises contributed to a significant part of Vietnam's export and import turnover. In 2012, the export turnover of foreign-invested enterprises reached USD 73.4

¹¹⁹ Source: General Statistics Office <<http://www.gso.gov.vn/default.aspx?tabid=628&ItemID=13483>>

¹²⁰ Nguyen Dinh Cung, "Ổn định kinh tế vĩ mô – điểm sáng nền kinh tế năm 2012", (2012) [Trans: Nguyen Dinh Cung (2012), "Macroeconomic stability - economic bright spots in 2012", (2012)] accessed on 30/12/2012 at <<http://baodientu.chinhphu.vn/Home/On-dinh-kinh-te-vi-mo--diem-sang-nen-kinh-te-nam-2012/201212/158024.vgp>>

¹²¹ Bo Ke hoach va Dau tu, 20 nam dau tu nuoc ngoai tai Viet Nam [translated: Ministry of Planning and Investment, 20 years of foreign investment in Vietnam] at <http://fia.mpi.gov.vn/News.aspx?ctl=newsdetail&p=2.44&aID=507>

¹²² Documentaries of the 11th National Congress of Vietnam's Communist Party: Strategy for Socio-Economic Development 2011-2020, Communist Party of Vietnam Online Newspaper, at http://123.30.190.43:8080/tiengviet/tulieuvankien/vankiendang/details.asp?topic=191&subtopic=8&leader_topic=989&id=BT531160752

¹²³ General Statistics Office at < <http://www.gso.gov.vn/default.aspx?tabid=392&idmid=3&ItemID=13100>>

¹²⁴ *Ibid*

¹²⁵ *Ibid*

¹²⁶ General Statistics Office at < <http://www.gso.gov.vn/default.aspx?tabid=392&idmid=3&ItemID=13100>> and Ministry of Planning and Investment, "Statistics on foreign direct investment" at <http://fia.mpi.gov.vn/News.aspx?ctl=newsdetail&aID=1395>

billion,¹²⁷ an increase of 33.2% compared to 2011, and accounting for 64% of total exports.¹²⁸ The import turnover reached USD 60.33 billion,¹²⁹ up 23.5% compared to 2011, and accounting for 52.76% of total imports.¹³⁰

1.2.5. Continuing economic structure transformation

Vietnam continues to pursue policies of economic restructuring towards industrialization and modernization. It not only assists industries where it has competitiveness, with products containing marginal modern technology such as footwear and apparel, but also industries manufacturing hi-tech products and applying advanced technologies. This is reflected in Vietnam's main exports: telephone and components (USD 12.6 billion in 2012, 2.7 times higher than in 2011),¹³¹ electronics and computers (USD 7.9 billion, 1.7 times higher than in 2011).¹³² In addition to crude oil exports, Vietnam has built oil refineries such as Dung Quat in Quang Ngai, Nghi Son in Thanh Hoa and Long Son in Ba Ria-Vung Tau.

Policies of industrialization and modernization of the economy continue to be emphasized in the 2011-2020 socio-economic development strategy of Vietnam. The goal is an 85% share of industry and services towards GDP. The value of hi-tech products and products applying hi-tech will reach 45% of GDP. Selective development of industrial processing, manufacturing, hi-tech industry, power industry, mining, metallurgy and chemicals will be implemented. Priority is given to the development of products with a competitive advantage, the ability to participate in a production network and global value chain for hi-tech industry, mechanical engineering, information technology and industrial media and the pharmaceutical industries.¹³³

The service sector is set to achieve higher growth than that of the production sector. Vietnam concentrates on the development of a number of services which gain advantage from a high

¹²⁷ Ministry of Planning and Investment, "Statistics on foreign direct investment" at <http://fia.mpi.gov.vn/News.aspx?ctl=newsdetail&aID=1395>

¹²⁸ *Ibid*

¹²⁹ *Ibid*

¹³⁰ *Ibid*

¹³¹ 40% of Samsung's smartphone products are manufactured in Vietnam

¹³² General Statistics Office at at < <http://www.gso.gov.vn/default.aspx?tabid=393&idmid=3&ItemID=13170>>

¹³³ Documentaries of the 11th National Congress of Vietnam's Communist Party: Strategy for Socio-Economic Development 2011-2020, Communist Party of Vietnam Online Newspaper, at http://123.30.190.43:8080/tiengviet/tulieuvankien/vankiendang/details.asp?topic=191&subtopic=8&leader_topic=989&id=BT531160752

amount of knowledge and technology, such as telecommunications, information technology, healthcare, maritime and aviation services.¹³⁴

Agriculture will be comprehensively developed towards modernization, efficiency and sustainability. Exploiting the advantages of tropical agriculture has led to the development of large-scale production with high productivity, quality, efficiency and competitiveness, and accelerating the application of advanced modern science and technology in production, processing and preservation. The application of biotechnology is preferred to create varieties of crops and livestock, and a high-quality and efficient manufacturing process.¹³⁵

2. VIETNAM'S INSURANCE INDUSTRY

2.1. Development of Vietnamese insurance industry

Before 1993, the main characteristic of Vietnam's insurance sector was the state monopoly in supplying insurance services. In 1964, Vietnam Insurance Company (Bao Viet) was established,¹³⁶ and it was the only state-owned insurance company in the North. After the country's reunification, all insurance companies in the South merged with Bao Viet in 1976-1977.¹³⁷

Doi Moi policy, an "economic renovation" period which began in 1986, marked a turning point in Vietnam's economic development. Vietnam has adopted an open economy, attracting foreign investment from many countries. Production and business activities gradually developed, requiring the insurance industry to innovate to meet the new demands.¹³⁸ The emergence of new insurance companies, joint ventures, joint stock companies and 100% foreign-owned capital companies was of great significance for the development of the insurance industry.

¹³⁴ *Ibid*

¹³⁵ *Ibid*

¹³⁶ Decision 179/CP, dated 17th December 1964, of Vietnam's Prime Minister

¹³⁷ Truong Moc Lam, "Nganh kinh doanh bao hiem o Vietnam- mot chang duong", (2003) *Tap chi Bao hiem 1* [Trans: Truong Moc Lam, "Vietnam's insurance industry- a history", (2003) *Insurance Review 1*], p1; Vu Nhu Thang, "Necessary reform of insurance business law in Vietnam after its accession to the WTO: prudential regulatory aspects" (2007) 12(6) *Fordham Journal of Corporate & Financial Law* 977, p980

¹³⁸ Truong Moc Lam, "Nganh kinh doanh bao hiem o Vietnam- mot chang duong", (2003) *Tap chi Bao hiem 1* [Trans: Truong Moc Lam, "Vietnam's insurance industry- a history", (2003) *Insurance Review 1*], p3

In 1993, Decree 100 of the Government broke the monopoly of insurance and set the stage for the birth of insurance organizations with many different forms in all economic sectors.¹³⁹ In 1995, several new insurance companies were established.¹⁴⁰ The development of the Vietnamese insurance market as well as the emergence of new companies had created conditions for an increasingly competitive environment. It required insurance companies to improve their old products, and introduce new attractive types of insurance products.

Although the Vietnamese insurance industry was established relatively late compared to the global insurance industry, Vietnamese insurance industry is now catching up, step by step, with the trend of development of regional and international insurance. Over twenty years, the Vietnamese insurance market has grown rapidly, with average growth in income premiums of around 38% a year.¹⁴¹ The non-life sector recorded an average growth rate of 23% a year.¹⁴² Life insurance started in 1996 and began to grow significantly from 1999 when large foreign insurers joined the market. Over the period 1999-2008, the life sector recorded a remarkable average growth of 81% a year,¹⁴³ much higher than the average growth in the South and East Asia region during the same period, which was 11% for life and 8.2% for non-life.¹⁴⁴ However, since 2010, the growth of the life sector in Vietnam has slowed significantly (about 16%).¹⁴⁵

Insurance penetration increased sharply, especially between 1993 and 2008. Insurance penetration increased from 0.37% in 1993¹⁴⁶ to 2.13% in 2006¹⁴⁷ and was approximately 1.5% of GDP between 2009 and 2012.¹⁴⁸ In the life sector the growth in premiums outpaced

¹³⁹ Article 2 of the Decree No 100/CP/1993, including: 100% foreign-owned companies, joint stock companies, joint ventures, branches of foreign insurance companies, and state-owned companies.

¹⁴⁰ For example, local insurance companies: Bao Minh, PVI and PJICO, and insurance joint venture companies: UIC, VIA, and foreign insurers in life insurance market: AIA, Korea Life, Dai-ichi, Manulife.

¹⁴¹ Association of Vietnam Insurance

¹⁴² *Ibid*

¹⁴³ *Ibid*

¹⁴⁴ Akash Rakyan & Nishith Srivastava, *Vietnam Insurance Sector: Untapped Potential*, (Sheffield Haworth, 2008)

¹⁴⁵ Hiep hoi bao hiem Viet Nam, "Tong quan thi truong bao hiem Viet Nam nam 2012" [Trans: Association of Vietnamese Insurance, "Overview of Vietnamese insurance market 2012"]

<<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013

¹⁴⁶ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2004*, (NXB Tai chinh, Ha Noi, 2005) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2004*, (Finance Publishing House, Hanoi, 2005)], p6; see also Vu Nhu Thang, "Necessary reform of insurance business law in Vietnam after its accession to the WTO: prudential regulatory aspects" (2007) 12(6) *Fordham Journal of Corporate & Financial Law* 977, p980

¹⁴⁷ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2006*, (NXB Tai chinh, Ha Noi, 2007) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2006*, (Finance Publishing House, Hanoi, 2007)], p8

¹⁴⁸ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)],

the growth in GDP; in the non-life sector, the annual increase in penetration was more stable than in the life sector. Despite the high growth rate of the insurance industry in Vietnam, the penetration and density rates are still very low compared to other countries in the region.¹⁴⁹ Vietnam is just in the mid range in terms of penetration.¹⁵⁰

2.2. Structure of the insurance market in Vietnam

2.2.1. Life insurance and non-life insurance

In Vietnam, life insurance is the most attractive product for individual customers. Foreign insurers with advantages in capital, design technique and actual supply of diversified products have offered premium rates that meet the demands of customers. Between 2001 and 2005 newly founded foreign insurers concentrated on supplying new products of interest to customers,¹⁵¹ and there were a number of changes in life insurance products. As a result, the number of new contracts in this period increased sharply.¹⁵² However, since 2010 the number of new policies has decreased as the market saturated.¹⁵³

After the promulgation of Decree 100/1993, several non-life insurers were established. Foreign insurers had also joined the Vietnamese non-life market as early as 1996. The penetration and density of the non-life sector is low in comparison to that of other countries in the region.¹⁵⁴ In addition it is significantly lower than that of the life sector. Nevertheless, this follows the general trend in emerging countries, where the non-insurance sector underperforms the life sector. In these countries where, on the one hand, GDP per capita is

p5; see also: Table 3: Vietnam life and non-life key market statistics from 2007 to 2012 at section 2.4.1 of this Chapter

¹⁴⁹ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)], p12

¹⁵⁰ Insurance penetration- premiums as a % of GDP in 2012: Vietnam: 1.46; Philippines: 1.40; Indonesia: 1.77; Malaysia: 4.80; Thailand: 5.02; Singapore: 6.03; China: 2.96; India: 3.96; Japan: 11.44, source: SwissRe Sigma, *World Insurance in 2012: Progressing on the long and winding road to recover*, (SwissRe, 2013), p43

¹⁵¹ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2005*, (NXB Tai chinh, Ha Noi, 2006) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2005*, (Finance Publishing House, Hanoi, 2006)], p9

¹⁵² In 2001, 1,307,380 new contracts; in 2002: 1,770,532 new contracts; in 2003: 2,070,816; in 2004: 1,805,789; in 2005: 1,198,000, source: Association of Vietnamese Insurance

¹⁵³ Hiep hoi bao hiem Viet Nam, "Tong quan thi truong bao hiem Viet Nam nam 2012" [Trans: Association of Vietnamese Insurance, "Overview of Vietnamese insurance market 2012"]

<<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013

¹⁵⁴ Insurance penetration- premiums (non-life insurance) as a % of GDP in 2006 and in 2012: Vietnam: 0.7- 0.78; Thailand: 1.6- 2.07; Malaysia: 1.7- 1.72; Singapore: 1.1- 1.60; Philippines: 0.6- 0.49; Indonesia: 0.6- 0.53; China: 1.0- 1.26; South Korea: 3.2- 5.25; Taiwan: 2.9- 3.16; Japan: 2.2- 2.27, respectively, see: SwissRe Sigma, *World Insurance in 2006: Premiums came back to "life"*, (SwissRe, 2007), p39 and SwissRe Sigma, *World Insurance in 2012: Progressing on the long and winding road to recover*, (SwissRe, 2013), p41

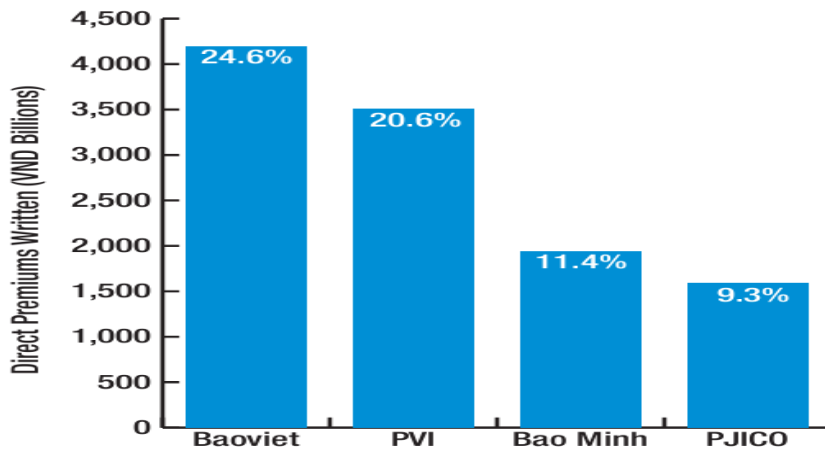
relatively low, people cannot afford to pay for insurance of their properties, and on the other, they do not have many valuable assets which need to be insured.

2.2.2. Role of state-owned insurance companies in insurance market.

There are currently 29 state-owned insurance companies,¹⁵⁵ operating mainly in the non-life insurance market, with more expected to enter due to the potential for growth.¹⁵⁶ All of the top four non-life insurers are state-owned enterprises, namely Baoviet, PVI, Bao Minh and PJICO. They together control 66% of the non-life market.¹⁵⁷ (see Chart 6 below)

Chart 6: Non-life insurance-Top 4 insurers by market share ¹⁵⁸

(Ranked by direct premiums written)



However, intense competition, high operating costs and a claims-heavy environment (particularly in motor insurance) have made profitable underwriting difficult to achieve. The four big state-owned non-life insurers have gradually been losing their market share to foreign competitors since the market removed all legal barriers.¹⁵⁹

2.2.3. Role of foreign insurance companies in insurance market.

¹⁵⁵ Hiep hoi bao hiem Viet Nam, “Tong quan thi truong bao hiem Viet Nam nam 2012” [Trans: Association of Vietnamese Insurance, “Overview of Vietnamese insurance market 2012”] <<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013

¹⁵⁶ *Ibid*

¹⁵⁷ Hiep hoi bao hiem Viet Nam, “Tong quan thi truong bao hiem Viet Nam nam 2012” [Trans: Association of Vietnamese Insurance, “Overview of Vietnamese insurance market 2012”] <<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013; see also Yvette Essen, “Vietnam’s Insurance Market Awakening to Further change”, (2011) A.M. Best’s Special Report, p 3

¹⁵⁸ Association of Vietnam Insurance

¹⁵⁹ Marius Gamser, “Vietnam Insurance Market Progress”, (2011) International Insurance and Healthcare Industry News

Foreign insurance companies dominate in the life insurance market.¹⁶⁰ Foreign insurers account for approximately 70% of the life insurance market.¹⁶¹ They dominate the life market because they have not only a large amount of capital but also technical expertise. Prudential is reported to be the number one player, and followed by BaoViet and in third position is Manulife.¹⁶² (see Table 2 below)

Table 2: Top 3 insurers and market share in Vietnamese life insurance market ¹⁶³

Rank	Company	Premiums	Market Share (%)	Total Number of Agents
1	Prudential	VND 5,374	39.0	82,539
2	Baoviet	4,023	29.2	19,999
3	Manulife	1,460	10.6	8,907

Source: Association of Vietnamese Insurance

In line with the trade liberalization, Vietnam’s life insurance market has become more and more attractive to foreign life insurers. The presence of foreign insurers provides consumers with greater choice and creates new standards in the insurance sector. They also play an important role in training human resources.¹⁶⁴

2.3. The current position of insurance industry in the Vietnam’s economy.

Vietnam’s insurance market has experienced strong, double-digit premium growth in over 20 years, and despite the ongoing economic uncertainties around the world, its expansion continues.¹⁶⁵ The insurance industry has become a shield against natural disasters and

¹⁶⁰ Only 04 local insurers offer life insurance products, namely: BaoViet and three joint ventures (Vietinbank-Aviva, Vietcombank-Cardiff Life Insurance, and PVI Sun Life)

¹⁶¹ Hiep hoi bao hiem Viet Nam, “Tong quan thi truong bao hiem Viet Nam nam 2012” [Trans: Association of Vietnamese Insurance, “Overview of Vietnamese insurance market 2012”] <<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013

¹⁶² Hiep hoi bao hiem Viet Nam, “Tong quan thi truong bao hiem Viet Nam nam 2012” [Trans: Association of Vietnamese Insurance, “Overview of Vietnamese insurance market 2012”] <<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013; Yvette Essen, “Vietnam’s Insurance Market Awakening to Further change”, (2011) A.M. Best’s Special Report, p7

¹⁶³ Association of Vietnam Insurance

¹⁶⁴ Lan Huong (2012), “Upper hand”, VnEconomy, available at <<http://news.vneconomy.vn/2012040511391811POC1/upper-hand.htm>>

¹⁶⁵ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam’s Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)], p1; see also: “Jurisdiction update: Vietnam’s insurance market- March 2013” <http://www.hoganlovells.com/files/Uploads/Documents/Vietnam%20newsflash_Jurisdiction%20Update%20Vietnam%20Insurance%20March%202013_1022600.pdf> accessed 15 June 2013

accidents for Vietnamese society and the national economy, with the compensation ratios at approximately 55% per year.¹⁶⁶ Total insurance revenue reached 41.1 trillion VND in 2012,¹⁶⁷ a 130% increase compared with 2007,¹⁶⁸ and a 5771% compared with 1993.¹⁶⁹ The insurance industry has helped initially to meet the insurance needs for businesses of foreign and domestic investment, and also to create medium and long-term capital for investment in Vietnam's development.

The contribution to GDP of the insurance sector increased dramatically, thanks mainly to the growth of the sector and investment activities of insurers. The rate of GDP contribution of the sector increased sharply from 0.37% in 1993 to 2% in 2004,¹⁷⁰ reached a peak of 2.13% in 2006,¹⁷¹ and remained steady at approximately 1.5% from 2009 to 2012.¹⁷² In 2012, although Vietnam's economy was continuously faced with several difficulties, the growth of the insurance sector was still twice as high as the GDP growth,¹⁷³ with the growth rate of non-life insurance at 10.33%¹⁷⁴ and life insurance reaching 14.8%.¹⁷⁵ The insurance sector was top among the leading financial services.

¹⁶⁶ Hiep hoi bao hiem Viet Nam, "Tong quan thi truong bao hiem Viet Nam nam 2012" [Trans: Association of Vietnamese Insurance, "Overview of Vietnamese insurance market 2012"]

<<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013

¹⁶⁷ SwissRe Sigma, *World Insurance in 2012: Progressing on the long and winding road to recover*, (SwissRe, 2013), p34; Hiep hoi bao hiem Viet Nam, "Tong quan thi truong bao hiem Viet Nam nam 2012" [Trans: Association of Vietnamese Insurance, "Overview of Vietnamese insurance market 2012"]

<<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013

¹⁶⁸ In 2007, the total insurance revenue was 17.8 trillion VND. In this year, Vietnam became a member of WTO, and the Vietnam's insurance market was opened up.

¹⁶⁹ In 1993, the total insurance revenue was only 700 billion VND, source: Association of Vietnam Insurance, and Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2004*, (NXB Tai chinh, Ha Noi, 2005) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2004*, (Finance Publishing House, Hanoi, 2005)], p6

¹⁷⁰ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2004*, (NXB Tai chinh, Ha Noi, 2005) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2004*, (Finance Publishing House, Hanoi, 2005)], p6; see also Vu Nhu Thang, "Necessary reform of insurance business law in Vietnam after its accession to the WTO: prudential regulatory aspects" (2007) 12(6) *Fordham Journal of Corporate & Financial Law* 977, p980

¹⁷¹ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2006*, (NXB Tai chinh, Ha Noi, 2007) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2006*, (Finance Publishing House, Hanoi, 2007)], p8

¹⁷² Table 3: Vietnam life and non-life key market statistics from 2007 to 2012 at section 2.4.1 of this Chapter; source: Association of Vietnam Insurance at <<http://avi.org.vn/News/Item/1524/202/vi-VN/Default.aspx>>; Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)] p5; SwissRe Sigma, *World Insurance in 2012: Progressing on the long and winding road to recover*, (SwissRe, 2013), p41

¹⁷³ In 2012, Vietnam's GDP growth rate: 5.0%

¹⁷⁴ Hiep hoi bao hiem Viet Nam, "Tong quan thi truong bao hiem Viet Nam nam 2012" [Trans: Association of Vietnamese Insurance, "Overview of Vietnamese insurance market 2012"]

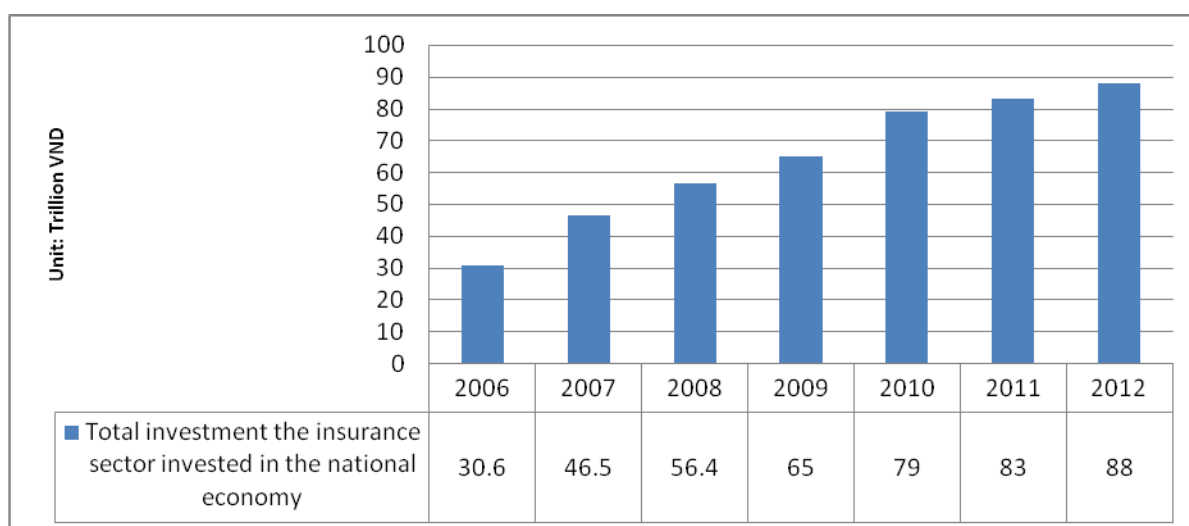
<<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013

¹⁷⁵ *Ibid*

In investments, the insurers have increasingly affirmed their role as an important channel for capital mobilization and for economic development. Investment structure has shifted from short-term investments to long-term investment in the form of government bonds, direct investment in infrastructure and business development.¹⁷⁶

Over the last 15 years, the total investment of the insurance sector has increased rapidly. In 1999, the total investment of the insurance sector was only VND 2.6 trillion,¹⁷⁷ and rose to VND 10 trillion in 2002,¹⁷⁸ 3.8 times higher. In 2006, this figure was VND 30.6 trillion,¹⁷⁹ and in 2012 it reached VND 88 trillion.¹⁸⁰ (see Chart 7 below)

Chart 7: Total investment of the insurance sector back to the Vietnam’s national economy in the period 2006-2012



Source: Insurance Commission, Ministry of Finance

¹⁷⁶ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam’s Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)] p12

¹⁷⁷ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2002*, (NXB Tai chinh, Ha Noi, 2003) [Trans: Vietnam’s Ministry of Finance, *Vietnamese insurance market 2002*, (Finance Publishing House, Hanoi, 2003)], p8

¹⁷⁸ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2003*, (NXB Tai chinh, Ha Noi, 2004) [Trans: Vietnam’s Ministry of Finance, *Vietnamese insurance market 2003*, (Finance Publishing House, Hanoi, 2004)], p9

¹⁷⁹ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2006*, (NXB Tai chinh, Ha Noi, 2007) [Trans: Vietnam’s Ministry of Finance, *Vietnamese insurance market 2006*, (Finance Publishing House, Hanoi, 2007)], p12

¹⁸⁰ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam’s Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)], p12

A large number of workers have been attracted to the insurance sector. Growth in the number of insurers and their operations has led to an increase in employment in the insurance sector. In 1993, there were 1,000 insurance employees and agents,¹⁸¹ by 2004 this was 136,900,¹⁸² and by 2012 the sector was employing 225.963 employees and agents,¹⁸³ 225.9 times as many as in 1993.

2.4. Impacts of trade liberalization on Vietnam's insurance industry.

2.4.1. Considerable changes in terms of market size and number of insurers

Vietnam's insurance market has witnessed considerable changes in terms of market size and number of insurers. In 1993, Bao Viet was the only insurer in the market and held a monopoly position. In 2000, the new markets of non-life insurance and life insurance were opened up with 10 non-life insurance and 2 life insurance companies.¹⁸⁴ So far, in 2013, there are 29 non-life insurers (11 foreign-invested enterprises), 15 life insurance companies (14 foreign-invested enterprises), 2 reinsurance companies, 12 insurance brokers and 23 representative offices in Vietnam. The insurance network has been expanded, with nearly 500 branches, and more than 2,000 offices covering all urban and rural districts and remote areas.¹⁸⁵

¹⁸¹ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2004*, (NXB Tai chinh, Ha Noi, 2005) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2004*, (Finance Publishing House, Hanoi, 2005)], p2

¹⁸² *Ibid*

¹⁸³ Hiep hoi bao hiem Viet Nam, "Tong quan thi truong bao hiem Viet Nam nam 2012" [Trans: Association of Vietnamese Insurance, "Overview of Vietnamese insurance market 2012"]

<<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013; Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)], p3

¹⁸⁴ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2002*, (NXB Tai chinh, Ha Noi, 2003) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2002*, (Finance Publishing House, Hanoi, 2003)], p2

¹⁸⁵ Association of Vietnamese Insurers at <http://avi.org.vn/News/Item/822/125/vi-VN/Default.aspx>; Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)], p2

Table 3: Vietnam life and non-life key market statistics from 2007 to 2012¹⁸⁶

	2007	2008	2009	2010	2011	2012
Gross Domestic Product (GDP) (VND trillions)	1,143.7	1,485.0	1,658.4	1,980.9	2,469.6	2950.6
Change in real GDP (%)	8.5	6.3	5.3	6.8	5.8	5.0
Insurance penetration (%)	1.6	1.4	1.5	1.6	1.5	1.5
Life	0.8	0.7	0.7	0.7	0.6	0.6
Non-life	0.7	0.7	0.8	0.9	0.9	0.9
Direct premiums written (VND trillions)	17.8	21.2	25.5	30.8	37.5	41.1
Life	9.4	10.3	11.8	13.8	16.0	18.4
Non-life	8.4	10.9	13.6	17.1	21.5	22.7
Change in total premium volume (%)	18.8	19.0	20.3	21.1	21.6	10.0

Source: Association of Vietnamese Insurers and General Statistics Office

Along with the growth of the economy and the increase in the number of insurance companies, the premiums revenue of the insurance industry has been also increasing steadily with an average increase of about 18.5% a year over the 2007-2012 periods.¹⁸⁷ WTO accession helped the industry achieve robust growth, with life insurance direct premiums written of VND 18.4 trillion in 2012,¹⁸⁸ up more than 105% compared to 2007. Non-life insurance direct premiums written also reached to VND 22.7 trillion in 2012,¹⁸⁹ a 25% increase year-on-year.

WTO entry has laid an important foundation for development of Vietnam's insurance industry, with a high growth rate in rising incomes, and high levels of investment. In the non-

¹⁸⁶ Association of Vietnamese Insurers at <http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx> and General Statistics Office at <http://www.gso.gov.vn/default.aspx?tabid=393&idmid=3&ItemID=13170>

¹⁸⁷ Own calculation based on the data in Table 3: Vietnam life and non-life key market statistics from 2007 to 2012 (Change in total premium volume)

¹⁸⁸ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)], p3; SwissRe Sigma, *World Insurance in 2012: Progressing on the long and winding road to recover*, (SwissRe, 2013), p36

¹⁸⁹ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)], p3; SwissRe Sigma, *World Insurance in 2012: Progressing on the long and winding road to recover*, (SwissRe, 2013), p38

life insurance market, the average growth is about 28% per year;¹⁹⁰ in the life insurance market, the number of new contracts increased by 25% per year.¹⁹¹ The total liability of the life insurance companies holding was VND 580 trillion in 2012.¹⁹² The growth rate of premiums written is about 22% per year.¹⁹³

2.4.2. Wider choice of products

There is an increasingly rich and diverse range of insurance products. In 2000, there were only 200 insurance products;¹⁹⁴ now, in 2013, there are nearly 700 non-life insurance and more than 100 life insurance products.¹⁹⁵ The insurance products vary between the insurers, providing wide choices to customers. The wide range of products initially meet the needs of the national economy, particularly with the technical professions requiring special insurance, such as oil and gas, aviation, satellites, shipbuilding, building construction, underground construction.

International economic integration makes local insurers more dynamic. Because of the local insurers' anxiety over the constant increase in new products offered by foreign insurers, they have to gradually diversify insurance products and distribution channels.¹⁹⁶ Besides the traditional products, domestic insurers have put considerable effort into designing new insurance products, both in life and non-life sector, to meet the increasing needs of clients.¹⁹⁷

¹⁹⁰ Own calculation based on the data in Table 3: Vietnam life and non-life key market statistics from 2007 to 2012

¹⁹¹ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)], p9

¹⁹² Hiep hoi bao hiem Viet Nam, "Tong quan thi truong bao hiem Viet Nam nam 2012" [Trans: Association of Vietnamese Insurance, "Overview of Vietnamese insurance market 2012"] <<http://avi.org.vn/News/Item/1753/202/vi-VN/Default.aspx>> accessed 14 June 2013

¹⁹³ Own calculation based on the data in Table 3: Vietnam life and non-life key market statistics from 2007 to 2012

¹⁹⁴ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2002*, (NXB Tai chinh, Ha Noi, 2003) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2002*, (Finance Publishing House, Hanoi, 2003)], p1

¹⁹⁵ Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)], p1

¹⁹⁶ Nguyen Nhu Tien, *Thi truong bao hiem Viet Nam: co hoi va thach thuc trong qua trinh hoi nhap*, (NXB Ly luan chinh tri, 2006) [Trans: Nguyen Nhu Tien, *Vietnam's insurance market: opportunities and challenges in international economic integration*, (Political Theory Publishing House, 2006)], p95

¹⁹⁷ *Ibid*, p96

2.4.3. A regulatory regime is more transparent, fair and closer to international standards

Numerous of changes in Vietnam's legal system have strengthened the insurance sector considerably, because economic integration requires Vietnam to improve its legal framework to bring it more in line with the WTO and BTA regulations.¹⁹⁸ The Law on Insurance Business 2000 replaced Decree 100/CP 1993 and now uniformly administers insurance activities. Supporting documents explain rules in the Law in greater details and are increasingly in line with international standards. Since 2007, a number of regulations have been issued,¹⁹⁹ and these have gradually improved the legal framework for the market in the direction of clarity and transparency, strengthened inspection and testing, and have become more favourable to the interests of the insureds. Those improvements have brought Vietnam's insurance market and insurance legal system closer to international benchmarks.

2.4.4. Increased business in the insurance market

One of the most important elements of opening the market is the breaking of the monopoly situation by quickly increasing insurance suppliers. A market of more suppliers motivates the process of expanding the product range, and hence, makes it easier for the insurance sector to perform its function of mobilizing capital and protecting individuals and businesses from risks.

Since Vietnam's insurance market opened the number of insurance companies has increased quickly.²⁰⁰ The most noticeable increase is in the number of foreign insurers. The participation of new insurers, especially foreign, has increased activity in the market, with insurance premiums written increasing continuously and quickly. The most remarkable premium growth was recorded by foreign life insurers.²⁰¹ The success of these companies illustrates the high potential of the market.²⁰²

¹⁹⁸ Vu Nhu Thang, "Necessary reform of insurance business law in Vietnam after its accession to the WTO: prudential regulatory aspects" (2007) 12(6) *Fordham Journal of Corporate & Financial Law* 977, p978

¹⁹⁹ See section 4 of this Chapter

²⁰⁰ See section 2.4.1 of this Chapter

²⁰¹ See section 2.2.3 of this Chapter

²⁰² Bo Tai chinh Viet Nam, *Thi truong bao hiem Viet Nam nam 2012*, (NXB Tai chinh, Ha Noi, 2013) [Trans: Vietnam's Ministry of Finance, *Vietnamese insurance market 2012*, (Finance Publishing House, Hanoi, 2013)], p4

2.4.5. Strengthening knowledge and transferring expertise

Local insurers are now in a better position to acquire knowledge and professional skills from foreign companies. Foreign companies can provide expertise in areas such as corporate governance, technology, training, production and distribution.²⁰³ Changes in the market over recent years reveal that foreign insurers are in a more advantageous position than the domestic insurers in terms of risk assessment and management, contract management, and marketing strategies. Higher competition pressures have forced domestic insurers to actively adjust their management structures and policies, train their employees and apply information technology to increase their competitiveness.

2.4.6. Improved awareness of insurance

Together with the opening of the market, the operation of insurance companies has made a contribution to increasing Vietnamese people's awareness of the role and function of insurance.²⁰⁴ Good awareness and knowledge of insurance and insurance activities will help achieve the targets set out by the sector.

3. THE VIETNAMESE LEGAL SYSTEM

3.1. Overview

3.1.1. Influence of civil law

Vietnam's legal system has been influenced by civil law legal systems, especially French law, in which the main sources are statute and legislation.²⁰⁵ Legal principles are codified into

²⁰³ Nguyen Nhu Tien, *Thi truong bao hiem Viet Nam: co hoi va thach thuc trong qua trinh hoi nhap*, (NXB Ly luan chinh tri, 2006) [Trans: Nguyen Nhu Tien, *Vietnam's insurance market: opportunities and challenges in international economic integration*, (Political Theory Publishing House, 2006)], p124

²⁰⁴ Nguyen Nhu Tien, *Thi truong bao hiem Viet Nam: co hoi va thach thuc trong qua trinh hoi nhap*, (NXB Ly luan chinh tri, 2006) [Trans: Nguyen Nhu Tien, *Vietnam's insurance market: opportunities and challenges in international economic integration*, (Political Theory Publishing House, 2006)], p36

²⁰⁵ Vietnam was a colony of France for nearly 100 years, from 1858 to 1945; see also Vu Minh Giang, *Lich su Vietnam: truyen thong va hien dai*, (NXB Giao duc, 2009), p52-53 [Trans: Vu Minh Giang, *Vietnamese history: tradition and modern*, (Education Publishing House)]; Dao Tri Uc, "Basic information of legal research- a case study of Vietnam" in the Project of "Doing legal research in Asian countries: China, India, Malaysia, Philippines, Thailand, and Vietnam" conducted by the Institute of Developing Economies (IDE-JETRO), Japan, 2003 (IDE Asian Law Series No. 23), p206 <<http://www.ide.go.jp/English/Publish/Download/Als/pdf/23.pdf>> accessed 09 June 2013

a system, including law codes, law acts, and delegated legislation.²⁰⁶ In Vietnam, case law is not a source of law.²⁰⁷

Sources of law in Vietnam comprise only written legislation which is referred to as legal instruments.²⁰⁸ These are organised in a hierarchy in which higher-ranking legal instruments set out general rules, and the lower-ranking provide the details.²⁰⁹ Among those instruments, Vietnam's Constitution stands at the top of this legal hierarchy and forms the foundation of the entire legal system.²¹⁰ Law codes and law acts are the second most important in the hierarchy, and govern specific areas.²¹¹ Only Vietnam's National Assembly has authority to issue law codes and law acts.²¹² Rules and provisions in those instruments must not be in conflict with the general rules provided in the Vietnam's Constitution.²¹³ The delegated legislation is enacted by government agencies in order to explain in more details about the rules and provisions in the law codes and law acts.²¹⁴

²⁰⁶ Le Minh Tam, *Xay dung va hoan thien he thong phap luat Viet Nam- nhung van de ly luan va thuc tien*, (NXB Cong an nhan dan, Ha Noi, 2003) [Trans: Le Minh Tam, *Building up and improving the Vietnamese legal system- issues on theories and practices*, (People's Public Security Publishing House, Hanoi, 2003)], p87-92

²⁰⁷ Le Minh Tam, *Xay dung va hoan thien he thong phap luat Viet Nam- nhung van de ly luan va thuc tien*, (NXB Cong an nhan dan, Ha Noi, 2003) [Trans: Le Minh Tam, *Building up and improving the Vietnamese legal system- issues on theories and practices*, (People's Public Security Publishing House, Hanoi, 2003)], p92

²⁰⁸ Do Thi Mai Hanh, "Transplanting common law precedents: an appropriate solution for defects of legislation in Vietnam", (2011) 25 *European Scientific Journal* 82, p89; Le Minh Tam, *Xay dung va hoan thien he thong phap luat Viet Nam- nhung van de ly luan va thuc tien*, (NXB Cong an nhan dan, Ha Noi, 2003) [Trans: Le Minh Tam, *Building up and improving the Vietnamese legal system- issues on theories and practices*, (People's Public Security Publishing House, Hanoi, 2003)], p155

²⁰⁹ Do Thi Mai Hanh, "Transplanting common law precedents: an appropriate solution for defects of legislation in Vietnam", (2011) 25 *European Scientific Journal* 82, p83

²¹⁰ Article 2 and 11 of Vietnam's Law on Promulgation of Legal Instruments 2008; Ngo Duc Manh, "Giai thich phap luat la bao dam tinh toi cao cua Hien phap", (2008) *Tap chi Nghien cuu lap phap* 5 [Trans: Ngo Duc Manh, "Legal interpretation is to guarantee the supremacy of the Constitution" (2008) *Journal of Legislative Studies* 5], p5

²¹¹ Vietnamese legal system is divided into branches of law, such as constitutional law, administrative law, criminal law, civil law, labour law, business law, land law, marriage and family law,...

²¹² Article 11 of Vietnam's Law on Promulgation of Legal Instruments 2008; see also Hoang Van Tu, "Ve quyen lap phap cua Quoc hoi", (2002) *Tap chi Nghien cuu lap phap* 11 [Trans: Hoang Van Tu, "On a legislative power of the National Assembly", (2002) *Journal of Legislative Studies* 11], p12

²¹³ Dao Tri Uc, *Nhung van de ly luan co ban ve nha nuoc va phap luat*, (NXB Chinh tri quoc gia, 1995) [Trans: Dao Tri Uc, *Basic theoretical issues on state and law*, (National Politics Publishing House, 1995)], p143; Hoang Van Tu, "Ve quyen lap phap cua Quoc hoi", (2002) *Tap chi Nghien cuu lap phap* 11 [Trans: Hoang Van Tu, "On a legislative power of the National Assembly", (2002) *Journal of Legislative Studies* 11], p14; Ngo Duc Manh, "Giai thich phap luat la bao dam tinh toi cao cua Hien phap", (2008) *Tap chi Nghien cuu lap phap* 5 [Trans: Ngo Duc Manh, "Legal interpretation is to guarantee the supremacy of the Constitution" (2008) *Journal of Legislative Studies* 5], p5

²¹⁴ In Vietnam, the delegated legislation includes: ordinances, orders, decrees, resolutions, decisions, directives and circulars. Legal effect of those legal documents is not the same and depends on the ranking of the government agency, which issues the documents, in the system state agency.; see also: Nguyen Cuu Viet, "Khai niem van ban quy pham phap luat va he thong van ban phap luat", (2007) *Tap chi Nghien cuu lap phap* 27 [Trans: Nguyen Cuu Viet, "A concept of legal normative documents and a system of legal documents", (2007) *Journal of Legislative Studies* 27], p28-30

Similar to other civil law countries, Vietnamese courts decide a dispute using statutory law on a case-by-case basis, without reference to other judicial decisions.²¹⁵ The precedent of a higher-ranking court is not binding upon a lower ranking court.²¹⁶ In a trial, judges must follow the rules set out in the legal instruments and have no power to make law.²¹⁷ In order to apply a rule, judges have discretion in explaining the rule (in accordance with its ordinary and literal meaning, or with the circumstances of the dispute).²¹⁸

One of the most important rules which the judges must follow when applying the legal instruments is that the provisions in specific laws prevail over the provisions in general laws.²¹⁹ For instance, concerning marine hull insurance, the provision governing insurance contracts in the Maritime Code 2005 shall be applied first. Where there is no provision governing the issue in question in the Maritime Code, the provisions governing insurance contracts in the Law on Insurance Business 2000 shall then be applied, because marine hull insurance is a specific field in insurance business. Where there is no provisions governing the issue in question in the Law on Insurance Business either, the provisions in Civil Code 2005 shall be applied, because insurance contract is a category of civil contract.

²¹⁵ Do Van Dai, *Luat hop dong Viet Nam: ban an va binh luan an*, (NXB Chinh tri quoc gia, 2008) [Trans: Do Van Dai, *Vietnamese contract laws: judgments and commentaries*, (National Politics Publishing House, 2008)], p51; Do Van Dai, “Toa an nhan dan toi cao voi van de giai thich phap luat dan su o Viet Nam” (2008) 6 *Tap chi Toa an nhan dan* 25, [Trans: Do Van Dai, “The Supreme People’s Court with its civil law interpretation in Vietnam”, (2008) 6 *Journal of People’s Court* 25], p26

²¹⁶ Vo Tri Hao, “Vai tro giai thich phap luat cua toa an”, (2003) *Tap chi Khoa hoc phap ly* 12 [Trans: Vo Tri Hao, “The role of legal interpretation of the courts”, (2003) *Journal of Legal Science* 12], p13-14; Do Van Dai, “Toa an nhan dan toi cao voi van de giai thich phap luat dan su o Viet Nam” (2008) 6 *Tap chi Toa an nhan dan* 25, [Trans: Do Van Dai, “The Supreme People’s Court with its civil law interpretation in Vietnam”, (2008) 6 *Journal of People’s Court* 25], p28

²¹⁷ Nguyen Hoang Anh, “Ap dung nguyen tac phap luat trong hoat dong xet xu”, (2004) *Tap chi Nghien cuu lap phap* 11 [Trans: Nguyen Hoang Anh, “Applying the rule of law in judging tasks”, (2004) *Journal of Legislative Studies* 11], p16

²¹⁸ In Vietnam, articles, which are contained in legal documents, are usually structured in a generalized manner to suit the variety of cases which may occur in reality. Many laws are expressed in general terms and their interpretation is open; see Do Van Dai, “Toa an nhan dan toi cao voi van de giai thich phap luat dan su o Viet Nam” (2008) 6 *Tap chi Toa an nhan dan* 25, [Trans: Do Van Dai, “The Supreme People’s Court with its civil law interpretation in Vietnam”, (2008) 6 *Journal of People’s Court* 25], p28; P. Nicholson, “Vietnamese jurisprudence: informing court reform” in J. Gillespie and P. Nicholson (eds), *Asian socialism & legal change: the dynamics of Vietnamese and Chinese reform*, (Asia Pacific Press, Canberra, 2005)

²¹⁹ Le Minh Tam, *Giao trinh ly luan nha nuoc va phap luat*, (NXB Tu phap, 2006) [Trans: Le Minh Tam, *Textbook on theories of state and law*, (Justice Publishing House, 2006)], p159; Tuong Duy Luong, “Vai suy nghi ve viec tong ket thuc tien xet xu, huong dan ap dung thong nhat phap luat cua toa an nhan dan toi cao”, (2007) *Tap chi Nha nuoc va Phap luat* 11 [Trans: Tuong Duy Luong, “Some thoughts on synthesizing judging experience, guidance for the consistent application of laws by the People’s Supreme Court”, (2007) *Journal of State and Law* 11], p14

3.1.2. *Reliance on communist legal theory*

The nature and characteristics of the Vietnamese legal system are strongly influenced by socialist law systems.²²⁰ It is based on Marxism-Leninism,²²¹ representing the will and aspirations of the working class and other labouring people because the Vietnamese state is a state of the people, from the people, for the people.²²²

The Vietnamese legal system has served to implement the objectives of a socialist state.²²³ It strengthens “socialist legality”, and facilitates the development of a socialist state exercising the administration of society by means of law.²²⁴ It protects the legitimate interests of working people, and brings democracy and fairness to the people.²²⁵

Since the Vietnamese Communist Party is the force leading the State and society,²²⁶ Vietnamese laws represent the Vietnamese Communist Party’s policies,²²⁷ and transform those policies into general rules and legal principles which set a legal framework for the establishment and operation of the State, government agencies, organisations, and the activity of the people.²²⁸ In economic activities, a legal framework for organisations and individuals doing business in accordance with a socialist-oriented market economy has been established.²²⁹

²²⁰ Dao Tri Uc, *Nhung van de ly luan co ban ve nha nuoc va phap luat*, (NXB Chinh tri quoc gia, 1995) [Trans: Dao Tri Uc, *Basic theoretical issues on state and law*, (National Politics Publishing House, 1995)], p198; Le Minh Tam, *Giao trinh ly luan nha nuoc va phap luat*, (NXB Tu phap, 2006) [Trans: Le Minh Tam, *Textbook on theories of state and law*, (Justice Publishing House, 2006)], p135; J. Gillespie, *Transplanting commercial law reform – developing a ‘rule of law’ in Vietnam*, (Aldershot: Ashgate, 2006), p60-62; Do Thi Mai Hanh, “Transplanting common law precedents: an appropriate solution for defects of legislation in Vietnam”, (2011) 25 *European Scientific Journal* 82, p82

²²¹ Article 4 of Vietnam’s Constitution 1992; Do Thi Mai Hanh, “Transplanting common law precedents: an appropriate solution for defects of legislation in Vietnam”, (2011) 25 *European Scientific Journal* 82, p83

²²² Article 2 of Vietnam’s Constitution 1992

²²³ P. Nicholson, “Vietnamese jurisprudence: informing court reform” in J. Gillespie and P. Nicholson (eds), *Asian socialism & legal change: the dynamics of Vietnamese and Chinese reform*, (Asia Pacific Press, Canberra, 2005), p171

²²⁴ Article 12 of Vietnam’s Constitution 1992

²²⁵ Article 3 and 5 of Vietnam’s Constitution 1992

²²⁶ Article 4 of Vietnam’s Constitution 1992

²²⁷ P. Nicholson, “Vietnamese jurisprudence: informing court reform” in J. Gillespie and P. Nicholson (eds), *Asian socialism & legal change: the dynamics of Vietnamese and Chinese reform*, (Asia Pacific Press, Canberra, 2005), p174-176

²²⁸ Tran Thai Duong, “The che hoa duong loi cua Dang” (2004) *Tap chi Nghien cuu lap phap* 12 [Tran Thai Duong, “Institutionalizing Communist Party of Vietnam’s policies”, (2004) *Journal of Legislative Studies* 12], p13-14

²²⁹ Article 15 of Vietnam’s Constitution 1992; J. Gillespie, “Changing concepts of socialist law in Vietnam” in J. Gillespie and P. Nicholson (eds), *Asian socialism & legal change: the dynamics of Vietnamese and Chinese reform*, (Asia Pacific Press, Canberra, 2005), p57; Do Thi Mai Hanh, “Transplanting common law precedents: an appropriate solution for defects of legislation in Vietnam”, (2011) 25 *European Scientific Journal* 82, p85-87

Ownership is a vital concept in Vietnamese laws because it lays down a fundamental foundation for a socialist economic regime.²³⁰ In Vietnam, the state ownership and collective ownership are the foundation of the national economy.²³¹ Most of the important production materials are owned by the state. For instance, the state owns all land; organisations and individuals only have rights to use the land.²³² The collective sector is given favourable conditions for consolidating, broadening and effectively operating,²³³ which plays an important role in agricultural industry.

3.1.3. Impacts of (Doi moi) economic renovation on Vietnamese legal system

Since 1986, Vietnam has implemented a policy of economic renovation. In order to meet the change of national economy and the objectives of the economic renovation policy, the Vietnamese legal system was comprehensively reformed.²³⁴ The Vietnamese national economy was to be managed by means of laws, no longer by centralised-command and control.²³⁵

A milestone in the development of the Vietnamese legal system was the enactment of the Vietnamese Constitution 1992. It states that Vietnam will consistently implement the policies of developing a socialist-oriented market economy and establishing a multi-sector economic structure²³⁶ with diversified forms of production and business organization;²³⁷ and it recognises the freedom of business of individuals and organisations.²³⁸ Vietnam was also to build an independent and sovereign economy on the basis of bringing into full play internal

²³⁰ Dinh Ngoc Vuong, “Khai niem va nhung moi quan he cua phap luat” in Dao Tri Uc (eds), *Nhung van de ly luan co ban ve nha nuoc va phap luat*, (NXB Chinh tri quoc gia, 1995) [Trans: Dinh Ngoc Vuong, “Concept and the relationship between state law and other norms” in Dao Tri Uc (eds), *Basic theoretical issues on state and law*, (National Politics Publishing House, 1995)], p317

²³¹ Article 15, 19 and 20 of Vietnam’s Constitution 1992; J. Gillespie, *Transplanting commercial law reform – developing a ‘rule of law’ in Vietnam*, (Aldershot: Ashgate, 2006), p64

²³² Article 17 of Vietnam’s Constitution 1992

²³³ Article 20 of Vietnam’s Constitution 1992

²³⁴ J. Gillespie and P. Nicholson, “The diversity and dynamism of legal change in socialist China and Vietnam” in J. Gillespie and P. Nicholson (eds), *Asian socialism & legal change: the dynamics of Vietnamese and Chinese reform*, (Asia Pacific Press, Canberra, 2005), p3-4

²³⁵ Ngo Huy Cuong, *Gop phan ban ve cai cach phap luat o Viet Nam hien nay*, (NXB Tu phap, 2006) [Trans: Ngo Huy Cuong, *Legal reform in Vietnam*, (Justice Publishing House, 2006)], p69

²³⁶ Article 15 of Vietnam’s Constitution 1992

²³⁷ Article 22 of Vietnam’s Constitution 1992; J. Gillespie, “Changing concepts of socialist law in Vietnam” in J. Gillespie and P. Nicholson (eds), *Asian socialism & legal change: the dynamics of Vietnamese and Chinese reform*, (Asia Pacific Press, Canberra, 2005), p57

²³⁸ Article 21 and 25 of Vietnam’s Constitution 1992

resources and actively integrating into the international economy, and carrying out national industrialization and modernization.²³⁹

From 1992 to 2005, there was a rapid development of the Vietnamese legal system, in which the development of business law was remarkable for the introduction of a number of laws, such as the Civil Code 1995, the Commercial Law 1995, the Law on Foreign Investment 1987 (amended and supplemented in 1996), the Law on Domestic Investment 1998, the Enterprise Law 1995, the Law on Enterprise Bankruptcy 1993, the Law on Insurance Business 2000, the Law on Civil Aviation 1992, the Law on the State Bank of Vietnam 1997, and the Law on Credit Institutions 1997, ...

In sum, in line with the transformation from a centrally planned economy to a market-oriented economy, Vietnam's legal system has experienced many positive changes, greatly facilitating the economic renovation policy.

3.1.4. Impacts of integration into the world economy on the Vietnamese legal system

The trend of international economic integration has positively influenced the legal system of Vietnam, especially after Vietnam became a member of the WTO in 2007.²⁴⁰ In recent years, the Vietnamese legal system has significantly improved and become more complete, harmonious and consistent with international laws and the laws of other countries in the region.²⁴¹

The legislation which was recently enacted demonstrates Vietnam's strong and long-term commitments to perform its obligations under regional or international treaties and conventions which Vietnam has signed or of which it has become a member. Many

²³⁹ Ngo Huy Cuong, *Gop phan ban ve cai cach phap luat o Viet Nam hien nay*, (NXB Tu phap, 2006) [Trans: Ngo Huy Cuong, *Legal reform in Vietnam*, (Justice Publishing House, 2006)], p75

²⁴⁰ Viện nghiên cứu quản lý kinh tế trung ương (CIEM), *Tac dong cua hoi nhap kinh te quoc te doi voi nen kinh te sau ba nam Viet Nam gia nhap WTO*, (2010), p85 [Trans: Vietnam's Central Institute for Economic Management (CIEM), *The impact of international economic integration on Vietnam's national economy: 03 years after becoming a member of WTO*, (2010)] available at <http://www.trungtamwto.vn/sites/default/files/Bao%20cao%20KT-XH%203%20nam%20WTO.pdf>

²⁴¹ Vietnam's National Committee for International Economic Cooperation (NCIEC), "Assessments of the impacts of Vietnam's WTO accession on some Vietnamese products and services", (2007), p18 available at <http://www.adetef.org.vn/website/documents/Etudes%20compl%C3%A9mentaires/NCIEC/Etude%20Impact%20sur%20produits%20et%20services%20-%20FSP%20I%20-%20EN.pdf>,

commitments have been incorporated into Vietnam's legal documents and put into practice domestically.²⁴²

The process of amending and reforming the legal documents relating to international integration has been undertaken in various areas, such as economics, commerce, investment, credit, intellectual property, customs, and taxation... Gradually, Vietnam issued or amended a number of legal instruments in order to fulfil its commitments to ASEAN, the Vietnam-America BTA 2000,²⁴³ and the AFTA 2006 (ASEAN Free Trade Agreement).²⁴⁴ Especially, after joining the WTO, the entire legal system in Vietnam dramatically changed in order to meet the requirements under the WTO's agreements and the accession commitments of Vietnam.²⁴⁵

The way of specifying the relationship between Vietnamese laws and international laws also shows Vietnam's commitment to improvement of its legal system in accordance with international laws, and the laws of commercially developed countries around the world. Where an international treaty to which Vietnam is a contracting party contains provisions different from the provisions under Vietnam law, the provisions under the treaty prevail.²⁴⁶ In

²⁴² Under its WTO commitments, since 2008, Vietnam began giving equal treatment to both foreign and domestic insurance enterprises. Foreign insurance enterprises may now provide insurance services to foreign invested and wholly foreign owned companies in Vietnam. They may also provide reinsurance, international transport insurance, and insurance brokerage services. Foreign invested insurance enterprises may also deal in compulsory insurance products, such as liability insurance for vehicle owners, see WTO, *Vietnam-Schedule of Specific Commitments*, General Agreement on Trade in Services (GATS), GATS/SC/142, at p42-43; Decree 103/2008/ND-CP of Vietnam's Government, dated 16th September 2008, on compulsory insurance on civil liability of motor vehicle owners. Regarding a company's withdrawal from insurance market, see Decree 114/2008/ND-CP, dated 03rd November 2008, of Vietnam's Government on implementation guidelines of some articles of the Law on Bankruptcy 2004 for businesses in the insurance sector

²⁴³ Implementation of the BTA eliminated the limits on U.S. capital participation in the insurance industry, see Appendix G in Vietnam- America BTA 2000.

²⁴⁴ See Protocol 5 ASEAN Scheme of Compulsory Motor Vehicle Third-Party Liability Insurance in the AFTA 2006

²⁴⁵ By 2005 (the 10th round of WTO accession negotiations), 38 laws and ordinances had been issued. Particularly in 2005, Vietnam passed many laws and ordinances, of which more than 20 laws and ordinances which had been notified to the WTO Secretariat directly related to Vietnam obligations as a WTO member: Law on Conclusion, Accession to and Implementation of Treaties 2005, Civil Code 2005, Enterprise Law 2005, Investment Law, Commercial Law 2005, Law on Intellectual Property Law 2005 (amended in 2009) ... Only in 2006, 07 laws and 04 ordinances that directly related to the WTO agreements were passed by National Assembly and the Standing Committee of the National Assembly: Law on Civil Aviation 2006, Law on Standards and Regulations Techniques 2006, Law on Lawyers 2006, Law on Securities 2006, Law on Information Technology 2006, Law on Real Estate Business 2006, Ordinance on amending and supplementing a number of articles of the Ordinance on Procedures for Settlement of Administrative Cases 2006, Ordinance on Safeguards in Merchandise Trade, Ordinance on Anti-dumping on the Goods imported into Vietnam, Ordinance on Anti-Subsidy on the Goods imported into Vietnam. See: Ministry of Justice (2010), Report on Vietnamese law reform in order to implement the commitments of the World Trade Organization (WTO), p. 7

²⁴⁶ Article 6 of Law on the conclusion, accession to and implementation of treaties 2005: "In cases where a legal document and a treaty to which the Socialist Republic of Vietnam is a party, contains different provisions on the same matter, the provisions of the treaty shall prevail"; Article 759(2) of Civil Code 2005: "Where an

other words, a provision under an international convention or treaty to which Vietnam is a party can be considered as a provision of domestic law. This demonstrates Vietnam's desire that Vietnam wants its legal system to be not too different from the legal systems with which trading partners and foreign investors are familiar.²⁴⁷

International economic integration has made the legal system in Vietnam more complete, more transparent, and more consistent with the rules under international conventions on trade and international commercial practices. In addition, it imposes a requirement that Vietnamese laws must be applied in a uniform manner in order to avoid overlap, ambiguity, and uncertainty.²⁴⁸

The uniform application of laws is important not only for the unity of Vietnam's legal system but also for the effective implementation of Vietnamese obligations under international treaties.²⁴⁹ The provisions in lower-ranking legal instruments must be consistent with the provisions in the higher-ranking.²⁵⁰ The legal instruments which are issued later shall prevail over the old ones in the event of differences between the legal instruments of the same level.²⁵¹ Moreover, the unification of the law on the entire territory of Vietnam is ensured through the legal rules that "the local agencies must follow the rules under the legal documents issued by the central government agencies" and that "the legal documents issued

international treaty of which the Socialist Republic of Vietnam is a member contains provisions different from those in this Code, such international treaty shall apply." Article 5(1) of Commerce Law 2005: "Where an international treaty to which the Socialist Republic of Vietnam is a member contains provisions applying foreign law, international commercial practice or other provisions which are inconsistent with the provisions of this Law, then the provisions of such international treaty shall apply."

²⁴⁷ Viện nghiên cứu quản lý kinh tế trung ương (CIEM), *Tác động của hội nhập kinh tế quốc tế đối với nền kinh tế sau ba năm Việt Nam gia nhập WTO*, (2010), p86-87 [Trans: Vietnam's Central Institute for Economic Management (CIEM), *The impact of international economic integration on Vietnam's national economy: 03 years after becoming a member of WTO*, (2010)] available at <<http://www.trungtamwto.vn/sites/default/files/Bao%20cao%20KT-XH%203%20nam%20WTO.pdf>>

²⁴⁸ See Article 1, 6 and 8 of Chapter VI: Transparency-related provisions and right to appeal in the Vietnam-America BTA 2000. Just over 3 years after becoming a member of WTO, over 400 legal documents and 300 business licenses were reviewed, assessed and eliminated; see also Article 3 (1) of the Law on Promulgation of Legal Instruments 2008; Le Mai Anh, *Giao trình luật quốc tế*, (NXB Công an nhân dân, 2006) [Trans: Le Mai Anh, *Textbook on international law*, (People's Public Security Publishing House, 2006)], p73

²⁴⁹ Nguyen Khanh Ngoc, "Phối hợp liên ngành trong xây dựng và hoàn thiện pháp luật thực hiện các điều ước quốc tế", (2009) *Tap chi Nghien cuu lap phap* 16 [Trans: Nguyen Khanh Ngoc, "Joining multi-organs in building up and improving laws on international treaties implementation", (2009) *Journal of Legislative Studies* 16], p21

²⁵⁰ Article 84 of Law on Promulgation of Legal Instruments 2008; Pham Duy Nghia, "Ban ve du thao luật ban hành văn bản quy phạm pháp luật", (2008) *Tap chi Nghien cuu lap phap* 31 [Trans: Pham Duy Nghia, "Discussion on the draft of law on the promulgation of legal documents", (2008) *Journal of Legislative Studies* 31], p35

²⁵¹ Article 9 of Law on Promulgation of Legal Instruments 2008; Nguyen Thi Minh Ha, "Vi tri cua van ban quy phạm pháp luật trong hệ thống pháp luật", (2006) *Tap chi Nha nuoc va Phap luật* 5 [Trans: Nguyen Thi Minh Ha, "Position of normative legal documents in the Vietnam's legal system", (2006) *Journal of State and Law* 5], p6

by the local agencies must comply with the rules set out by the central government agencies.”²⁵²

In short, international economic integration has helped the Vietnamese legal system to be more consistent with international standards, contributing to the country’s economic reform.

3.2. Legislative bodies

In Vietnam, the system of legal document is divided into two main types: legislation (the Constitution and law codes, law acts) and delegated legislation.²⁵³ The legislation sets out general rules. In order to apply the general rules (provisions of the laws) in a specific case in practice, there is a need for delegated legislation which provides the details. The delegated legislation is issued by state agencies that are authorised by the National Assembly (NA).²⁵⁴ A provision in the delegated legislation shall not be contrary to the spirit and detailed content of the Constitution and the law codes and law acts.²⁵⁵

In Vietnam, the National Assembly is the only organ with constitutional and legislative powers.²⁵⁶ The NA is the highest representative organ of the people, representing the will and power of the people,²⁵⁷ and is the highest state authority in Vietnam,²⁵⁸ having the rights to decide the most important issues of Vietnam and the rights to exercise supreme control over all activities of the State.²⁵⁹ Therefore, only the NA has the sole right to make and amend the

²⁵² Dao Tri Uc, *Nhung van de ly luan co ban ve nha nuoc va phap luat*, (NXB Chinh tri quoc gia, 1995) [Trans: Dao Tri Uc, *Basic theoretical issues on state and law*, (National Politics Publishing House, 1995)], p53-55; Le Minh Tam, *Giao trinh ly luan nha nuoc va phap luat*, (NXB Tu phap, 2006) [Trans: Le Minh Tam, *Textbook on theories of state and law*, (Justice Publishing House, 2006)]; p83

²⁵³ Pham Duy Nghia, *Chuyen khao luat kinh te*, (NXB Dai hoc Quoc gia, 2004) [Trans: Pham Duy Nghia, *Vietnamese Business Laws: Textbook for Postgraduate Program*, (Publisher of National University, 2004)], p148; Le Minh Tam, *Xay dung va hoan thien he thong phap luat Viet Nam- nhung van de ly luan va thuc tien*, (NXB Cong an nhan dan, Ha Noi, 2003) [Trans: Le Minh Tam, *Building up and improving the Vietnamese legal system- issues on theories and practices*, (People’s Public Security Publishing House, Hanoi, 2003)], p87-92

²⁵⁴ Article 8 of Law on Promulgation of Legal Instruments 2008

²⁵⁵ Article 2 and 83 of Law on Promulgation of Legal Instruments 2008; see also: Nguyen Cuu Viet, “Khai niem van ban quy pham phap luat va he thong van ban phap luat”, (2007) *Tap chi Nghien cuu lap phap* 27 [Trans: Nguyen Cuu Viet, “A concept of legal normative documents and a system of legal documents”, (2007) *Journal of Legislative Studies* 27], p29; Nguyen Thi Minh Ha, “Vi tri cua van ban quy pham phap luat trong he thong phap luat”, (2006) *Tap chi Nha nuoc va Phap luat* 5 [Trans: Nguyen Thi Minh Ha, “Position of normative legal documents in the Vietnam’s legal system”, (2006) *Journal of State and Law* 5], p8

²⁵⁶ Article 83 of Vietnam’s Constitution 1992

²⁵⁷ *Ibid*

²⁵⁸ *Ibid*

²⁵⁹ *Ibid*

Constitution, to make and amend laws, and to work out a programme for making laws.²⁶⁰ Only governmental agencies which are authorised by the NA have rights to issue delegated legislation.²⁶¹

According to the Constitution and Law on the promulgation of legal documents 2008, the governmental agencies have authority to issue legal documents, as follows:

(i) The NA has the power to amend the Constitution and to promulgate law codes and law acts.²⁶²

(ii) The NA's Standing Committee has authority to issue ordinances and resolutions.²⁶³ Ordinances contain regulations on issues upon instruction by the NA.²⁶⁴ After a certain period of implementation, these issues can be submitted to the NA for its consideration and decision in order to develop into laws. Resolutions are issued to explain the Constitution, laws and ordinances, and to guide the operations of Peoples Councils.²⁶⁵

(iii) The President has the power to issue orders and decisions in order to carry out its powers.²⁶⁶

(iv) The Government has the power to issue decrees.²⁶⁷ Decrees provide detailed guidelines on the implementation of laws and resolutions of the NA and ordinances and resolutions of the NA's Standing Committee.²⁶⁸

(v) Ministry and the ministry-level government agencies are allowed to issue circulars.²⁶⁹ Circulars give detailed guidelines on the implementation of laws and resolutions of the NA, ordinances and resolutions of the NA's Standing Committee, orders and decisions of the State

²⁶⁰ *Ibid*; see also: Truong Quoc Hung, "Quoc hoi co phai la co quan lam luat", (2008) *Tap chi Nghien cuu lap phap* 23 [Trans: Truong Quoc Hung, "Is the National Assembly a legislative body?" (2008) *Journal of Legislative Studies* 23], 25-26

²⁶¹ Nguyen Dang Dung, *Giao trinh luat Hien phap Viet Nam*, (NXB DH Quoc gia, 2006) [Trans: Nguyen Dang Dung, *Textbook on the Constitution Law of Vietnam*, (National University Publishing House, 2006)], p358-359

²⁶² Article 11 of Law on Promulgation of Legal Instruments 2008

²⁶³ Article 12 of Law on Promulgation of Legal Instruments 2008

²⁶⁴ *Ibid*

²⁶⁵ *Ibid*

²⁶⁶ Article 13 of Law on Promulgation of Legal Instruments 2008

²⁶⁷ Article 14 of Law on Promulgation of Legal Instruments 2008

²⁶⁸ *Ibid*

²⁶⁹ Article 16 of Law on Promulgation of Legal Instruments 2008

President, decrees of the Government,²⁷⁰ and provide regulations on technical processes and standards of the sector covered by each ministry.²⁷¹

(vi) People's Councils and People's Committees are given authority to issue resolutions, decisions and directives. The People's Council is the local organ of state power, representing the will, aspirations, and authority of the people.²⁷² It is elected by the local people and is accountable to them and to the superior state organs. The People's Committee elected by the People's Council is the latter's executive organ and the organ of local state administration. It is its responsibility to implement the Constitution, the law, the formal written orders of superior state organs and the resolutions of the People's Council.²⁷³

The legal instruments which are issued by People's Councils and People's Committees aim to secure implementation of the Constitution and the laws and the legal instruments issued by the central governmental agencies at local level;²⁷⁴ and to carry out the plan for socio-economic development, defence and security tasks, and the execution of the budget in the locality.²⁷⁵

3.3. Judicial bodies

The judicial system of Vietnam consists of the court system and the prosecution system. They are under the duty to safeguard socialist legality, the socialist regime and the people's mastery, the property of the State and the collectives, the lives, property, freedom, honour and dignity of the citizen.²⁷⁶

The Chairman of the People's Supreme Court and the Chairman of the Supreme People's Procuracy are elected, removed from office and dismissed by the NA at the proposal of the State President, and are subject to the NA's supervision.²⁷⁷ The local People's Courts and

²⁷⁰ *Ibid*

²⁷¹ *Ibid*

²⁷² Article 119 of Vietnam's Constitution

²⁷³ Article 123 of Vietnam's Constitution

²⁷⁴ Dao Tri Uc, *Nhung van de ly luan co ban ve nha nuoc va phap luat*, (NXB Chinh tri quoc gia, 1995) [Trans: Dao Tri Uc, *Basic theoretical issues on state and law*, (National Politics Publishing House, 1995)], p248; Le Minh Tam, *Giao trinh ly luan nha nuoc va phap luat*, (NXB Tu phap, 2006) [Trans: Le Minh Tam, *Textbook on theories of state and law*, (Justice Publishing House, 2006)]; p194

²⁷⁵ Nguyen Dang Dung, *Giao trinh luat Hien phap Viet Nam*, (NXB DH Quoc gia, 2006) [Trans: Nguyen Dang Dung, *Textbook on the Constitution Law of Vietnam*, (National University Publishing House, 2006), p382

²⁷⁶ Article 126 of Vietnam's Constitution 1992

²⁷⁷ Constitution 1992; Law on organisation of the People's Courts 2002

local People's Procuracies are subject to the supervision of the People's Councils of the same levels, and have the responsibility to report on their activities before the People's Councils.²⁷⁸

3.3.1. People's Court

Under the Law on organisation of the People's Courts 2002, the hierarchy of the People's Courts was divided into three levels:²⁷⁹ (i) the Supreme People's Court, (ii) the province-level People's Courts,²⁸⁰ and (iii) the district-level People's Courts.²⁸¹

At the central level and the provincial level, the organizational structure of the People's Courts is divided into six types: administration courts, criminal courts, civil courts, economic courts, labour courts and military tribunals which are special courts for military crimes.²⁸² At the district level, the people's courts are not divided into specialized courts, but there are specialized judges who are in charge of each type of incident.²⁸³

The Vietnamese courts follow the regime of two-level adjudication: first-instance trial and appellate trial.²⁸⁴

The courts' first-instance judgments can be appealed or protested against.²⁸⁵ First-instance judgments which are not appealed or protested against according to appellate procedures within the time limit of 15 days become legally effective.²⁸⁶ Where first-instance judgments are appealed or protested against, the cases must undergo appellate trials. The appellate judgments shall be legally effective and will be final and conclusive.

However, in some exceptional circumstances, special procedures must be followed. The courts' judgments which have already taken legal effect but in which serious law violations or new details have been detected shall be reviewed according to the cassation or reopening procedures.²⁸⁷ Cassation or reopening procedures²⁸⁷ are special procedures in which the

²⁷⁸ Article 29, 31, and 33 of Law on organisation of the People's Courts 2002; article 35 of Law on organisation of the People's Procuracies 2002

²⁷⁹ Article 2 of Law on organisation of the People's Courts 2002

²⁸⁰ Province-level includes centrally-run cities, provinces

²⁸¹ District-level includes urban districts, rural districts and provincial cities

²⁸² Article 18 and article 27 of Law on organisation of the People's Courts 2002

²⁸³ Nguyen Dang Dung, *Giao trinh luat Hien phap Viet Nam*, (NXB DH Quoc gia, 2006) [Trans: Nguyen Dang Dung, *Textbook on the Constitution Law of Vietnam*, (National University Publishing House, 2006)], p387

²⁸⁴ Article 17 of Civil Procedure Code 2004

²⁸⁵ Article 17 of Civil Procedure Code 2004

²⁸⁶ Article 245 of Civil Procedure Code 2004

²⁸⁷ Article 17 and 18 of Civil Procedure Code 2004

Supreme People's Court supervises the adjudication by courts of all levels in order to ensure a strict and uniform application of law.²⁸⁸

In terms of legislation, the People's Supreme Court has authority to issue resolutions, which are legal instruments, to guide courts of all levels in applying laws in a consistent manner.²⁸⁹

3.3.2. People's Procuracy

The system of the People's Procuracy is similar to the system of the People's Court. Under the Law on organisation of the People's Procuracies 2002, the hierarchy of the People's Procuracies are also divided into three levels:²⁹⁰ (i) The People's Supreme Procuracy, (ii) provincial-level procuracies, and (iii) district-level procuracies.

The People's Procuracies are in charge of exercising the right to initiate public prosecution and to ensure a serious and uniform implementation of the law.²⁹¹ To do this, they supervise the law's observance in all types of procedures and exercise the rights to request, petition or protest according to law provisions in order to ensure lawful and timely resolution of cases and matters; and they also supervise the lawfulness of the activities of the law enforcement agencies, such as criminal investigations and enforcement of judgments.²⁹²

In terms of legislation, the Supreme People's Procuracy has authority to issue circulars (legal instruments) to ensure the fulfilment of the tasks and authority of local People's Procuracies.²⁹³

4. INSURANCE LEGISLATION IN VIETNAM

4.1. Development of legal framework governing insurance sector

There were two important landmarks in the legal environment after the Vietnamese government launched the economic renovation policies.²⁹⁴ The first is the Decree 100/1993

²⁸⁸ Article 18 of Civil Procedure Code 2004

²⁸⁹ Article 17 of Law on promulgation of legal instruments 2008

²⁹⁰ Article 30 of Law on organisation of the People's Procuracies 2002

²⁹¹ Article 137 of Vietnam's Constitution 1992

²⁹² Article 2 and 3 of Law on organisation of the People's Procuracies 2002

²⁹³ Article 18 of Law on promulgation of legal instruments 2008

²⁹⁴ "Doi moi" policies- economic reform in 1986

which is the first regulation on insurance business;²⁹⁵ and the second is the first Law on Insurance Business 2000.²⁹⁶ Therefore, the development of the legal framework governing the insurance sector in Vietnam can be divided into three stages: before 1993, from 1993 to 2000, and after 2000.

4.1.1. Before 1993:

Before 1993, there was only one state-owned insurance company (Bao Viet) operating in Vietnam.²⁹⁷ It can be said that, at this stage, a legal framework for insurance activities in Vietnam had not been established.²⁹⁸ Insurance was not considered a business activity. It was viewed as a means of sharing risk among state-owned enterprises. The supply of insurance services was governed by the rules of the Ministry of Finance. These rules were administrative orders, and not specified in detail.²⁹⁹ Only a few issues were addressed, such as insurance products, insurance contracts, terms and conditions, premium rate, and dispute settlements.

In addition to the rules of the Finance Ministry, some insurance services were governed by separate legal documents; for example, marine insurance contracts were governed by the Maritime Code 1990,³⁰⁰ and civil liability of aircraft carriers by the Law on Aviation 1992.³⁰¹

4.1.2. From 1993 to 2000

The legal framework governing the insurance sector in Vietnam had undergone its first transformation in 1993, marked by the Decree 100/CP/1993, regulating insurance business activities. It was considered as an initial step for opening the insurance market.³⁰² This was the first time that Vietnam officially recognised insurance as a business activity, and the insurance market was opened to private insurance companies. The monopoly in the insurance

²⁹⁵ Decree No 100/CP/1993, dated 18th Dec. 1993, of Vietnam's Government on insurance business. (This is delegated legislation)

²⁹⁶ Law on Insurance Business 2000, dated 9th Dec 2000 (this is a law act, and has a higher value than delegated legislation in the Vietnam's system of legal documents)

²⁹⁷ See section 2.1 of this Chapter

²⁹⁸ Truong Moc Lam, "Nganh kinh doanh bao hiem o Vietnam- mot chang duong", (2003) *Tap chi Bao hiem 1* [Trans: Truong Moc Lam, "Vietnam's insurance industry- a history", (2003) *Insurance Review 1*], p8

²⁹⁹ For example, see Decision 254/QD/ TC-BH of Vietnam's Finance Ministry, dated 25th May 1990, gave permission to Bao Viet to supply marine insurance services

³⁰⁰ 41 articles- from article 200 to article 240

³⁰¹ 10 articles- from article 72 to article 81

³⁰² Vu Nhu Thang, "Necessary reform of insurance business law in Vietnam after its accession to the WTO: prudential regulatory aspects" (2007) 12(6) *Fordham Journal of Corporate & Financial Law* 977, p982; Truong Moc Lam, "Nganh kinh doanh bao hiem o Vietnam- mot chang duong", (2003) *Tap chi Bao hiem 1* [Trans: Truong Moc Lam, "Vietnam's insurance industry- a history", (2003) *Insurance Review 1*], p10

sector was replaced by diversified players, including: 100% foreign-owned companies, joint stock companies, joint ventures, branches of foreign insurance companies, and state-owned companies.³⁰³ Insurance services were diversified, namely as life insurance, non-life insurance, reinsurance, brokerage, and agency.³⁰⁴

The Decree consisted of 6 chapters- 37 articles concerning the establishment and operation of an insurance company and the state management on insurance business. On the scope of the insurance business, insurance companies were allowed to provide basic insurance products.³⁰⁵ However, an insurance company had to conduct business strictly in accordance with the lines of insurance business listed in the business registration certificate issued by the Ministry of Finance.³⁰⁶ The decree also stipulated strict regulations on minimum legal capital to establish an insurance company,³⁰⁷ the ability to guarantee payment and the duty to establish a reserve fund of an insurance company,³⁰⁸ and obligations to report about operating results and financial position to the Ministry of Finance.³⁰⁹ But, in this Decree, there is no provision governing insurance contracts.

In addition, as insurance was considered a business activity, competitiveness of insurance companies was initially subject to business regulation. Before 1995, it was not unusual for ministries, or governmental departments, or state-owned companies to require entities or individuals under their administrative jurisdiction to purchase insurance from state-owned insurance companies.³¹⁰ In 1996, the Vietnamese government requested that government agencies cease to influence the insurance market;³¹¹ and, the Ministry of Finance eliminated an earlier legal requirement that, when purchasing insurance for a state-financed construction project, project managers give priority to state-owned insurance companies.

³⁰³ Article 2 of the Decree No 100/CP/1993

³⁰⁴ Article 6 and 8 of the Decree No 100/CP/1993

³⁰⁵ See article 7 of the Decree No 100/CP/1993, namely: life insurance; voluntary health insurance and personal accident insurance; property damage insurance; insurance on transportation by road, sea, river, rail and air; hull insurance and civil liability of ship-owners; general liability insurance; aviation insurance; motor vehicle insurance; fire insurance; credit insurance and insurance on financial risks; insurance on business damage; and agricultural insurance.

³⁰⁶ Article 5 and 8 of the Decree No 100/CP/1993

³⁰⁷ Article 22 of the Decree No 100/CP/1993

³⁰⁸ Article 9, 10, 11 and 13 of the Decree No 100/CP/1993

³⁰⁹ Article 25 to article 33 of the Decree No 100/CP/1993

³¹⁰ Truong Moc Lam, "Nganh kinh doanh bao hiem o Vietnam- mot chang duong", (2003) *Tap chi Bao hiem* 1 [Trans: Truong Moc Lam, "Vietnam's insurance industry- a history", (2003) *Insurance Review* 1], p11

³¹¹ Official Letter 3780/TC-TCNH of Vietnamese government, dated 25th October 1996

4.1.3. From 2000 to the present

In 2000, the Decree 100/CP/1993 was replaced by Vietnam's Law on Insurance Business 2000. The legal framework governing the insurance sector was significantly improved under the Law on Insurance Business 2000.³¹² This Law reinforced the safety and soundness of the domestic insurance market, and strengthened the financial capacity of insurance companies.³¹³

First, both local and foreign insurance companies are governed by the same legal framework. Market access requirements such as minimum legal capital,³¹⁴ deposits,³¹⁵ and application procedures³¹⁶ are the same for both local and foreign investors.³¹⁷ Second, the Law on Insurance Business itself specifically prohibits illegal competitive action.³¹⁸ For example, it forbids providing untruthful information and false advertising related to insurance terms and polices, and intimidating customers or employees of other insurance companies.³¹⁹ Third, insurance companies in Vietnam have the freedom to develop their distribution systems.³²⁰ They are allowed to formulate their own strategies for agencies and set up their own agency commission rates. They are free to create insurance products that meet clients' demands and determine prices through market competition. Fourth, in order to strengthen the financial capacity of insurance companies, detailed requirements to ensure the solvency of insurers are stipulated in the Law and guiding decrees.³²¹ A system of internal supervision and control for

³¹² The Law consists of 129 articles, which are divided into nine chapters. Chapter One covers general principles, including the application of law, terms and definitions, and classes of insurance services. Chapter Two covers 46 articles governing insurance contracts, including categories of insurance contracts, their contents, rights and obligations of insurers and insured. Chapters Three through Five provide rules for market entry and operations of domestic insurance companies, insurance brokers and agents, including licensing procedures, transfer of insurance contracts, recovery of solvency, dissolution, bankruptcy, as well as accounting and financial statements. Chapter Six deals with specific requirements for licensing and operations of foreign invested insurance companies and foreign invested insurance brokers in Vietnam. Chapter Seven gives rules for the state administration of the insurance industry, including regulatory and supervisory functions. While Chapter Eight includes provisions on rewards and handling of breaches of the law, the final chapter is comprised of implementing provisions.

³¹³ Vu Nhu Thang, "Necessary reform of insurance business law in Vietnam after its accession to the WTO: prudential regulatory aspects" (2007) 12(6) *Fordham Journal of Corporate & Financial Law* 977, p983

³¹⁴ Article 94 of the Law on Insurance Business 2000; see also article 4 of the Decree 46/2007/ND-CP, dated 27th March 2007, on the financial regime applicable to insurance companies and insurance brokerage companies.

³¹⁵ Article 95 to 98 of the Law on Insurance Business 2000

³¹⁶ Article 58 to article 69 of the Law on Insurance Business 2000

³¹⁷ Article 5 of the Law on Insurance Business 2000

³¹⁸ Article 10(1) of the Law on Insurance Business 2000

³¹⁹ Article 10(2) of the Law on Insurance Business 2000

³²⁰ Article 84 to 88 of the Law on Insurance Business 2000

³²¹ Article 77 to 81, article 96, and article 97 of the Law on Insurance Business 2000; see also Decree 46/2007/ND-CP, dated 27th March 2007, on the financial regime applicable to insurance companies and insurance brokerage companies.

insurance companies has been introduced,³²² measuring changes in capital sources and funds, indemnity ratios, insurance commission ratios, and asset investment profit ratios. An independent regulatory body, monitoring and supervising all the activities in the insurance market has been established.³²³ Fifth, provisions governing insurance contracts have been put into the Law, including categories of insurance contracts, their contents, and the rights and obligations of insurers and insureds.³²⁴

Besides the advantages of the Law in facilitating the development of Vietnam's insurance industry in order to keep up with requirements of the process of opening up the economy and international economic integration, practical application of the rules in the Law has revealed a number of weaknesses. The Law puts great emphasis on the provisions relating to the establishment and operation of insurance companies, and creation of a sound and fair business environment to both local and foreign insurers in order to fulfil Vietnam's commitments under bilateral and multilateral agreements, but it does not pay adequate attention to the provisions governing insurance contracts.³²⁵ The provisions governing insurance contracts are not comprehensive. There exist contradictions,³²⁶ ambiguities, different understandings³²⁷ or insufficiencies of detailed guidelines. Some of the provisions are no longer appropriate to the practical requirements of the insurance market.³²⁸

³²² Decision 153/2003/QĐ-BTC of Ministry of Finance, dated 22nd September 2003) on criteria for monitoring financial capacity of insurance companies. The Supervisory criteria reports produced based on the criteria in the Decision 153 must be submitted to the Ministry of Finance along with an enterprise's annual financial reports.

³²³ Insurance Commission was established under the Decision 288/QĐ-BTC of the Ministry of Finance, dated 12th February 2009, on functions, tasks, powers and organizational structure of the Insurance Commission, and the Decree 118/2008/ND-CP, dated 27th November 2008, on functions, tasks, powers and organizational structure of the Ministry of Finance. The Insurance Commission administers state works in the insurance industry and directly supervises insurance business and other related services.

³²⁴ From article 12 to article 57 in Chapter 2 of the Law on Insurance Business 2000

³²⁵ Nguyen Thi Thuy, "Chuyen giao quyên doi boi thuong trong bao hiem tai san" (2008) *Tap chi Khoa hoc phap ly* 5 [Trans: Nguyen Thi Thuy, "Transfer of right to make a claim in property insurance", (2008) *Journal of Legal Science* 5] p5; Tran Vu Hai, *Hợp đồng bảo hiểm nhân thọ - Những vấn đề lý luận và thực tiễn*, (NXB Tu pháp, 2006) [Trans: Tran Vu Hai, *Contracts of life insurance- theories and practices*, (Justice Publishing House, 2006)], p67

³²⁶ In terms of terminating insurance contracts, according to article 19 of the Law, an insurer has the right to unilaterally suspend contracts and collect insurance premiums up to the time of contract suspension when a policyholder has intentionally provided false information in order to enter an insurance contract to make an unfair profit. Meanwhile, according to article 22 of the Law, an insurance contract is invalid where a policyholder engages in fraud when entering an insurance contract. As a result, the provision of false information to enter an insurance contract may lead to either unilateral termination of a contract or annuls the contract. Nevertheless, the legal consequences of unilateral termination and these invalid contracts are completely different.

³²⁷ There is confusion between doctrine of subrogation and doctrine of assignment in article 49 of the Law. This confusion is analysed in section 5 of Chapter 5: Subrogation.

³²⁸ I.e. article 3(9) relating to insurable interest. It is discussed in Chapter 4: Insurable interest.

4.2. Sources of insurance legislation

4.2.1. Primary legislation

The most important legal documents in the field of insurance law is the Law on Insurance Business, no. 24/2000/QH10, issue date: Dec 9th, 2000; effective date: Jan 4th, 2001, amended and supplemented by the Law no. 61/2010/QH12, issue date: Jun 12th, 2010; effective date: Jul 1st, 2011.³²⁹

In addition, a number of other law acts relating to insurance were issued, such as the Law on Fire Prevention and Fighting, no. 27/2001/QH10, issue date: Jun 29th, 2001; effective date: Oct 4th, 2001 (governing fire and explosion insurance); Vietnam's Marine Code, no. 40/2005/QH11, issue date: Jun 27th, 2005, effective date: Jan 1st, 2006 (governing marine insurance).

For each specific field of insurance, Vietnam's NA enacted regulatory legal documents, for instance, in the field of social insurance, the Law on Social Insurance, no. 71/2006/QH11, issue date: Jul 12th, 2006; effective date: Jan 1st, 2007; the Labour Code, Chapter XII. Social insurance, issue date: Jul 5th, 1994; effective date: Jan 1st, 1995 (repealed by new Labour Code 2012), Resolution 80/TVQH, dated Jan 1st, 1961, ratifying the temporary regulation of social insurance for state-owned staff, in the field of health insurance, the Law on Health Insurance, no. 25/2008/QH12, issue date: Nov 28th, 2008; effective date: Jul 1st, 2009.

In relation to insurance contracts, in addition to the provisions of the Law on Insurance Business 2000 (Chapter 1, Section 1: General regulation on insurance contract), the provisions under Part II, Chapter XVIII, Section 11 of Vietnam's Civil Code regulate this type of contract. The order of application of the provisions of these two legal documents complies with the principle that specific laws prevail over general laws. The provisions of the Law on Insurance Business 2000 prevail over those of the Civil Code 2005. Where the provisions of the former are unclear or incomplete, or there is no provision of the former governing the issue in question, the provisions of the later shall apply. This principle also applies for insurance contracts in each particular field. For example, a marine insurance contract will be first governed by the Maritime Code 2005 (specific laws), and then the Law on Insurance Business 2000 (general laws).

³²⁹ 16 articles relating to establishment and operation of an insurance company and to state management on insurance business under the Law on Insurance Business 2000 are amended.

4.2.2 Delegated legislation

The Vietnamese government and the ministries have enacted many legal documents to provide the details and guidelines for implementation of the above legislation. These documents include decrees issued by the government and circulars issued by the ministries, and ministerial-level government agencies.

In relation to general insurance, there are several documents, such as: (i) Decree no. 100/CP, dated Dec 18th, 1993, (amended by Decree no. 42/2001/ND-CP, dated Aug 1st, 2001, regulating in detail the application of Law on Insurance Business), and (ii) Decree no. 45/2007/ND-CP, dated Mar 27th, 2007, regulating in detail the application of Law on Insurance Business), and (iii) Decree no. 123/2011/ND-CP, regulating in detail the application of the Law amending and supplementing the Law on Insurance Business 2010, and (iv) Decree no. 41/2009/ND-CP, dated May 5th, 2009, provisioning administrative sanctions in business insurance. In addition, there are many relevant circulars.³³⁰

Concerning other fields of insurance, such as fire insurance, health insurance, social insurance, there are also many relevant legal documents.³³¹

In terms of the legal validity and order of application of the legal instruments, the legislation will have higher legal value than the decrees, and then circulars, which are the lowest. Thus, where the decrees and circulars contain provisions inconsistent with the provisions of law codes or law acts, they will not apply.

Conclusion

After having considered the Vietnamese political, economic and social background and the insurance industry and insurance legislation in Vietnam, it is now appropriate to discuss, in the next three chapters, the principle of indemnity and the doctrine of insurable interest and the doctrine of subrogation, and how the principle and the doctrines are applied in Vietnamese insurance laws and practice.

³³⁰ Circular no. 43/TC/TCT, dated June 5th, 1995, Guiding on the tax revenue of insurance and re-insurance business, Circular no.26/TT-BTCT, dated March 4th, 1998, Guiding on the procedure of issuing the qualification certificate for business insurance, Circular no. 71/2001/TT-BTC, dated Aug 28th, 2001, Guiding on the application of Decree no. 42/2001/ND-CP, Circular no. 155/2007/TT-BTC, dated Dec 20th, 2007, Guiding on the application of Decree no. 45/2007/ND-CP, Circular no. 6/2009/TT-BTC, dated Apr 28th, 2009, appending and amending the circular no. 155/2007/TT-BTC and circular no. 156/2007/TT-BTC, Circular no. 03/2010/TT-BTC, dated Jan 12th, 2010, guiding on the application of Decree no. 41/2009/ND-CP.

³³¹ Because these legal documents are not directly related to this thesis, no further information is provided.

CHAPTER 3: THE PRINCIPLE OF INDEMNITY

1. INTRODUCTION:

The principle of indemnity is a fundamental principle in indemnity insurance, and is the backbone and the foundation for the formulation of the other principles in insurance laws, such as the principle of insurable interest and the principle of subrogation, which are discussed in chapters 4 and 5 separately. The nature of the principle is that when the insured event occurs, the insureds are entitled to receive compensation equal to the actual loss they have suffered.³³² In any case, the insured cannot receive compensation greater than the actual loss, but not less than the actual loss.³³³ Based on this principle, the rights and obligations of the parties to the insurance contract are agreed upon in the contract. When a dispute arises between the parties, the interpretation of the terms of the insurance contract must be consistent and must adhere to the nature of this principle.³³⁴

The nature of the principle of indemnity is well recognised and reflected in all countries' insurance laws.³³⁵ The purpose of indemnity insurance is to put the insureds into the financial position enjoyed immediately before the loss occurs, no more and no less. This principle was well developed in England, and then gradually recognized in the insurance laws of many countries around the world, including Vietnam.

³³² In *Castellain v. Preston* (1883) 11 Q.B.D. 380, p387 Brett L.J. said: "The fundamental rule of insurance law is that the contract of insurance contained in a marine or fire policy is a contract of indemnity, and of indemnity only, and this contract means that the assured, in the case of a loss against which the policy has been made, shall be fully indemnified, but shall never be more than fully indemnified."

³³³ ALRC Discussion Paper 63, para. 7.3; R. Keeton, *Basic text on insurance law*, (West Publishing Co., 1971), p88; SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p133-134

³³⁴ S Hodges, *Law of Marine Insurance*, (Cavendish Publishing Limited, London, 2005), p1

³³⁵ W. Williams, "The principle of indemnity: a critical analysis" (1960) *Ins. L.J.* 471, p471; A. Lindblad, "How relevant is the principle of indemnity in property insurance" (1976) *Ins.L.J.* 271, p271; J.P. Van Niekerk, "Maintaining the principle of indemnity: theory and practice", (1996) *J. S. Afr. L. [Journal of South Africa Law]* 572, p572; Article 46 of Vietnam's Law on Insurance Business 2000: "*Basis of indemnity*: (1). The amount of indemnity which an insurer must pay to the insured person shall be determined on the basis of the market price of the insured property at the point of time when and place where the loss is suffered and on the basis of the actual level of damage, unless otherwise provided in the insurance contract. The cost of determining the market value and the level of damage shall be borne by the insurer. (2). The amount of indemnity which an insurer shall pay to the insured person shall not exceed the amount of the sum insured, unless otherwise provided in the insurance contract. (3). In addition to the amount of indemnity, an insurer must also pay to the insured person the necessary and legitimate expenses of measures for prevention and minimization of loss and the costs arising which the insured person must bear in order to implement instructions of the insurer." Article 47 of Vietnam's Law on Insurance Business 2000: "*Forms of indemnity*: (1). The purchaser of insurance and the insurer may agree on one of the following forms of indemnity: (a) Repair of the damaged property; (b) Replacement of the damaged property with other property; (c) Payment of monetary compensation. (2). If the purchaser of insurance and the insurer fail to agree on the form of indemnity, monetary compensation shall be paid. (3). In the case of indemnity under clauses 1(b) and (c) of this article, the insurer shall have the right to repossess the damaged property after it has been replaced or after full payment of indemnity in accordance with the market price of the property."

To ensure an effective implementation of the principle of indemnity, insurance laws of the countries have set out rules and regulations limiting the possibility that the insureds receive compensation amount greater than the losses they have suffered. These rules and regulations prevent the insureds from making profit from insurance contracts. The principles derived from the principle of indemnity are the principle of insurable interest, the principle of subrogation, the principle of double insurance, and the principle of abandonment,... The measure of indemnity is also formulated to ensure that the principle of indemnity can be easily applied in practice.

Preventing the insureds from obtaining unjust enrichment from insurance contracts is the primary purpose of the principle of indemnity. Therefore, the principles derived from the principle of indemnity reflect this primary purpose, and the interpretation and application of these principles often inhibit the insureds from making an unfair profit.³³⁶ In terms of judicial matters, the courts also incline towards pursuing this goal of the indemnity principle.³³⁷

The indemnity principle is a “two-sides” principle. It prevents the insureds from making profit from their insured loss; on the other hand, it also allows the insureds to be fully indemnified. Therefore, there is another goal of the principle of indemnity, which is to ensure that the insureds are compensated no less than the actual losses they have suffered, or in other words, are fully compensated for the losses.³³⁸ This goal is often not emphasized in the insurance laws of some countries. Sometimes the interpretation and application of the principles derived from the principle of indemnity are even contrary to this goal,³³⁹ leaving the insureds compensated for less than the actual losses, or denying them compensation. Within the scope of this thesis, it is submitted that this is an important goal of the indemnity principle, which should be kept in mind when interpreting and applying this principle as well as the principles derived from it. This will help to avoid situations in which the insurers

³³⁶ J.P. Van Niekerk, “Maintaining the principle of indemnity: theory and practice”, (1996) J. S. Afr. L. [Journal of South Africa Law] 572, p572

³³⁷ See section 3.2.2 of Chapter 4: Insurable interest and section 4 of Chapter 5: Subrogation

³³⁸ J.P. Van Niekerk, “Maintaining the principle of indemnity: theory and practice”, (1996) J. S. Afr. L. [Journal of South Africa Law] 572, p572; W. Williams, “The principle of indemnity: a critical analysis” (1960) *Ins. L.J.* 471, p471; J Birds, “Insurance: subrogation in the House of Lords”, (1993) *J.B.L* 294, p299; M Hemsworth, “Subrogation: the problem of competing claims to recovery monies”, (1998) *J.B.L* 111, p114; A Tar, “Subrogation and the Ash Wednesday bushfire disaster”, (1987-1988) *11 Adel. L. Rev.* 232, p233; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1028-1029; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p720; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p326; G Veal, “Subrogation: The duties and obligations of the insured and rights of the insurer revisited”, (1992) *28 Tort & Ins.L.J* 69, p74

³³⁹ See section 3.2.2 of Chapter 4: Insurable interest and section 4 of Chapter 5: Subrogation

refuse to make compensation to the insureds in an unreasonable and unacceptable manner, thereby severely affecting the legal rights and legitimate interests of the insureds.

In this chapter of the thesis, the nature and purposes of the principle of indemnity in the property insurance laws of England and Vietnam are critically analysed to show that there is not much difference between the laws of the two countries in relation to the interpretation and application of the principle, and to clarify the understanding of giving the insureds compensation to restore them to the financial position enjoyed immediately before the loss occurred, no more and no less. Not only emphasizing the aspect of “no more”, the thesis also emphasizes the aspect of “no less” as an important goal of the indemnity principle. The relationship between the indemnity principle and other principles of insurance law (particularly subrogation and insurable interest) will be made clear.

2. PURPOSES OF THE INDEMNITY PRINCIPLE

To understand the purpose of the principle of indemnity, the nature of insurance should first be considered. Insurance is a mechanism whereby the insureds transfer the risk of an uncertain event to the insurers, and the insurers promise in return for the premiums to pay to the insureds a sum of money if the uncertain event occurs.³⁴⁰ Insurance is a system for wide distribution of accidental losses among all those who are insureds.³⁴¹ Therefore, insurance helps to divide the accidental losses of one or several insureds, and then all of the people who take out insurance share the losses between them. The division and distribution are made through insurance companies, and the insurance companies will restore the insureds to the financial position they were in immediately before the occurrence of the loss, no more and no less.

However, in practice, it is not uncommon that the insureds and insurers may do something against the nature of insurance by violating the principle of indemnity. The insureds may engage in fraud or gambling in the guise of insurance in an attempt to make a profit from insurance contracts.³⁴² On the other hand, the insurers may use legal tools as a technical

³⁴⁰ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p8; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p3

³⁴¹ R. Keeton, *Basic text on insurance law*, (West Publishing Co., 1971), p88

³⁴² *Routh v Thompson* [1809] 11 East 428; *Lonsdale & Thompson v Black Arrow Group* [1993] 2 Lloyd's Rep 428; D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine*

defence³⁴³ or interpret the terms of insurance policies in favour of themselves in order to minimize the amount of compensation paid to the insureds. These behaviours and activities are not consistent with the nature of insurance. The principle of indemnity and other principles derived from the principle of indemnity aim to remove this violation. Therefore, the indemnity principle has two purposes: (i) to prevent the insureds from obtaining unfair enrichment, and (ii) to make sure that the insurers give full compensation for the actual losses the insureds have suffered.

2.1. Preventing the insureds from obtaining unfair enrichment

The indemnity principle is a “checkpoint” to ensure that property insurance contracts shall be interpreted and enforced consistently with the objective of insurance that the insureds are fully compensated for the actual losses they suffered, no more and no less.³⁴⁴ The indemnity principle makes sure that the insureds cannot make a profit from insurance. They cannot receive compensation greater than the actual loss; the maximum amount of compensation which they are entitled to recover is sufficient to place them in the same financial position after a loss as they enjoyed immediately before it occurred. Therefore, the compensation that the insurers pay to the insureds shall not exceed the sum insured, and shall not exceed the actual loss.

In principle, the indemnity principle is infringed if an insurance contract provides a compensation amount greater than the actual loss the insureds suffered.³⁴⁵ The reason for this is that the amount of compensation greater than the actual loss creates opportunities for the insureds to make a profit from insurance contracts. There are two ways in which the insureds

Insurance: The Law in Transition, (Informa, London, 2006), p17; Lee Kiat Seng, “Insurable interest in Singapore”, (1997) *Singapore Journal of Legal Studies* 499, p528; J. Davey, “The reform of gambling and the future of insurance law”, (2004) *Legal Study* 507, p514-515; R. Merkin, “Gambling By Insurance – A Study of the Life Assurance Act 1774” (1980) 9 *Anglo-American L.R.* 331; ALRC 20, p73

³⁴³ *Stock v Inglis* [1884] 12 Q.B.D. 564 per Brett M.R.; *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587; EWCA Civ 885, at para. [7] per Waller L.J.; J. Birds, “A shareholder’s insurable interest in his company’s property”, (1987) *J.B.L.* 309, p309; UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), para 11.45; M. Templeman, “Insurable interest: a suitable case for treatment?” in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p202; J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 *Yale L.J.* 474, p495; Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 *Col.I.R.* 1162, p1163; ALRC 20, p72, ALRC Discussion Paper 63, para. 7.14; ALRC Report 91, para 11.22; D. Galbraith, “An Unmeritorious Defence – The Requirement of Insurable Interest in the Law of Marine Insurance and Related Matters” (1992) 5(3) *Ins LJ* 177

³⁴⁴ “No less” here is understood as the total sum of the amount of insurance money paid by the insurers and the amount that the insured agrees to be his own insurer equals to the actual loss that the insured have suffered.

³⁴⁵ R. Keeton, *Basic text on insurance law*, (West Publishing Co., 1971), p88

may make a profit: (i) gambling in the guise of insurance, and (ii) destroying or causing damage to the insured property and then making a fraudulent claim.

Gambling in the guise of insurance may occur when the insureds do not have any relationship with, or have no legal liability arising from the insured property. For example, in the 18th century, before the development of information technology, anyone could buy insurance for a ship and cargo at sea. Where the insured event occurred, and the insured properties were damaged or destroyed, the insureds were entitled to make a claim to receive insurance proceeds.³⁴⁶ This was an act of betting or gambling in the form of an insurance contract. The insureds had not suffered any actual loss, and they would have made an unfair profit from the insurance policy if any amount of money had been paid to them.

The attempt to cause damage or destruction to the insured property may be made when the insureds fraudulently take out insurance for the value of their property greater than its true value, or when the insured property no longer has value in use for the insureds. Then, the possibility of receiving insurance money gives the insureds an incentive to destroy the insured property or creates in them an expectation or desire for ill fortune to befall the property. The above cases are contrary to the nature of insurance, and the insureds shall not be compensated. The principle of indemnity provides safeguards against such cases.

2.2. The insureds should be fully compensated for their actual losses

In principle, it can be said that the purpose of the indemnity principle is not only to prevent the insureds from obtaining unjust enrichment, but also to ensure that the insurers must pay full compensation for the actual loss the insureds have suffered. This is so because the purpose of the indemnity principle in indemnity insurance contracts is to restore the insureds to the same financial position as they enjoyed immediately before the occurrence of the losses, no more and no less. The insured should not get more than the actual loss, but should not receive less than the actual loss.

³⁴⁶ *Andrews v Herne* [1662] 1 Lev. 33, *Danvers v Thistlewaite* [1669] 1 Lev. 44, *Firebrase v Brett* [1688] 1 Vern 469; *Dalby v India & London Life Ass. Co* [1854] 15 C.B. 365; UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), para. 11.6, p104; Issue Paper 4, para. 2.2, p5; J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p479

In some countries, insurance laws and judicial practices do not emphasize this purpose of the indemnity principle.³⁴⁷ This may prejudice the legitimate interests of the insured. In the relationship between the insurers and the insureds, the insurers are normally the stronger parties; at least, the insurers have more professional skills, and more comprehensive knowledge of insurance law than the insureds. This may lead to the situations wherein insurers take advantage of their strengths to infringe the principle of indemnity. Where a dispute between the parties arises, the insurers use legal instruments or search for the provisions of insurance laws or seek to interpret the terms and conditions of the insurance contract in their favour in order to minimize the compensation amount or to refuse to indemnify the insureds. Therefore, in many cases, the insureds can only get a compensation amount less than the actual loss they have suffered.³⁴⁸ This is unreasonable and unfair.

For example, when applying the principle of insurable interest, the strict interpretation of this principle in accordance with the legal right approach may deprive the insureds of the right to be compensated for their actual loss, or their insurance contracts may be declared void due to lack of a legal interest.³⁴⁹ Under this approach, in order to make a valid claim for the loss, the insured must have the rights to the property, or have the rights or legal liability arising from the insured property. This approach has narrowed the number of cases where the insureds have an insurable interest in the subject matter of insurance. Indeed, there have been several cases in which the insureds actually gained economic benefits from the existence and safety of the property insured, and the insurers accepted to assume the insured risks of uncertain events and promised to pay the insureds in return for the premium if the uncertain events occur. Then however, when the uncertain events actually occurred, in order to deny compensation to the insureds, the insurers alleged that the economic relationship between the insureds and the insured property was not recognized by law, that the insureds had no insurable interest in the property,³⁵⁰ and that therefore the claim for economic losses of the insureds was invalid.

Regarding the principle of subrogation, this principle is often interpreted by insurers in ways that benefit themselves but harm the interests of the insureds. In case of under-insurance and

³⁴⁷ Vietnam, for more details see section 3.2 of Chapter 4: Insurable interest and section 4.1 of Chapter 5: Subrogation

³⁴⁸ For more details, see section 4.1 of Chapter 4: Insurable interest

³⁴⁹ For more details, see section 4.1 of Chapter 4: Insurable interest

³⁵⁰ *Lucena v Craufurd* [1806] 2 Bos. & P.N.R. 269; *Macaura v Northern Assurance Co.* [1925] A.C. 619; *Glengate-KG Properties v Norwich Union Fire Ins Society* [1996] 1 Lloyd's Rep 614

excess clause, although there is no clear agreement in the contract of insurance, the insured are deemed to be their own insurers with respect to the uninsured loss in all circumstances. Following this interpretation, when distributing the subrogation recovery from the third party at fault, the insurers are entitled to first recoup in full the amount they have paid to the insureds regardless of whether or not the latter have been fully compensated for their losses.³⁵¹

It is submitted that where there are legal rules or principles that allow the insurers to reject compensation or give compensation less than the actual loss of the insureds without justifiable grounds, it is a violation of the principle of indemnity. These rules and principles should be removed, because they are inconsistent with the nature of the indemnity principle.

3. THE MEANING OF FULL COMPENSATION

In theory, the insureds, in indemnity insurance, will be fully compensated for their actual losses, and the aim of the principle of indemnity is to place the insureds in the same financial position enjoyed immediately before the losses occur. However, in practice, difficulties in application of the indemnity principle often arise from different understandings of the concept of full compensation.³⁵² Indeed, this concept is complex and is interpreted in several different ways; this leads to different ways of applying the other principles derived from the principle of indemnity.³⁵³

There are some academics who uphold the view that full compensation means that the insureds are fully indemnified according to the terms of their policy, but may not be fully compensated for their actual total loss.³⁵⁴ It means that an insurance benefit shall not be

³⁵¹ See Chapter 5: Subrogation

³⁵² *Simpson v Thomson* [1877] 3 App. Cas. 279; *Burnard v Rodocanachi* [1882] 7 App Cas 333, HL; *Castellain v. Preston* [1883] 11 QBD 380; *Dalby v India & London Life Ass. Co* [1854] 15 C.B. 365; *Prudential Ins Co v Commissioner of Inland Revenue* [1904] 2 K.B. 658; *Jabbour v Custodian of Israeli Absentee Property* [1954] 1 W.L.R. 139; *Firma C-Trade SA v Newcastle P & I Association (The Fanti)* [1991] 2 A.C. 1; *Ventouris v Mountain (The Italia Express (No2))* [1992] 2 Lloyd's Rep. 281; *Sprung v Royal Ins (UK) Ltd* [1999] Lloyd's Rep. I.R 111; see also: N Campell, "The nature of an insurer's obligation" (2000) LMCLQ 42, p48, it said: "The meaning of "to indemnify" and the English cases: A promise "to indemnify" against loss could have one of three meanings: (1) a promise to prevent loss from occurring; (2) a promise that loss will not occur; (3) a promise to compensate the insured in the event that loss does occur"

³⁵³ For more details, see section 4 and 5 of Chapter 4: Insurable interest and section 3 and 4 of Chapter 5: Subrogation

³⁵⁴ For example: under-insurance, excess clause; J Birds, "Insurance: subrogation in the House of Lords", (1993) J.B.L 294, p297; A Green, "Strengthening the insurer's subrogation rights", (1995) 3(10) Int.I.L.R. 348; p349

greater in value than the loss the insureds have suffered but it does not imply, conversely, that the insurance benefit must be no less than the loss.³⁵⁵ This view pays little attention to the aspect of “no less” in the indemnity principle. As a result, the insureds are not fully compensated for their actual losses.

It is submitted that the insureds should be fully compensated for their actual loss. When applying the other principles derived from the principle of indemnity, both aspects of “no more and no less” of the indemnity principle should be taken into consideration. The insureds’ legitimate interests and legal rights to receive full compensation for their actual loss should be protected.³⁵⁶ This will be discussed in details in the following chapters on the subrogation principle and the insurable interest principle. Interpretation of full compensation in relation to each principle derived from the principle of indemnity is given as follows:

- Full compensation in connection with the principle of insurable interest means that the insureds are fully compensated for their actual economic losses if they can prove the losses. If they cannot prove the losses, they will recover nothing.³⁵⁷
- So far as the subrogation principle is concerned, full compensation is understood to be that where the insured loss is caused by a third party the insureds should be fully compensated for their actual loss. They cannot receive compensation greater than the actual loss from the third party and the insurer, but they should not receive less than the loss.³⁵⁸ The insurer's subrogation rights only arise when the insureds are fully compensated for the total loss, not when the insurers have fulfilled their contractual obligations under the insurance contract. Therefore, after receiving compensation from a third person, the two following questions must be raised in the order of priority: (i) first, whether the insureds have been fully compensated for their actual

³⁵⁵ *Napier v Hunter* [1993] A.C. 713; *Leppard v Excess Ins Co Ltd* [1979] 2 All E.R. 668; R. Keeton, *Basic text on insurance law*, (West Publishing Co., 1971), p88; J Birds, “The Measure of Indemnity in Property Insurance”, (1980) 43 *Modern Law Review* 456; C Lewis, “A fundamental principle of insurance law”, (1979) *L.M.C.L.Q* 275; J Lowry and P Rawlings, *Insurance Law: Doctrines and Principles*, (2nd edn, Hart Publishing, Oxford, 2005), p263

³⁵⁶ SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p133-134

³⁵⁷ See section 6 of Chapter 4: Insurable interest

³⁵⁸ *Commercial Union Assurance Co v Lister* [1874] L.R. 9 Ch.App. 483; *Driscoll v Driscoll* [1918] 1 I.R. 152; *Page v Scottish Insurance Corp.* (1929) 33 *L.L.Rep* 134; *Kuwait Airways Corp v Kuwait Insurance SAK (No1)* [1996] *Lloyd’s Rep* 664; A Brown, “An insurer’s rights in litigation or contractual subrogation: an oxymoron?”, (1996) 8 *Ins.L.J.* 60, p60; SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p133-134; M Luey, “Proprietary remedies in insurance subrogation”, (1995) 25 *Victoria.U.Wellington.L.Rev.* 449, p457

losses (ii) second, whether the insureds hold any surplus, if yes this surplus must be paid to the insurers.

- Full compensation, in the case of double insurance,³⁵⁹ indicates that although the insureds have purchased insurance policies from several insurers to cover the same property against the same insured risk, they are only entitled to receive full compensation for their losses, and cannot get insurance monies from all of the insurers with whom they have contracted.³⁶⁰ The most important point here is that, if the insureds have been fully compensated for their loss, they cannot receive insurance money from the other insurers, and the insurer who has paid full compensation to the insureds has a right to recoup an equitable proportion from the other insurers of the same risk.³⁶¹ If the insureds have not been fully compensated and want to make claims against the other insurers, then they are entitled to receive a full compensation. The principle of double insurance and contribution enables the total actual loss of the insureds to be shared in a fair way. Unlike the principle of subrogation, which governs the relationship between the insureds and the insurers, the principle of double insurance only regulates the relationship between insurers who assume the same risks against damage of or destruction to the same insured property.³⁶² This principle exists to support the indemnity principle.
- For the principle of abandonment,³⁶³ full compensation means that the insureds who have been fully compensated for their total loss are required to give up their interests in and control of the insured property to the insurers in case of a total loss.³⁶⁴ For example, where a cargo has been lost at sea and later is salvaged after a full compensation for the total loss has been paid to the insureds, the insurers are entitled

³⁵⁹ Although principle of double insurance is not involved in this thesis, it is helpful to mention it here in order to understand the meaning of “full compensation”.

³⁶⁰ *Bovis Construction Ltd v Commercial Union Assurance Co Plc* [2001] 1 Lloyd’s Rep. 416; *Austin v Zurich General Accident & Liability Ins Co* [1945] 1 K.B. 250; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p743

³⁶¹ Section 32 and 80 of the MIA 1906; *Godin v London Assurance Co* [1758] 1 Burr. 489; *Newby v Reed* [1763] 1 W.Bl. 416; *Rogers v Davis* [1777] 2 Park 601; *North British and Mercantile Ins Co v London, Liverpool and Globe Ins Co* [1877] 5 Ch.D. 569; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p743

³⁶² John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p761

³⁶³ Principle of abandonment is not involved in this thesis.

³⁶⁴ Section 61 to 63 of the MIA 1906; *Rankin v Potter* [1873] L.R.6. H.L. 83; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p691

to acquire the ownership of the salvaged cargo.³⁶⁵ After having been fully compensated for the total loss, the insureds cannot retain ownership of the salvaged cargo; otherwise, they would make a profit from the insurance contract.

The compensation depends on the premium rate for a specific type of risk

In principle, in terms of a specific type of risk, compensation under an insurance contract corresponds to the premium rate paid by the insureds.

Usually, the insurers have fixed a premium rate in advance, and the premiums are calculated based on the premium rate. Corresponding to each level of the premiums, the insurers are responsible for respectively reimbursing for a loss. If the insureds pay a higher insurance premium, they normally receive a greater compensation amount and vice versa. The highest premium is equivalent to the maximum responsibility of the insurer, and the insured property is fully insured. The insurers give compensation for the whole value of the insured property when the property is completely destroyed.

The lower premium is equal to the lower level of responsibility of the insurers, and the insured property is not fully insured. The insurers are only responsible for a part of the value of the insured property, and the insured agrees to be his own insurer for the rest. For example, in an insurance contract with an excess clause or an under-insurance clause, the sum insured is less than the actual value of the insured property. In terms of the relationship between the insured and the insurers, the purpose of the principle of indemnity is guaranteed, because the total value of the compensation amount paid by the insurers and the value of the uninsured loss is equal to the value of the actual loss the insureds have suffered.

The principle of indemnity is not perfect

In principle, full compensation, for purposes of the indemnity principle, is considered as exact financial compensation sufficient to restore the insureds to the same financial position after a loss as they enjoyed immediately before it. This is true in most cases. However, in some exceptional cases, due to difficulties in measuring the actual losses of the insureds, it is impracticable to place them in exactly the same position.

³⁶⁵ Section 63 of the MIA 1906; *Glen Line Ltd v Att Gen* [1930] 36 Com.Cas 1

However, it should be born in mind and be emphasized that the principle of indemnity is always there, and it is a “strong supporting frame” for the courts and judges when interpreting the other principles derived from the principle of indemnity and when calculating the amount of compensation for the insureds.³⁶⁶ It is submitted that Lord Sumner’s statement in *British and Foreign Ins. Co v Wilson Shipping Co*³⁶⁷ is completely true. He stated: “in practice contracts of insurance by no means always result in a complete indemnity, but indemnity is always the basis of the contract”. At this stage, it is worthwhile to examine the exceptions.

Exceptions

In some situations, the insurers cannot provide financial compensation to restore the insureds to exactly the same position immediately before the loss, but they should be in an attempt to get as near as possible to doing so. Those situations are exceptions to the indemnity principle. Valued policies³⁶⁸ and policies with a reinstatement clause³⁶⁹ are two of the exceptions:

Valued policies: A valued policy is a policy which specifies the agreed value of the insured property.³⁷⁰ The agreed value of the subject matter insured is, as between the insured and the insurer, conclusive of the insurable value of that property.³⁷¹ Valued policies are commonly used in marine insurance. In non-marine insurance, they are sometimes used to cover an article of particular value, for example, a piece of jewellery, work of art, or an antique.³⁷² Valued policies simplify the loss adjustment and the process of evaluating the value of the insured property. If there is a total loss, the insurers give full compensation for the specified sum to which the parties agreed in the insurance policy, without considering the actual value of the property and the actual loss the insureds sustained.³⁷³ Therefore, when making a

³⁶⁶ S Hodges, *Law of Marine Insurance*, (Cavendish Publishing Limited, London, 2005), p2; Lord Sumner stated in *British and Foreign Ins. Co v Wilson Shipping Co* [1921] 1 AC 188 (HL) at p 214: “in practice contracts of insurance by no means always result in a complete indemnity, but indemnity is always the basis of the contract”. In *Irving v Manning* [1847] 1 HLC 287 at p307, Mr Justice Patterson pointed out the fact that perfection may be difficult, if not impossible, to achieve. He stated: “A policy of assurance is not a perfect contract of indemnity”.

³⁶⁷ [1921] 1 AC 188 (HL) at p 214

³⁶⁸ Section 27(3) of the MIA 1906; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p137

³⁶⁹ Section 83 of the Fires Prevention (Metropolis) Act 1774

³⁷⁰ Section 27(2) of MIA 1906

³⁷¹ S 68(1) & s27(3) of MIA 1906

³⁷² J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p309

³⁷³ A. Lindblad, “How relevant is the principle of indemnity in property insurance” (1976) *Ins.L.J.* 271, p274

payment as compensation, the insurers may give an amount greater than or less than the actual losses.³⁷⁴

The calculation of compensation which is based on the agreed value of the insured property in an insurance contract shows a departure from a true indemnity but it is not contrary to the purposes of the indemnity principle. The drawback, which is that this departure may have an impact on the application of the indemnity principle, is offset by commercial convenience. For difficult cases, fixing the value of the property in advance in the policy may reduce or avoid disputes between the parties which may later arise. Furthermore, valued policies uphold the freedom of contract of the parties.³⁷⁵ At the stage of negotiations for a contract, the parties can foresee the difficulties in evaluating the insured property and measuring the loss. They have to negotiate and reach an agreement in order to avoid disputes on insured value when an insured event occurs. If the parties have agreed honestly and in good faith on a voluntary basis, the agreement should be supported by the courts.

Policies with a reinstatement clause: Reinstatement is also an exception to the indemnity principle. This method of providing indemnity is commonly used in construction insurance and fire insurance. It is applied where the insurers are bound to restore the insured property to its original condition or to rebuild a building which is damaged or destroyed by the insured risks.³⁷⁶ Where reinstatement has been effectively elected by the insurers, they are required to implement it regardless of the cost, even if the cost may be greater than the value of the insured property.³⁷⁷ The insurers are only able to limit their expenditure to the sum insured if there is an express term in the policy.

³⁷⁴ *Burnard v Rodocanachi* [1882] 7 App Cas 333, HL; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p309

³⁷⁵ H. Bennett, "Valued policies" in D. Rhidian Thomas (eds), *The Modern Law of Marine Insurance*, (LLP, 2002), p104

³⁷⁶ There are two types of reinstatement: contractual reinstatement and statutory reinstatement, see John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p673; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p312; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p469

³⁷⁷ *Alchorne v Favil* [1825] 4 L.J. 47; *Sutherland v Sun Fire Office* [1852] 14 D. 775; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p674-675; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p314

4. THE RELATIONSHIP BETWEEN THE INDEMNITY PRINCIPLE AND INSURABLE INTEREST

As required by the principle of indemnity, in order to make a valid claim against the insurers, the insured must prove that he has suffered an actual economic loss at the time of loss.³⁷⁸ To prove that he has suffered the loss, he must show that he has an interest in the subject matter of insurance.³⁷⁹

Consequently, the principle of insurable interest was set up and has been developed in insurance laws. The insurable interest principle is the “second door” to prevent the insured from making a profit from insurance contracts. To prove the losses, the insured must show an economic relationship with the insured property. If the insured does not have any relationship with the insured property, he does not suffer any loss when that property is lost or destroyed.³⁸⁰ As a result, the insured’s claim is rejected.

The insurable interest principle requires the insured to have a relationship with the insured property. The word “relationship” is very vague. Initially, the lawmakers supposed that, in order to constitute an insurable interest, this relationship must be a legally recognized relationship. In the opinion of lawmakers, economic relations that are not recognized by law are not sufficient to give the insureds an insurable interest in the insured property. This approach made the task of determining the existence of an insurable interest easier.³⁸¹

However, the explosive growth of economic activities nowadays has revealed disadvantages in this approach. The legal right approach narrowed down the situations in which the insureds may have an insurable interest in the insured property.³⁸² In several cases, the insured actually suffered an economic loss, but the economic relationship between the insured and the insured

³⁷⁸ D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p17

³⁷⁹ ALRC Discussion Paper 63, para. 7.3; UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p99; Issue Paper 4, p3

³⁸⁰ Section 5 of the MIA 1906; section 1 to 3 of the LAA 1774; article 3(9) of Vietnam’s Law on Insurance Business 2000; article 225 and 226 of Vietnam’s Maritime Code 2005; article 577 of Vietnam’s Civil Code 2005; *Lucena v Craufurd* [1806] 2 Bos. & P.N.R. 269

³⁸¹ For critical analyses on the legal right approach, see section 4 of Chapter 4: Insurable interest

³⁸² See section 4.1 of Chapter 4: Insurable interest

property was not recognized by law, and therefore the insurance contract is declared void and the insured's claim was denied.³⁸³

To overcome the above disadvantages, a broader approach, called the "factual expectation" approach, has been introduced.³⁸⁴ According to this approach, an insurable interest exists when an insured will suffer an economic detriment or loss if the property is damaged or destroyed, but receives some economic benefit or advantage by its continued existence.³⁸⁵ If a risk of loss is capable of being valued in monetary terms, it is sufficient to constitute an insurable interest.³⁸⁶ The factual expectation approach broadens the potential range of legitimate insurance, and it runs in parallel with the fundamental economic nature of insurance contracts, which is to indemnify the insureds for actual economic losses.³⁸⁷ However, this approach has a drawback, which is that, in some cases, it is difficult to calculate or quantify the economic detriment and loss of the insured.³⁸⁸

5. THE RELATIONSHIP BETWEEN THE INDEMNITY PRINCIPLE AND SUBROGATION

Subrogation can be described as when the insurers have paid a claim to the insureds, but a different party was liable for the cost of the loss, and the insurers are entitled to all the rights and remedies of the insureds in mitigation of the loss. A simple example of subrogation is the case where A has fully indemnified B for loss caused by C to B: under some form of agreement between A and B, A is entitled to exercise B's rights against C.

³⁸³ *Lucena v Craufurd* [1806] 2 Bos. & P.N.R. 269; *Macaura v Northern Assurance Co.* [1925] A.C. 619; *Fuerst Day Lawson v Orion Ins* [1980] 1 Lloyd's Rep 656; *Piper v Royal Exchange Assurance* [1932] 44 Lloyd's Rep 103

³⁸⁴ *Lucena v Craufurd* [1806] 2 Bos. & P.N.R. 269; *Wilson v Jones* [1867] L.R. 2 Ex 139; *The Moonacre* [1992] 2 Lloyd's Rep 501; *Petrofina (UK) Ltd v Magnaload Ltd* [1984] QB 127; *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587; EWCA Civ 885

³⁸⁵ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1172; R. Pinzur, "Insurable interest: a search for consistency", (1979) 46 Ins.Counsel J. 109,

³⁸⁶ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p34; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p142-143

³⁸⁷ D. Rhidian Thomas, "Insurable interest- accelerating the liberal spirit" in D. Rhidian Thomas, *Marine insurance: the law in transition*, (Informa, London, 2006), p35, see also Chapter 4: Insurable interest for more details.

³⁸⁸ For more details, see section 5.3 of Chapter 4: Insurable interest

To ensure that the insured shall not be compensated more than the actual loss

The subrogation principle has been developed to prevent the insured from making a profit at the expense of the insurer and the third party,³⁸⁹ i.e. to prevent a double indemnity or over-compensation of the insured. In the above example, the insured (B) cannot receive double compensation from both the insurer (A) and the party at fault (C) because that would conflict with the principle of indemnity. In accordance with the subrogation principle, A pays compensation to B and then has a subrogation right to bring an action against C to recover the payment he has made to B.

The subrogation principle is also designed to ensure that a wrongdoer who is legally responsible for the insured's loss will not be released from liability merely because the insured has been indemnified by the insurance policy. Therefore, after having paid the insureds, the insurers are allowed to pursue all the rights and remedies which the insureds may possess to recover the payment they have made.

The subrogation principle is derived from the principle of indemnity.³⁹⁰ It fulfils the objectives of the indemnity principle by ensuring that the insureds receive a full indemnity for a loss, but should not receive more than a full indemnity.³⁹¹ The possibility that the insured may recover more than an indemnity results from the fact that the insured who has recovered his entire loss from his insurer still has a right to take an action against the third party responsible for the loss to claim for compensation, or that the third party is under an contractual obligation to make a payment to the insured regardless of the destruction of or damage to the insured property.³⁹² This possibility is undermined by the principle of subrogation, and the aim of the principle of indemnity, that the insured cannot profit from an insured event, is preserved.

³⁸⁹ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p325-326; Z Jing, "The Confusion between Subrogation and Assignment in the Insurance Law of the People's Republic of China 1995-A Critical Analysis on Article 44 of the Insurance Law", (2002) J.B.L. 608, p609

³⁹⁰ Z Jing, "The Confusion between Subrogation and Assignment in the Insurance Law of the People's Republic of China 1995-A Critical Analysis on Article 44 of the Insurance Law", (2002) J.B.L. 608, p609; M Hemsworth, "Subrogation: the problem of competing claims to recovery monies", (1998) J.B.L 111, p111

³⁹¹ Brett LJ in *Castellain v Preston* (1883) 11 QBD 380, p386; similarly, the insurer may not recover, through the exercise of subrogation rights, more than the sum paid out under the contract. The insurer cannot also make profit from the insured's loss- case: *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330

³⁹² John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p689-690

To ensure that the insured receives compensation not less than his actual loss

Because the doctrine of subrogation is derived from the indemnity principle, the former must follow the nature of the latter. Accordingly, the insured must be fully indemnified, and is entitled to receive compensation not less than his actual loss. This is related to the distribution of the subrogation recovery from a third party at fault. There are several approaches to this distribution.

Let us take the above example in more detail: B buys insurance for only 70% of the value of the insured property. When a loss occurs, A gives compensation of 70% of the value to B, and then substitutes for B to bring an action against the third party at fault (C). If A can only recover 60% of the value from C, the distribution of the subrogation recovery between A and B will be made. This is a difficult matter, and will be discussed in details later.³⁹³ There are several possible approaches. The first is that A does not have to share the money with B because A has fulfilled his contractual obligation under the insurance contract.³⁹⁴ A is entitled to recoup in full the subrogation recovery from C. The second approach is that the recovery money from C is divided between A and B by the corresponding ratio 70/30.³⁹⁵ The third approach is that B is entitled to take 30% of the value in order to receive a full compensation for the actual loss, leaving the balance (30%) to A.³⁹⁶ However, when considering the subrogation principle in relation to the indemnity principle, it is submitted that the third approach is more appropriate because it ensures that the insured is fully compensated for his total loss.

³⁹³ See Chapter 5: Subrogation

³⁹⁴ *Napier v Hunter* [1993] A.C. 713; Article 577 of Vietnam's Civil Code 2005, Article 248(3) of Vietnam's Maritime Code 2005, Article 49 of Vietnam's Law on Insurance Business 2000; for critical analyses on those articles, see section 3.2 of Chapter 5: Subrogation

³⁹⁵ *The Commonwealth* [1907] P 216 CA; In *Goole & Hull Steam Towing Co Ltd v Ocean Marine Ins Co Ltd* (1928) 1 KB 589, at p594, it was alleged that the £2,500 recovered from the third party wrongdoer should be apportioned 4:1 between insurer and insured as regards the £5,000 loss – cost of repairing the vessel with an agreed value of £4,000; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p721

³⁹⁶ *Commercial Union Assurance Co v Lister* [1874] L.R. 9 Ch.App. 483; *Driscoll v Driscoll* [1918] 1 I.R. 152; *Kuwait Airways Corp v Kuwait Insurance SAK (No1)* [1996] Lloyd's Rep 664; *National Fire Insurance Company v McLaren* (1886) 12 O.R. 682; *Ledingham v. Ontario Hospital Services Commission* (1974) 46 D.L.R. (3d) 699; *Arthur Barnett Ltd v National Insurance Co of New Zealand* [1965] NZLR 874; *AFG Insurances Ltd v City of Brighton* [1972] 126 C.L.R. 655; *American Society Co v Westinghouse Electric Manufacturing Co* (1935) 296 U.S. 133; *Garrity v Rural Mutual Insurance Co* (1977) 253 N.W. 512; J Birds, "Contractual Subrogation in Insurance", (1979) J.B.L. 124, p128; A Tar, "Subrogation and the Ash Wednesday bushfire disaster", (1987-1988) 11 Adel. L. Rev. 232, p233; M Hemsworth, "Subrogation: the problem of competing claims to recovery monies", (1998) J.B.L 111, p114

The third approach is not universally accepted, but it is submitted that it is an appropriate interpretation of the subrogation principle which ensures consistency with the nature of the principle of indemnity and the nature of insurance. Adoption of the third approach avoids the case that the insureds are not fully compensated for their actual loss. Moreover, this approach is very suitable in the insurance markets where the insurers tend to take advantage of their strengths to deny compensation to the insureds.³⁹⁷

6. OTHER PRINCIPLES DERIVED FROM PRINCIPLE OF INDEMNITY

Besides the principle of insurable interest and the subrogation principle, there are several other principles which are the corollary of the indemnity principle, such as the principle of double insurance, the principle of abandonment, and the principle of reinstatement,... It is not the intention to discuss the double insurance principle and the abandonment principle in this work, but a brief explanation of them is helpful for understanding the nature of the indemnity principle.

6.1. Double insurance

The principle of double insurance and contribution applies only to those insurance contracts that are contracts of indemnity.³⁹⁸ This principle does not exist independently but exists to support the principle of indemnity, with the aim of preventing unjust enrichment.³⁹⁹ This principle applies in cases where more than one insurance policy covers the same insured property against the same risks. When an insured risk occurs, causing damage to the insured property, the insured is entitled to make claims against one or more insurers for his actual losses, provided that the amount of compensation is not greater than the actual loss.⁴⁰⁰ If the insured has been fully compensated from an insurer, he cannot get compensation from other insurers.⁴⁰¹ The insurer who has paid full compensation to the insured can recoup an

³⁹⁷ For more details, see section 3 and 5 of Chapter 5: Subrogation

³⁹⁸ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p351

³⁹⁹ Section 32 of the MIA 1906; article 44 of Vietnam's Law on Insurance Business 2000; article 234 of Vietnam's Maritime Code 2005; *Godin v London Assurance Co* [1758] 1 Burr. 489; *Newby v Reed* [1763] 1 W.Bl. 416; *Rogers v Davis* [1777] 2 Park 601; *North British and Mercantile Ins Co v London, Liverpool and Globe Ins Co* [1877] 5 Ch.D. 569; *Bovis Construction Ltd v Commercial Union Assurance Co Plc* [2001] 1 Lloyd's Rep. 416; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p526

⁴⁰⁰ *Godin v London Assurance Co* [1758] 1 Burr. 489; *Albion Insurance Co Ltd v Government Insurance Office of New South Wales* [1969] 121 C.L.R. 342

⁴⁰¹ *Newby v Reed* [1763] 1 W.Bl. 416; *Bousfield v Barnes* [1815] 4 Camp. 228; *Bruce v Jones* [1863] 1 H. & C. 769

equitable proportion from the other insurers who cover the same risk.⁴⁰² This principle regulates the relationship between the insurers, not between the insured and the insurers.⁴⁰³

6.2. Abandonment

The principle of abandonment is also derived from the principle of indemnity. This principle applies in the cases where the insured who has been fully compensated for the total loss of insured property is required to give up ownership of the insured property and transfer it to the insurers.⁴⁰⁴ The insurers become the new owner of what was left of the insured property, and acquire all proprietary rights to the insured property as well as are responsible for any obligations which may arise from it.⁴⁰⁵ If the insured, after having been fully compensated for the total loss, did not abandon the insured property, they would be obtaining unjust enrichment from insured events.

7. CONCLUSION

The principle of indemnity is a fundamental principle in indemnity insurance. The nature of this principle is clear and is recognised by all countries' insurance laws: that is, when the loss occurs, the insureds are entitled to be fully compensated for their actual loss, but should not receive compensation greater than their loss. On the other hand, the principle also protects the insureds by obtaining for them payment not less than their actual loss. The purposes of this principle are achieved through the application of other principles derived from the indemnity principle. Problems also arise from this. In practice, the application and interpretation of the principles derived from the principle of indemnity depart from the principle of indemnity. In the insurance laws of each country there are various ways of applying and interpreting those principles.

⁴⁰² Section 80 of the MIA 1906; *Newby v Reed* [1763] 1 W.Bl. 416; *Austin v Zurich General Accident & Liability Ins Co* [1945] 1 K.B. 250; *Bovis Construction Ltd v Commercial Union Assurance Co Plc* [2001] 1 Lloyd's Rep. 416

⁴⁰³ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p351

⁴⁰⁴ Section 61 to 63 of the MIA 1906; article 47 of Vietnam's Law on Insurance Business 2000; article 250 to 254 of Vietnam's Maritime Code 2005; *Randal v Cochran* [1748] 1 Ves.Sen. 98; *Houstman v Thornton* [1816] Holt N.P. 242; *Rankin v Potter* [1873] L.R.6. H.L. 83; *Kaltenbach v Mackenzie* [1878] 3 C.P.D. 467; *Provincial Ins Co of Canada v Leduc* [1874] L.R. 6 P.C.224; *Captain JA Cates Tug and Wharfage Co Ltd v Franklin Insurance* [1927] A.C. 689; *Panamanian Oriental Steamship Corporation v Wright* [1970] 2 Lloyd's Rep 365; *Dornoch Ltd v Westminster International BV (No2)* [2009] Lloyd's Rep. I.R. 573

⁴⁰⁵ Section 79(1) of the MIA 1906; *Barracrough v Brown* [1897] A.C. 615; *Dornoch Ltd v Westminster International BV (No2)* [2009] Lloyd's Rep. I.R. 573

The concept of full compensation, in its original sense, should be understood as the entitlement of the insureds to be restored to the same financial position enjoyed immediately before the loss, no more and no less. However, some rules of the principle of subrogation only reflect one side of the concept, i.e. full compensation only means “no more” than the insureds’ loss. There are a number of cases where the insureds may receive compensation less than the actual loss.⁴⁰⁶ As to the principle of insurable interest, some rules here also do not keep in line with the nature of the principle of indemnity. This principle acts as the “second door” to prevent the insureds from making a profit from an insured event, and the rigid interpretation of this principle may result in the insureds being denied compensation on unjustifiable grounds.

These ways of applying and interpreting principles derived from the principle of indemnity change the nature of insurance and the purposes of the indemnity principle. They only emphasize one side of the indemnity principle, that of preventing the insureds from making a profit from an insurance contract.

Another side of the indemnity principle should be looked at, which is to ensure that the insureds are fully compensated for their actual loss. If this side is ignored, the purposes of the indemnity principle are not fulfilled, and the principle of indemnity, for the purposes of property insurance as contracts of indemnity, does not fully reflect the nature of insurance.

This thesis would like to emphasize that the second purpose of the indemnity principle should be respected and guaranteed for two reasons: firstly, to ensure the implementation of the principle of equality between the parties to a contract in laws of contract in general and in property insurance contracts in particular; and secondly, to prevent insurers from taking advantage of their position and power in relation to the insureds in order to deny compensation or provide compensation less than the actual loss of the insureds. This direction is consistent with the development of regulations and guidelines to protect consumer rights in law and in judicial practice in many countries around the world, including Vietnam.

The main task of this thesis is to critically analyse the rules of the doctrine of insurable interest and the doctrine of subrogation which affect the nature of the principle of indemnity. As mentioned above, the rules only reflect one side of the nature of the indemnity principle, and overly emphasize one of its purposes that of preventing unjust enrichment, while

⁴⁰⁶ For more details, see Chapter 4: Insurable interest and Chapter 5: Subrogation

ignoring the other purpose, which is to allow the insureds to receive an indemnity not less than their actual loss. It is the intention of this thesis to critically discuss these rules and to suggest amendments to them in order to keep them in line with the nature of the indemnity principle, a fundamental principle of insurance law.

Rules of insurable interest are discussed in Chapter 4 and rules relating to subrogation are examined in Chapter 5.

CHAPTER 4: INSURABLE INTEREST

1. INTRODUCTION

The doctrine of insurable interest is an important principle in insurance contract law, which is closely related to the principle of indemnity for indemnity insurance.⁴⁰⁷ The doctrine reflects the fundamental nature of a contract of insurance as a contract of indemnity.⁴⁰⁸ Under the principle of indemnity, the insurer is under an obligation to indemnify the insured for the actual loss he has suffered, and the insured is entitled to be restored, subject to the terms and conditions of the policy, to the financial position enjoyed immediately before the loss. To confirm that the insured suffered an actual loss, he must show that he had an insurable interest in the subject matter insured.⁴⁰⁹ If he has no interest in the subject matter of insurance, he will not suffer a loss, and then the insurer's obligation cannot arise.⁴¹⁰

Insurable interest is a basic requirement of any contract of insurance.⁴¹¹ Generally, the insureds or policyholders must have a particular relationship with the subject matter of the insurance. They must gain benefits from the continued existence of the life insured or of the insured property, or suffer a disadvantage if the subject matter of insurance is lost or damaged.⁴¹² It means that an insured cannot take out a life insurance policy on a stranger or a property insurance policy on the property of a stranger. Insurance contracts lacking such "an insurable interest" may be considered as invalid or unenforceable on the grounds of illegality or public policy.⁴¹³ The reason for this is that such contracts are employed as an instrument of wager, or will give the policyholders an incentive to murder a stranger or destroy the insured property in order to obtain the insurance money.

The doctrine of insurable interest is adopted by insurance law in a number of countries. For instance, in Vietnam, matters relating to insurable interest are governed by article 3 of the

⁴⁰⁷ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p17

⁴⁰⁸ H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p67

⁴⁰⁹ ALRC's Discussion Paper 63, at 7.3

⁴¹⁰ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p17

⁴¹¹ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p39

⁴¹² Law Commission Consultation Paper No 201, "Insurance Contract Law: Post Contract Duties and other Issues", (2012), p99; D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p16

⁴¹³ S.4 of MIA 1906; s.1 of LAA 1774; article 22 of Vietnam's Law on Insurance Business 2000

Law on Insurance Business 2000⁴¹⁴ for non-marine insurance, and by article 225 and 226 of the Maritime Code 2005⁴¹⁵ for marine insurance. Under English law, the principle of insurable interest is governed by the Life Assurance Act 1774,⁴¹⁶ the Marine Insurance Act 1906,⁴¹⁷ the Gambling Act 2005,⁴¹⁸ and the common law. However, there are material differences between the Vietnamese, English and other countries' approaches to the requirement of insurable interest.

In English insurance laws, the basis for the requirement of insurable interest is complicated. In marine insurance, the insured must have a legal or equitable relation to or legal liability arising out of the subject matter of insurance.⁴¹⁹ The insured must possess an insurable interest at the time of loss.⁴²⁰ For non-marine indemnity insurance, the basis is uncertain.⁴²¹

⁴¹⁴ Article 3(9) of Law on Insurance Business 2000: "Insurable interest means a right of ownership, right of possession, right of use, or property right; maintenance rights and obligations to the person insured against." "Property rights" are defined in article 181 of Vietnam's Civil Code 2005 as "rights which can be valued in terms of money and may be transferred in civil transactions, including intellectual property rights". "Maintenance rights and obligations to the person insured against" mean "rights and obligations of parents and children regarding provision of food and maintenance."

⁴¹⁵ Article 225 of Maritime Code 2005: "*Subject-matter of marine insurance*: A subject-matter of marine insurance may be any pecuniary interest related to maritime adventures, which can be valued in terms of money, including seagoing vessel, seagoing vessel in course of building, cargo, freight, passage money for the carriage of passengers, charter-hire, hire and purchase money, expected profit on cargo, commission, general average costs, obligations arising under civil liability and sums of money secured by vessel, cargo or freight."

Article 226 of Maritime Code 2005: "*Identification of insurable interests*: (1) A person with an insurable interest is a person who is interested in a subject-matter of insurance in a sea voyage. (2) A person is interested in a sea voyage when he/she has grounds to prove that he/she has any relation to the voyage or to any subject-matter of insurance at risk in it, in consequence of which such person may benefit by the safety and due arrival of the subject of insurance, or may not benefit by its loss or by damage to it or by the detention of it, or may incur liability in respect of it. (3) The assured must have interest in the subject of insurance at the time of occurrence of the loss though the assured need not be interested in the subject of insurance when the insurance is effected. When the subject of insurance is insured under the "lost or not lost" condition, the assured may recover although the assured may not have acquired that interest until after the loss occurred, unless the assured was aware of the loss and the insurer was not.

Where the assured has no interest in the subject of insurance at the time of occurrence of the loss, he cannot acquire interest by any act or selection after he is aware of the loss. (4) Where the buyer of goods has insured them, the buyer shall have an insurable interest, even though the buyer might have rejected the goods or have treated them as at the seller's risk, by reason of the latter's delay in making delivery or otherwise."

⁴¹⁶ Section 1, 2, 3 of LAA 1774

⁴¹⁷ Section 4, 5, 6 of MIA 1906

⁴¹⁸ Section 334 of GA 2005

⁴¹⁹ Section 5(2) of MIA 1906

⁴²⁰ Section 6(1) of MIA 1906

⁴²¹ For policies on non-marine goods, it is asserted that there is no statutory requirement of insurable interest {see John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p23; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p40}; Merkin agreed that there is no statutory requirement at the time of inception, but the insured must possess an insurable interest at the time of loss due to the principle of indemnity {see R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p142}. For policies on land, building, and liability, the insured must have an insurable interest at the time of inception, due to LAA 1774, and at the time of loss as well, due to the principle of indemnity. Those policies used to be regarded as covered by the LAA 1774, but there is a modern view that the LAA 1774 does not apply to such policies. {see John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell,

Similar to English laws, in marine insurance, the insured must have a legal relation to the subject matter of insurance, and he must possess an insurable interest at the time of loss under Vietnamese insurance laws.⁴²² In non-marine indemnity insurance, the legal relation between the insured and the subject matter of insurance is also required.⁴²³ There is no clear provision in law on the time when an insurable interest must be attached. However, in practice, the insured must show an insurable interest at the time of inception and at the time of loss as well, because article 23(1) of the Vietnamese Law on Insurance Business 2000 stipulates that an insurance contract shall terminate if the purchaser of insurance no longer has an insurable interest.⁴²⁴ A lapse of insurable interest at any stage during the life of the policy will terminate the insurance contract.⁴²⁵

In American, Canadian and Australian laws, the legal or equitable relation is required at the time of loss in marine insurance.⁴²⁶ For non-marine insurance, there is no requirement of insurable interest under Australian law.⁴²⁷ It is required that, under American and Canadian laws, the insured should have a factual expectation of either an economic benefit from the continued existence of the insured subject matter or an economic loss on its destruction at the time of loss.⁴²⁸

However, as Professor Bennett comments, despite its long development, universal recognition of its need, and attendant extensive consideration, it is difficult to give a precise

London, 2012), p23-24; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p40; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p142; *Dalby v India & London Life Ass. Co* [1854] 15 C.B. 365; *Turnbull & Co v Scottish Provident Institution* [1896] 34 SLR 146; *Petrofina (UK) Ltd v Magnaload Ltd* [1984] QB 127; *Siu Yin Kwan and another v Eastern Insurance Co Ltd* [1994] 1 All ER 213; *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587 }

⁴²² Article 226 of Vietnam's Maritime Code 2005- see note 7

⁴²³ Article 3(9) of Vietnam's Law on Insurance Business 2000- see note 6

⁴²⁴ Article 23 of the Vietnam's Law on Insurance Business 2000: "... an insurance contract shall also terminate in the following circumstances: (1). The purchaser of insurance no longer has an insurable interest;..." If the insurance contract terminates, the parties do not have to continue to perform their obligations. A party which has already performed its obligation may demand the other party to make payment, see Article 24 of the Vietnam's Law on Insurance Business: "*Legal consequences of termination of insurance contracts*: (1). In the case of termination of an insurance contract pursuant to the provisions in article 23.1 of this Law, an insurer must refund to the purchaser of insurance that part of the paid insurance premium which corresponds to the remaining duration of the insurance contract, after deducting legitimate expenses relating to the insurance contract;..."

⁴²⁵ See section 3.2 of this Chapter

⁴²⁶ Section 7 of Canadian MIA 1993; section 11 of Australian MIA 1909; section 6(2) of New Zealand's MIA 1908

⁴²⁷ Section 16 and 17 of Australian Insurance Contracts Act 1984;

⁴²⁸ Section 3401 of New York State Insurance Act 2006, *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208

and comprehensive definition of insurable interest;⁴²⁹ and whether an insured possesses an insurable interest remains, on occasion, a difficult and controversial question.⁴³⁰

In addition, Professor Merkin comments that the doctrine of insurable interest creates a confusing and illogical mess.⁴³¹ In judicial practices, courts are sometimes faced with several difficulties in determining the existence of an insurable interest.⁴³² On similar facts, different courts have different opinions, and judges do not agree with each other. Those differences produce confusion over application of the doctrine to both insurers and insureds, occasionally preventing them from doing legitimate business, and causing inefficiency in the insurance market.⁴³³

The doctrine also creates uncertainty over the validity of an insurance policy which can be exploited by insurers. Some insurers may cheat their insureds by using the doctrine. When the insureds take out insurance, the insurers just issue the policies and collect the premiums, regardless whether or not there is an insurable interest. Yet, when the insured perils occur, the insurers may argue that the policy in question is invalid for lack of insurable interest, and consequently they may be relieved of their obligation to pay under the policy. The insureds finally find the policy in their hands worthless. If the insured perils never happen, the insurers can keep the premiums for themselves.

It may be argued that the insurers who act in “bad faith” should be liable to the insureds as damages. However, the doctrinal uncertainty creates the legal gap for the insurers to maintain the appearance of “good faith” for policies that are not clearly supported by an insurable interest when issued.⁴³⁴ This is a technical defence for the insurers.⁴³⁵ It is unfair to the

⁴²⁹ Law Commission Consultation Paper No 201, “Insurance Contract Law: Post Contract Duties and other Issues”, (2012), p123

⁴³⁰ H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p67

⁴³¹ R. Merkin, “Reforming insurance law: is there a case for reverse transportation?”, A report for the English and Scottish Law Commissions on the Australian experience of insurance law reform (2007) available at http://www.lawcom.gov.uk/docs/merkin_report.pdf >

⁴³² *Lucena v Craufurd* [1806] 2 Bas. & P.N.R. 269; *Macaura v Northern Assurance Co.* [1925] A.C. 619; *The Moonacre* [1992] 2 Lloyd’s Rep 501; *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587; *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208; *Fidelity Phoenix and Globe Fire Ins. Co. v Raper* [1942] 6 So. 2d 513; *Liverpool and London and Globe v Bolling* [1940] 10 S.E. 2d 578; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p67; J. Stockton, “An analysis of insurable interest under article two of the Uniform Commercial Code”, (1963-1964) 17 Vand. L. Rev 815, p815

⁴³³ J Hjalmarsson, “Legal or equitable relationship to insured subject-matter as a determinant of insurable interest- the approaches of English and Swedish law”, (2008) L.M.C.L.Q 97, p97

⁴³⁴ J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p477

insureds because the insurers have accepted the premiums from the insureds at the time of inception, and then are allowed to escape their promised payment obligations, irrespective of their faults. The uncertainty about application of the doctrine actually puts the insurers into the position of “gaining something or losing nothing”, when they provide policies which are not clearly supported by an insurable interest.

In recent years, some countries have abolished or intended to abolish the requirement of insurable interest in indemnity insurance. For example, the Australian insurance laws have eliminated the requirement in non-marine indemnity insurance. In marine insurance, the question of whether the requirement is necessary has been put up for discussion by the Australian Law Reform Commission.⁴³⁶ In the UK, it has been argued that the Gambling Act 2005 has eliminated the requirement of insurable interest in non-marine insurance.⁴³⁷

The objectives of this chapter are to critically analyse the doctrine of insurable interest by comparing the Vietnamese approach with the English approach and other countries’ approach in order to find out the problems in law and practice in Vietnam regarding the principle of insurable interest, and to find possible solutions to overcome those problems.

In addition, the chapter attempts to explore whether the requirement is necessary in indemnity insurance, and to discuss whether the principle of indemnity is an effective barrier to prevent the insured from taking advantage of insurance policies or from gambling in the guise of insurance, and whether the indemnity principle may reduce the insured’s incentive to destroy the insured property, and whether freedom of contract may help the insurers to reduce intolerable moral hazard and gambling in the guise of insurance. Finally, suggestions are made on how to reform the provisions relating to the principle of insurable interest under Vietnamese insurance laws.

⁴³⁵ *Stock v Inglis* [1884] 12 QBD 564, p571; D. Galbraith “An Unmeritorious Defence – The Requirement of Insurable Interest in the Law of Marine Insurance and Related Matters” (1992) 5(3) *Ins LJ* 177, p177; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p137

⁴³⁶ See ALRC’s Discussion Paper 63: Review of the Marine Insurance Act 1909; ALRC’s Report 91

⁴³⁷ Issue Paper 4; Law Commission Consultation Paper No 201; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p22-23; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p141-142; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p140-142; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p40; C. Nicoll, “Insurable interest: as intended?” (2008) *J.B.L* 432, p432; R. Merkin, “Insurable interest, the repeal of the prohibition on gambling”, (2005) 17 *ILM* 4, p5; J. Davey, “The reform of gambling and the future of insurance law”, (2004) *Legal Study* 507

The structure of this chapter, therefore, is outlined as follows: firstly, to discuss the nature of insurable interest; secondly, to critically examine the current Vietnamese and English laws on insurable interest; thirdly, to critically analyse problems of the “strict proprietary test” approach and the “factual expectation test” approach; fourthly, to reveal complications arising from the application of either the “legal right” approach or the “factual expectation test” approach; fifthly, to discuss whether the insurable interest doctrine is necessary in indemnity insurance; and finally, to make some suggestions and recommendations for the amendment of Vietnamese insurance laws.

2. THE NATURE OF THE INSURABLE INTEREST PRINCIPLE

The doctrine of insurable interest has been developed to provide safeguards against wagering and moral hazard. In order to understand the reasons underlying the requirement of insurable interest, the history and the nature of insurable interest will be examined.

2.1. History of insurable interest:

Historically, under English common law, insurance contracts in the seventeenth century were enforceable even if they lacked an insurable interest.⁴³⁸ Policies were commonly issued “interest or no interest” or in similar form. This avoided the need for the policyholder to declare his interest and the underwriter normally received a higher premium. This state of affairs continued to exist until 1745, when the British Parliament passed a statute outlawing wagering contracts on marine insurance.⁴³⁹ There were concerns that British vessels and cargoes were deliberately harmed by policyholders, who were unconnected to the voyage, but were able to make a claim under their policy.⁴⁴⁰ Marine policies made without interest or which provided that the policy itself was to be conclusive proof of interest (“ppi” policies) or was made “interest or no interest” were rendered void. A subsequent Act in 1774 (Life Assurance Act 1774) extended this prohibition from marine insurance to life insurance and

⁴³⁸ *Andrews v Herne* [1662] 1 Lev. 33, *Danvers v Thistlewaite* [1669] 1 Lev. 44, *Firebrase v Brett* [1688] 1 Vern 469; *Dalby v India & London Life Ass. Co* [1854] 15 C.B. 365

⁴³⁹ Marine Insurance Act 1745, 19 Geo 2, c37; However, the 1745 Act did not invalidate wager policies completely. Wager policies were expressly permitted for British-financed privateers that would prey solely on enemy vessels and for cargo from any European or American port under Spanish or Portuguese control; see *Andree v Fletcher* [1787] 2 TR 161

⁴⁴⁰ See the Preamble to the MIA 1745

other insurance.⁴⁴¹ Later, the Gaming Act 1845 rendered all contracts by way of gaming or wagering void.⁴⁴²

In 1806, there was a discussion on the requirement of insurable interest in a leading case of *Lucena v Craufurd*.⁴⁴³ Two English judges famously disputed whether the insurable interest must involve a formal property right (the “legal right”)⁴⁴⁴ or whether the interest is required to only involve a factual expectation of economic gain (the “factual expectation test”).⁴⁴⁵ Subsequently, the MIA 1906 adopted the “legal right” approach of Lord Eldon, which is sometime called the “narrow approach”.⁴⁴⁶ Section 5 of the MIA 1906 requires that the insured must have “legal or equitable” relation to the subject-matter insured.

However, since the late twentieth-century, the factual expectation approach, which is sometimes called the “broader approach”, has been adopted in other common law jurisdictions, such as: Canada⁴⁴⁷ and America.⁴⁴⁸ In addition, under English law, some decisions indicate that the “traditional narrow approach” does not match current commercial practices.⁴⁴⁹

In 2005, the UK Gambling Act 2005 was promulgated. The impact of the GA 2005 on the requirement of insurable interest is still unclear.⁴⁵⁰ It appears that most contracts of indemnity

⁴⁴¹ See the Preamble to the LAA 1774: “...Whereas it hath been found by experience that the making insurances on lives or **other events** wherein the assured shall have no interest hath introduced a mischievous kind of gaming...”

⁴⁴² S.18 of the Gaming Act 1845: “all contracts or agreements, whether by parole or in writing, by way of gaming or wagering, shall be null and void”. However, the Gaming Act 1845 was repealed by the Gaming Act 2005

⁴⁴³ [1806] 2 Bas. & P.N.R. 269

⁴⁴⁴ Per Lord Eldon

⁴⁴⁵ Per Lawrence J.

⁴⁴⁶ This statute invalidates all insurance contracts lacking insurable interest, without exception. Section 4 of the MIA 1906 provides that: “every contract of marine insurance by way of gaming or wagering is void.”

⁴⁴⁷ *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208

⁴⁴⁸ *Liverpool and London and Globe v Bolling* [1940] 10 S.E. 2d 578; *Fidelity Phoenix and Globe Fire Ins. Co. v Raper* [1942] 6 So. 2d 513

⁴⁴⁹ *The Moonacre* [1992] 2 Lloyd’s Rep 501; *National Oilwell [UK] Ltd v Davy Offshore Ltd* [1993] 2 Lloyd’s Rep 582; *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587

⁴⁵⁰ In Law Commission Consultation Paper No 201, “Insurance Contract Law: Post Contract Duties and other Issues”, (2012), p109-110, it is argued that the GA 2005 has no effect on insurance contracts; and in John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p22-23, it is contended that whether s.335 of the GA 2005 applies to non-indemnity insurance is of little practical importance because they will in any event be unenforceable at common law if a valid insurable interest cannot be demonstrated at the time of loss, regardless of whether a lack of interest has the effect of making them gambling contracts. However, some academic writers asserted that the GA 2005 has abolished the requirement of insurable interest in non-marine insurance. (see M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p141-142; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p140-142; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p40; C. Nicoll, “Insurable interest: as intended?”

insurance without insurable interest are valid under English law,⁴⁵¹ because section 335(1) of GA 2005 sets out the general rule that a contract relating to gambling is enforceable.⁴⁵² It seems that, in non-marine indemnity insurance, the insureds no longer need to show an insurable interest in the subject matter of insurance, but the GA 2005 still has no impact on marine insurance. It means that the insureds still have to show an insurable interest in marine insurance. This change may have been more by accident than design.⁴⁵³

2.2. The nature of insurable interest:

The nature of insurable interest demonstrates the situation that someone taking out insurance must stand to gain a benefit from the continued existence of the subject matter of insurance or suffer a disadvantage when it is damaged or destroyed.⁴⁵⁴ This reflects the nature of the indemnity insurance contract which aims to give an economic indemnity to the policyholder who has suffered loss caused by the insured event.

In indemnity insurance, the principle of indemnity requires that, in order to make a valid claim against the insurer, the policyholder must prove that he has suffered an actual economic loss at the time of loss. To prove it, the policyholder must show his economic relationship to the insured property. If he has no particular relationship with the insured property, he will not suffer any economic loss, and he therefore cannot recover anything from the insurer.

Under English law, the insurable interest must be a legal or equitable interest. If the relationship between the policyholder and the insured property is not recognised by law, the insurance contract will be considered as invalid. This is a statutory requirement for a contract of insurance to be valid. The parties to an insurance contract cannot waive this requirement in their contract.⁴⁵⁵

(2008) J.B.L 432, p432; R. Merkin, “Insurable interest, the repeal of the prohibition on gambling”, (2005) 17 ILM 4, p5; J. Davey, “The reform of gambling and the future of insurance law”, (2004) Legal Study 507

⁴⁵¹ Issue Paper 4, p iii

⁴⁵² S.335 of the GA 2005: “(1) The fact that a contract relates to gambling shall not prevent its enforcement. (2) Subsection (1) is without prejudice to any rule of law preventing the enforcement of a contract on the grounds of unlawfulness (other than a rule relating specifically to gambling).”

⁴⁵³ Issue Paper 4, p iii

⁴⁵⁴ Law Commission Consultation Paper No 201, “Insurance Contract Law: Post Contract Duties and other Issues”, (2012), p99

⁴⁵⁵ If there is no statutory requirement of insurable interest, the parties to an insurance contract can define the economic relationship between the insured and the insured property or waive the requirement of insurable interest in their contract. Freedom of contract will prevail. Such agreements between the parties cannot be voided by laws

It should be submitted that insurable interest stipulated by statute is inconsistent with the nature of the contract of indemnity insurance.⁴⁵⁶ The insurable interest required by the nature of indemnity insurance contract is merely an economic relationship.

The different meaning of insurable interest may cause different consequences for lack of insurable interest. According to the nature of indemnity insurance contract, if the insured has no interest in the insured property, he cannot prove his actual loss, and then cannot recover from his insurers. However, by law, if the insured has no insurable interest, the insurance contract will be declared as void or illegal.

The nature of insurable interest was discussed at length in the classical leading case of *Lucena v. Craufurd*.⁴⁵⁷ Examining the views of the judges in this case is helpful for better understanding of the nature of insurable interest.

The facts of the case in brief were that Commissioners of Admiralty were empowered by King to take charge of ships captured from the Dutch. They had not taken possession of four enemy Dutch ships which had been captured but nonetheless insured them for their homebound voyage from St Helena to England. The ships were lost due to perils of the sea and the Commissioners made a claim for this loss under their policy. The House of Lords was required to decide if the Commissioners had sufficient insurable interest to support such a policy. It should be noted that although the Commissioners had not taken possession of the ships in question, there was no doubt that these enemy ships would be condemned by the High Court of Admiralty as prizes of war, and thereupon the Commissioners would be given possession of these ships for sale and management, as was their right under statute. Two main different views in this case, which reflect the nature of insurable interest, were given by two judges, namely: the “factual expectation test” and the “legal right”.

The “factual expectation test” was put forward by Lawrence J.⁴⁵⁸ “A man is interested in a thing to whom advantage may arise or prejudice happen from the circumstances which may attend it; and whom it importeth that its condition as to safety or other quality should continue. Interest does not necessarily imply a right to the whole or a part of the thing, nor necessarily and exclusively that which may be the subject of privation, but the having some relation to, or concern in, the subject of the insurance; which relation or concern, by the

⁴⁵⁶ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p9

⁴⁵⁷ (1806) 2 B. & P.N.R. 269.

⁴⁵⁸ *Ibid*, at 302-303.

happening of the perils insured against, may be so affected as to produce a damage, detriment or prejudice to the person insuring. And where a man is so circumstanced with respect to advantage or benefit but for those risks or dangers, he may be said to be interested in the safety of the thing. To be interested in the preservation of a thing is to be so circumstanced with respect to it as to have the benefit from its existence, prejudice from its destruction. The property of a thing and the interest derivable from it may be very different. Of the first the price is generally the measure; but by interest in a thing, every benefit and advantage arising out of or depending on such a thing may be considered as being comprehended.”

According to Lawrence J’s point of view, a mere expectancy or moral certainty⁴⁵⁹ of loss would suffice to find an insurable interest in the subject matter of insurance.⁴⁶⁰ Lawrence J’s formulation is wide. He emphasized that the nature of an insurance contract as one of indemnity did not require the concept of insurable interest to be limited to “interest which arises out of property”.⁴⁶¹ He carefully distinguished interest from a right of ownership, and suggested that the proper test is that of possible prejudice following loss of the insured subject matter.⁴⁶² In accordance with Lawrence J’s approach, “an indirect loss”, such as loss of entitlement or opportunity, would be sufficient to constitute an insurable interest.⁴⁶³ This approach emphasizes economic or pecuniary interest. Where a risk of loss is capable of being valued in monetary terms, it will suffice to find an insurable interest. The difficulties of making such a valuation will not deny the policyholder an insurable interest.⁴⁶⁴ This approach runs in parallel with the fundamental economic nature of insurance contracts which is to indemnify an insured for direct and indirect economic or pecuniary losses.⁴⁶⁵

On the other hand, Lord Eldon took a narrower view of what constitutes insurable interest (legal right approach), he stated as follows:⁴⁶⁶ “In order to distinguish that intermediate thing between a strict right, or a right derived under a contract, and a mere expectation or hope, which has been termed an insurable interest, it has been said in many cases to be that which

⁴⁵⁹ “Moral certainty” can probably be defined as a “high degree of certainty”, see D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p36

⁴⁶⁰ Lee Kiat Seng, “Insurable interest in Singapore”, (1997) *Singapore Journal of Legal Studies* 499, p502

⁴⁶¹ H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p75

⁴⁶² R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p144. This dictum was cited by Kerr L.J. in *Mark Rowlands Ltd v Berni Inns Ltd*, even though it does not represent prevailing English law.

⁴⁶³ D. Rhidian Thomas, “Insurable interest- accelerating the liberal spirit” in D. Rhidian Thomas, *Marine insurance: the law in transition*, (Informa, London, 2006), p16

⁴⁶⁴ For example, it is difficult to value loss of future profit or loss of opportunity to buy a property

⁴⁶⁵ D. Rhidian Thomas, “Insurable interest- accelerating the liberal spirit” in D. Rhidian Thomas, *Marine insurance: the law in transition*, (Informa, London, 2006), p35

⁴⁶⁶ *Ibid*, at 321.

amounts to a moral certainty. I have in vain endeavoured however to find a fit definition of that which is between a certainty and an expectation; nor am I able to point out what is an interest unless it be a right in the property, or a right derivable out of some contract about the property, which in either case may be lost upon some contingency affecting the possession or enjoyment of the party.... As to expectation of profits and some other species of interest which has been insured in later times, there is nothing to show that they were considered as insurable.”

Lord Eldon’s approach rests upon the insured’s ownership of or right to possess the insured subject matter. In order to find an insurable interest, the insured must have a legal or equitable right or legal liability arising from the insured property. An expectant or future right or obligation is insufficient to constitute an insurable interest. For example, a buyer of goods, who has yet to take delivery and when title and risk of loss of the goods remain with the seller, has no insurable interest.⁴⁶⁷ Under Lord Eldon’s approach, it is not sufficient that the insured has suffered an economic loss, whether indirect or direct; the loss must have been caused by the impact of insured perils on the insured’s legal or equitable right or legal liability arising from the insured property.⁴⁶⁸

This approach has been criticized for being too technical and restrictive.⁴⁶⁹ It excludes insurance from areas of legitimate concern to the commercial community.⁴⁷⁰ However, Lord Eldon’s narrow view (the “legal right”) has been accepted in England as a law.

Based on the classical decision of *Lucena*, the narrower approach of Lord Eldon has been adopted in the MIA 1906. Section 5(2) of the MIA 1906 defines insurable interest in terms of: “In particular a person is interested in a marine adventure where he stands in any **legal or equitable** relation to the adventure or to any insurable property at risk therein, in consequence of which he may benefit by the safety or due arrival of insurable property, or may be prejudiced by its loss, or damage thereto, or by the detention thereof, or may incur liability in respect thereof.”

⁴⁶⁷ *Anderson v Morice* [1875] L.R. 10 C.P. 609

⁴⁶⁸ D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p33

⁴⁶⁹ D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p34

⁴⁷⁰ Doctrine of “pervasive interest” has been developed to support commercial convenience in the context of large commercial transactions, for example: offshore or construction projects.

It can be seen that the MIA 1906 does not attempt to formulate any exhaustive definition of insurable interest even in the limited field of marine insurance.⁴⁷¹ In this definition, the word “in particular” is used, it means that policyholders who come within the definition have an insurable interest; it does not state that those outside the list fail to have an insurable interest.⁴⁷² This definition merely states in condensed form the principles laid down in the *Lucena*.⁴⁷³ The most important words in this definition are “legal or equitable relation”, a clear statement on legal right approach.

The decision of the marine insurance cases and the definition for insurable interest in marine insurance also applied to non-marine insurance.⁴⁷⁴ The leading non-marine insurance case, which represents the narrow view of insurable interest, is *Macaura v. Northern Assurance Co.*⁴⁷⁵ The judgment on the *Macaura* has received several criticisms for its strictness because it required the insured to have a legally recognised interest in the property, in order to show insurable interest.⁴⁷⁶ In some later non-marine insurance cases, judges resisted adopting the strict narrow view of insurable interest.⁴⁷⁷

Some English academic writers have attempted to give a proper definition of the concept: “insurable interest may be described loosely as the assured's pecuniary interest in the subject-matter of the insurance arising from a relationship with it recognised in law.”⁴⁷⁸ A working definition applicable to all risks under the LAA 1774 has been given in *MacGillivray on Insurance Law*: “where the assured is so situated that the happening of the event on which the insurance money is to become payable would, as a proximate cause, involve the assured in the loss or diminution of any right recognised by law or in any legal liability there is an insurable interest in the happening of that event to the extent of the possible loss or liability.”⁴⁷⁹ This definition includes the definition under section 5(2) of the MIA 1906 plus

⁴⁷¹ *The Moonacre* [1992] 2 Lloyd's Rep 501; *O'Kane v Jones [The Martin P]* [2004] 1 Lloyd's Rep 389, [2003] EWHC 2158; D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p24; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p77

⁴⁷² UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p107

⁴⁷³ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p27

⁴⁷⁴ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p27

⁴⁷⁵ [1925] A.C. 619.

⁴⁷⁶ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p50

⁴⁷⁷ *Sharp v. Sphere Drake Insurance, The Moonacre* [1992] 2 Lloyd's Rep 501; *National Oilwell (UK) v. Davy Offshore* [1993] 2 Lloyd's Rep 582; *Glengate-KG Properties Ltd v. Norwich Union Fire Insurance Society* [1996] 2 All E.R. 487.

⁴⁷⁸ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p9

⁴⁷⁹ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p27

any legal liability arising from destruction of, or damage to, the insured property.⁴⁸⁰ It is submitted that this definition is still not comprehensive, and it may prevent insureds from recovering their actual economic loss in some circumstances, which is inconsistent with the principle of indemnity.

Vietnamese insurance laws adopt the narrow English approach. For non-marine insurance, the definition of the concept is given in article 3(9) of Vietnam's Law on Insurance Business 2000, which provides that: "Insurable interest means a right of ownership, right of possession, right of use, or property right;⁴⁸¹ maintenance rights and obligations to the person insured against."⁴⁸² Article 3(9) indicates that the insurable interest must be legally recognised, because all the rights which are listed in the article are legal rights.

In marine insurance, Article 226(2) of Maritime Code 2005 stipulates that: "A person is interested in a sea voyage when he/she is able to prove that he/she has any relation to the voyage or to any subject-matter of insurance at risk in it, in consequence of which such person may benefit by the safety and due arrival of the subject of insurance, or may not benefit by its loss or by damage to it or by the detention of it, or may incur liability in respect of it." This provision is an identical copy of section 5(2) of the MIA 1906 under English laws. Article 226 does not use the legal terms of "legal or equitable relation" because there is no equity in the Vietnamese legal system. However, the meaning of article 226 is the same as that of section 5(2) of the MIA 1906.

Moreover, Article 225 of Vietnam's Maritime Code 2005 defines a subject-matter of marine insurance as "any pecuniary interest related to maritime adventures, which can be valued in terms of money, including seagoing vessel, seagoing vessel in course of building, cargo, freight, passage money for the carriage of passengers, charter-hire, hire and purchase money, expected profit on cargo, commission, general average costs, obligations arising under civil liability and sums of money secured by vessel, cargo or freight." Article 225 does not define the concept of "legal relation", instead merely listing types of subject matter which are recognised by Vietnamese law. This list narrows the possibility of giving policyholders an insurable interest. The reason is that listing types of subject matter of insurance never

⁴⁸⁰ *Glengate-KG Properties v Norwich Union Fire Ins Society* [1996] 1 Lloyd's Rep 614, p624; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p57

⁴⁸¹ "Property rights" are defined in article 181 of Vietnam's Civil Code 2005 as "rights which can be valued in terms of money and may be transferred in civil transactions, including intellectual property rights".

⁴⁸² "Maintenance rights and obligations to the person insured against" means "rights and obligations of parents and children regarding provision of food and maintenance."

embraces all of the economic relation between insureds and insured property which may arise out of commercial practices.

Australian law has radically dispensed with English law in respect of the nature of the insurable interest required in contracts of non-marine indemnity insurance. The Insurance Contract Act 1984 (ICA) abolished the requirement of insurable interest in non-marine indemnity insurance. Section 16 of the ICA 1984 states that a “contract of general insurance is not void by reason only that the insured did not have, at the time when the contract was entered into, an interest in the subject matter of the contract.”; and section 17 of the ICA provides that where the insured has suffered a pecuniary or economic loss, the insurer is not relieved of liability by reason only that, at the time of loss, the insured did not have an interest in law or in equity in the property.

The ICA 1984 uses an economic test to determine whether the insured has a sufficient interest to claim under the policy.⁴⁸³ If a loss has been suffered, the lack of interest, either at the time of inception or at the time of loss, should not prevent the insured from recovery. Contracts of indemnity insurance should be excluded from the statutory requirement of insurable interest because the principle of indemnity indeed sets up a barrier that potential recovery of the insured is limited to his actual loss, if he has not suffered any loss, he cannot recover under his policy.⁴⁸⁴

To sum up, the nature of insurable interest reflects the nature of insurance contract, an indemnity contract. In order to prove his actual loss, the insured must show some kind of relationship to the insured property. However, the question of what kind of relationship is sufficient to show his interest in the property is difficult to answer. It may be required that this relationship must be recognised by laws or that it is only an economic one to constitute an insurable interest. The debate on this question has not come to an end yet, although the concept of insurable interest was introduced more than 200 years ago.

2.3. The purposes of the principle of insurable interest

There is public concern that allowing a policyholder who has no interest in the insured property or has no interest other than the policy itself will lead to two dangers: gambling in

⁴⁸³ ALRC Report 91, para 11.26; S. Derrington, “Australia: Perspective and permutations on the law of marine insurance” in D. Rhidian Thomas (editor), *The modern law of marine insurance*, (LLP, 2002), p370

⁴⁸⁴ ALRC 20, para 117

the guise of insurance, and an incentive to damage or destroy the insured property (moral hazard). The purposes underlying the requirement of insurable interest are to avoid or reduce mischievous kinds of gaming and moral hazard.⁴⁸⁵

2.3.1. Preventing wagering in the guise of insurance:

One of the original purposes behind the principle of insurable interest is the social policy against wagering.⁴⁸⁶ If the insured has no interest in the subject matter, he would suffer no loss. The insurance contract, therefore, would be a pure gamble.⁴⁸⁷ On the social level, wagering activities are essentially unproductive because when one gambler gains, another loses.⁴⁸⁸ Wagering may cause several problems for the wagerer's family, especially for the person who is addicted to gambling. It may lead to corruption in public affairs,⁴⁸⁹ physical violence, immorality,⁴⁹⁰ criminal offences, and may adversely affect the interests of a third party.⁴⁹¹ Proceedings on a wager are considered a waste of judicial time.⁴⁹² It creates a great burden on courts because there are a considerable number of cases involving the enforcement of socially unproductive and unnecessary contracts.⁴⁹³ Therefore, wagering is an anti-social activity, and does not give any benefit to society.

⁴⁸⁵ See the Preamble to the LAA 1774

⁴⁸⁶ Preamble to the LAA 1774, *Routh v Thompson* [1809] 11 East 428; *The Moonacre* [1992] 2 Lloyd's Rep 501, p510 per Colman QC stated that: "provided the assured has sufficient interest in the subject matter of the insurance to prevent his contract being a wagering contract, he is entitled to enforce that contract."; *Lonsdale & Thompson v Black Arrow Group* [1993] 2 Lloyd's Rep 428, p432 per Sumption QC; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p78; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p139; D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p17; Lee Kiat Seng, "Insurable interest in Singapore", (1997) *Singapore Journal of Legal Studies* 499, p528 – see note 96 for critical analysis of other writers on the difference between wagering and insurance contract; ALRC 20, p73; J. Davey, "The reform of gambling and the future of insurance law", (2004) *Legal Study* 507, p514-515; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p135-136; R. Merkin, "Gambling By Insurance – A Study of the Life Assurance Act 1774" (1980) 9 *Anglo-American L.R.* 331

⁴⁸⁷ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p17

⁴⁸⁸ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 *Col.I.R.* 1162, p1179

⁴⁸⁹ *Foster v Thackeray* [1781] 1 T.R. 57; *Atherfold v Beard* [1788] 2 T.R. 610

⁴⁹⁰ *Jones v Randall* [1774] 1 Cowp. 37; *Hartley v Rice* [1808] 10 East 22; *Gilbert v Sykes* [1812] 16 East 150

⁴⁹¹ *Earl of March v Pigot* [1771] 5 Burr. 2802; *Da Costa v Jones* [1778] 2 Cowp. 37; *Good v Elliot* [1790] 3 T.R. 693; *Ditchburn v Goldsmith* [1815] 4 Camp. 152; *Eltham v Kingsman* [1818] 1 B&Ald. 683; for a critical analysis on this issue, see: R. Merkin, "Gambling By Insurance – A Study of the Life Assurance Act 1774" (1980) 9 *Anglo-American L.R.* 331

⁴⁹² *Brown v Leeson* [1792] 2 H.Bl. 43; *Bulling v Frost* [1794] 1 Esp. 235; *M'Allester v Haden* [1810] 1 Samp. 438; *Squires v Whisken* [1811] 3 Samp. 140

⁴⁹³ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 *Col.I.R.* 1162, p1180

By contrast, insurance is justified by reference to the transfer of risk from insureds to insurers, and gives financial security to the insureds.⁴⁹⁴ Insurance is viewed as a necessary element of trade, but wagering should be dismissed as immoral and unproductive. Lord Mansfield in the case of *Kent v Bird*⁴⁹⁵ stated that: “a policy of insurance is, in the nature of it, a contract of indemnity, and of great benefit to trade. But the use of it was perverted by its being turned into a wager.”⁴⁹⁶

The requirement of insurable interest would distinguish contracts that sought to insure against the risk of actual future loss from those that instead sought to speculate on whether some contingency would occur; and it would prevent use of insurance contracts to gamble or speculate on properties or lives.⁴⁹⁷ It was believed that this kind of gambling in the guise of insurance could be limited by invalidating contracts lacking an insurable interest.⁴⁹⁸

However, the distinction between insurance and wagering was a product of law and culture, and not axiomatic.⁴⁹⁹ The courts have faced difficult tasks in distinguishing the two contracts in a number of cases.⁵⁰⁰ It is difficult to make a clear-cut dividing line. An insurance contract and a wager have two similar characteristics. First, both contracts are a contract upon a condition. An insurance contract is an agreement whereby the insurer, in return for a consideration of premiums, promises to pay a sum of money upon the occurrence of a particular event or contingency resulting in loss. It means that a contract of insurance is a contract upon a condition. A gambling is also a contract upon a condition; when the condition bet against happens, the gambler will win the prize. Second, the purchaser in both contracts pays a relatively small amount of money in exchange for the possibility of recovering something of much greater value.

⁴⁹⁴ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p139-140; J. Davey, “The reform of gambling and the future of insurance law”, (2004) Legal Study 507, p509

⁴⁹⁵ [1777] 98 ER 1253

⁴⁹⁶ *Ibid*, p1253

⁴⁹⁷ J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p479-480

⁴⁹⁸ J. Davey, “The reform of gambling and the future of insurance law”, (2004) Legal Study 507, p509

⁴⁹⁹ J. Davey, “The reform of gambling and the future of insurance law”, (2004) Legal Study 507, p507

⁵⁰⁰ *Moran, Galloway v Uzielli* [1905] 2 KB 555, p563; *The Moonacre* [1992] 2 Lloyd’s Rep 501, p510; *Lonsdale & Thompson Ltd v Black Arrow Group Plc* [1993] 3 All ER 648, p653

2.3.2. Preventing moral hazard:

Another purpose of the requirement of insurable interest is to prevent moral hazard.⁵⁰¹ Moral hazard in the context of insurance refers to the attempt to destroy the insured property or to murder the insured life. The beneficiaries of an insurance contract that lacks an insurable interest will be tempted to make such ill fortune happen, and then get insurance money.⁵⁰² The introduction of the principle of insurable interest, to some extent, reduced the moral hazard.

Moral hazard refers to two situations: (i) where a policyholder tends to take less care in safeguarding his own insured property, and (ii) more broadly, and which raises more serious concern, where a policyholder has insured the property of a third party or a life of a stranger.⁵⁰³ In the former situation, it increases the risk of loss to the insured's property. The insured may try to turn the insured property which is difficult to sell in a depressed market into cash by destroying it. In the latter, it increases the risk of loss to a third party.⁵⁰⁴ The policyholder is likely to destroy the subject matter of insurance in order to gain the benefit of the insurance. If the policyholder does not have an interest in the continued life of a person covered by the policy, that person has the ill fortune of being worth more to the policyholder dead than alive; likewise, insured property of a third party is worth more destroyed than preserved.

However, it is debatable that the requirement of insurable interest can reduce moral hazard.⁵⁰⁵ It is asserted that, just as banking regulation cannot eliminate armed robbery, so the concept of insurable interest cannot eliminate deliberate causing of loss.⁵⁰⁶

⁵⁰¹ Preamble to the MIA 1745: "...it hath been found by experience, that the making of insurances, interest or no interest, or without further proof of interest than the policy, hath been productive of many pernicious practices, whereby great numbers of ships, with their cargoes, have ... been fraudulently lost or destroyed."

⁵⁰²D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p17; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p134; Issuer Paper 4, p5; J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p480

⁵⁰³ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p138

⁵⁰⁴ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p480-481

⁵⁰⁵ It will be critically analysed at section 6.2.2 of this Chapter

⁵⁰⁶ *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208, p27

3. THE CURRENT POSITIONS OF ENGLISH AND VIETNAMESE LAWS ON INSURABLE INTEREST IN INDEMNITY INSURANCE

This part will provide an overview of current English and Vietnamese laws on insurable interest in indemnity insurance. It is not the author's intention to examine everything on insurable interest. Discussion will focus on some issues about the relationship between insurable interest and principle of indemnity, and certain types of indemnity insurance which cause complexity and uncertainty over enforceability of an insurance contract. In addition, comparison between English law and Vietnamese law will be made to show the similarities and differences, which will help to discover problems under Vietnamese law.

3.1. English position:

The English current law on insurable interest is complex and confusing.⁵⁰⁷ There are several statutes governing the requirement of insurable interest, some of which are out of date or appear to be a dead letter.⁵⁰⁸ In addition, the rules differ depending on type of indemnity insurance. Case law also creates uncertainty over the application of the principle of insurable interest.

3.1.1. Statutory law:

Before 2005, the Gaming Act 1845, for indemnity insurance, indirectly required the insured to show an insurable interest in the subject matter of insurance because it provided that any contract for gaming or wagering would be declared void and unenforceable.⁵⁰⁹ After 2005, the Gambling Act 2005 repealed the Gaming Act 1845.⁵¹⁰ The GA 2005 states that: "the fact that a contract relates to gambling shall not prevent its enforcement."⁵¹¹ As a result, both contracts of gambling and insurance can be enforceable, and an insured need not to show an

⁵⁰⁷ R. Merkin, "Reforming insurance law: is there a case for reverse transportation?", A report for the English and Scottish Law Commissions on the Australian experience of insurance law reform (2007) available at http://www.lawcom.gov.uk/docs/merkin_report.pdf >

⁵⁰⁸ Marine Insurance Act 1788, and Marine Insurance (Gambling Policies) Act 1909. It seems that the former still technically govern policies on goods, and it requires the name of the person interested in the insurance shall be inserted into the policy. The latter states that any person without an insurable interest taking out a contract of marine insurance will commit a criminal offence. However, it seems there has never been a prosecution under it.

⁵⁰⁹ Section 18 of the Gaming Act 1845

⁵¹⁰ Section 334(1) of the Gambling Act 2005

⁵¹¹ Section 335(1) of the Gambling Act 2005

insurable interest to prove that the contract is not a gambling contract.⁵¹² However, the question of whether the GA 2005 applies to insurance contract is still open to debate.⁵¹³

It should be noted that even if there had been no requirement of insurable interest, the principle of indemnity would still apply to all indemnity insurance contracts. It requires the insured to show an interest in the subject matter of insurance. The insured must prove his actual loss at the time of loss in order to make a valid claim. If he cannot prove the loss, the principle of indemnity prevents him from recovering, and the insurer's obligation to indemnify cannot arise.

Under English law, based on the type of insurance, rules on insurable interest relating to indemnity insurance can be divided into three categories:⁵¹⁴ rules governing marine insurance, rules governing insurance on goods, and rules governing other indemnity insurance (e.g. liability insurance and insurance on land or building). With the assumption that the GA 2005 applies to insurance contracts, the general rules on insurable interest in indemnity insurance can be summarised as follows:

- (i) Marine insurance is governed by MIA 1906. It is required that the insured must have a legal or equitable relation to the subject matter of insurance at the time of loss.
- (ii) Insurance on goods is excluded from the LAA 1774,⁵¹⁵ and it is clear that there is no statutory requirement of insurable interest. It is argued that, in insurance on goods, case law

⁵¹² M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p140; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p139-140; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p40; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p74; The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008), p39; UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p108

⁵¹³ In R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p140, it is argued that it is uncertain whether the GA 2005 applies to insurance at all. The Act was not intended to affect insurance contract because it did not include insurance within its statutory. The definition of gambling in section 3 of the GA 2005 is gaming, betting or participating in a lottery. No reference is made to insurance contract. Wager in the guise of insurance may fall within the definition of betting in section 9(b) of the GA 2005 as "making or accepting a bet on the likelihood of anything occurring or not occurring". In John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p22-23, it is argued that the GA 2005 has no effect on insurance contract, or at least has little practical importance. In UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p110, it is also argued that the GA was not intended to apply to insurance contract, and contended that the GA 2005 had introduced unfortunate uncertainty into the law on insurable interest; see also M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p204

⁵¹⁴ The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008), p37-42

⁵¹⁵ Section 4 of the LAA 1774

required the insured to have an insurable interest.⁵¹⁶ However, it is asserted that, in accordance with the principle of indemnity, the insured only needs to prove his actual loss at the time of loss in order to make a valid claim.

(iii) For other indemnity insurance, such as liability insurance and insurance on land or building, the requirement seems unclear and confusing. It was believed that those policies were covered by the LAA 1774.⁵¹⁷ If the LAA 1774 was to apply to those policies, which was a statutory requirement, then an insured would have to show an insurable interest in the subject matter of insurance at the time of making the insurance contract.

However, there is a modern view that the LAA 1774 does not apply to those policies.⁵¹⁸ Therefore, there is no statutory requirement of insurable interest. Yet, it was argued that, even if there was no such statutory requirement, case law still required the insured to have an insurable interest, concerning fire policy on building.⁵¹⁹ This argument is debateable. If the modern view is correct, in order to make a valid claim to the insurers, the insured only needs to demonstrate his actual loss as required by the principle of indemnity. The position for liability insurance and insurance on building and land is the same as that for insurance on goods.

⁵¹⁶ In UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p109, it is argued that there was a common law requirement of insurable interest. It cited the cases of *Goddard v Garrett* [1692] 2 Vern 269 and of *The Sadler's Company v Badcock* [1743] 2 Atk 554. In the latter, it was held that the insured must hold an interest in the insured property both at the time of inception and at the time of loss; see also M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p189

⁵¹⁷ See section 1 of the LAA 1774: "**No insurance to be made on the lives of persons having no interest.** From and after the passing of this Act no insurance shall be made ... on the life or lives of any person, or persons, or **on any other event or events whatsoever,...**". In M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p204, it is doubted whether the LAA 1774 applies to insurance on land and building.

⁵¹⁸ In *Mark Rowlands Ltd v Berni Inns Ltd* [1986] 1 Q.B. 211, p227, the Court of Appeal rejected the application of the LAA 1774. It stated that "this ancient statute was not intended to apply, and does not apply, to indemnity insurance". In *Siu Yin Kwan and another v Eastern Insurance Co Ltd* [1994] 1 All ER 213, the Privy Council came to the same conclusion. It adopted the reasoning that: "by no stretch of the imagination could indemnity insurance be described as 'a mischievous kind of gaming'". However, the Supreme Court has not yet given the final decision on this matter; therefore, it may be changed by the Supreme Court. Some writers also argue that this matter is not yet conclusively decided, see M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p148. Clarke said writers are divided but most agree that the LAA 1774 does not apply to indemnity insurance. He cited the case of *Re King* [1963] Ch 459 in support for the application of the LAA 1774.

⁵¹⁹ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p40, 57; UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p109

3.1.2. Case law:

At this stage, the application of the principle of insurable interest in some leading cases will be examined. It will reveal the difficulty and struggle involved in the English courts' decision as to which approach, whether the legal right test or the factual expectation test, offers the best solution. It seems that the debate between the two has never come to an end due to the lack of a comprehensive and precise definition of insurable interest. It also reveals the consistent trend towards expansion of the concept of insurable interest due to the development of economic and commercial activities. New types of interest will emerge, and these will go beyond any boundary or border to the concept of insurable interest that insurance laws and the courts have attempted to draw.

3.1.2.1. Marine insurance

In marine insurance, the insured must have a legal or equitable relation to the subject matter of insurance (the legal right test approach). If the insured has no legal or equitable relation, the insurance contract will be unenforceable; and taking out marine policies without an insurable interest is a criminal offence.⁵²⁰ This approach has been long criticised for being too narrow, and unsuited to modern commercial practices. Perhaps it might only have been suitable for the commercial practices of 200 years ago.

Indeed, it is submitted that the legal right approach is not consistent with the principle of indemnity. The principle of insurable interest is derived from the indemnity principle, but the narrow approach to insurable interest in marine insurance actually departs too far from the indemnity principle. The insured cannot recover for his actual loss just because he has no legal or equitable relation to the insured property. Some cases illustrate the problem.

In *Anderson v Morice*,⁵²¹ the insured was the buyer of a cargo of rice. After loading most of the cargo, the ship sank; and both the ship and the remaining cargo on board were lost. It was held that the insured could not recover for the loss under the insurance policy. The reason was that the risk did not pass to the buyer until the complete cargo had been loaded on board, and the risk of loss of cargo prior to shipment still remained with the seller. Therefore, the insured buyer had no insurable interest in the cargo before the shipment was completed. It is

⁵²⁰ The Marine Insurance (Gambling Policies) Act 1909; see also The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008), para. 2.15, p8

⁵²¹ [1875] L.R. 10 C.P. 609

submitted that this is unfair to the insured. The insurer had accepted the premiums to cover for the loss, but was allowed to refuse to fulfil his obligation to indemnify the insured when the loss occurred. Although the risk still remained with the seller, and the buyer was able to recover his payment from the seller,⁵²² the insured buyer finally found his policy worthless because the seller may have been insolvent and unable to refund the payment.⁵²³

In *Moran, Galloway & Co v Uzielli*,⁵²⁴ the insureds, the agents in the United Kingdom of a foreign ship, effected an insurance for a named voyage "on disbursements against the risk of total and constructive total loss of ship only". At the date of the policy the shipowners were indebted to the insureds to a considerable amount for advances for the ship's disbursements, part of which had been made for the purposes of the particular voyage and part at prior dates. The ship suffered severe damage on the voyage, and was considered as a constructive total loss. The freight, which was received and retained by the insureds under their lien, was insufficient to recoup them the amount of their advances, and the insureds, who had no lien upon the ship, brought an action on the policy of insurance to recover the balance of their advances. It was held that the fact that the insureds were interested in the debt merely as a debt⁵²⁵ did not give them any insurable interest in the ship; however, fortunately, they did have an insurable interest because they had a right to bring an action "*in rem*"⁵²⁶ to enforce their claim for advances under section 6 of the Admiralty Court Act 1840.⁵²⁷ If the insured had not had such a right, they would not have had an insurable interest because they, as an unsecured creditor only, could not show a legal or equitable relation to the insured property.⁵²⁸ It is submitted that, where the insured had an interest in the debt, and the insurers specifically agreed to cover for the risk of loss of the insured property, and later the insured

⁵²² If the payment had been made in advance by the buyer

⁵²³ It was held differently in *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* [1991] 25 NSWLR 699, an Australian case with similar facts. The *NSW Leather* will be discussed in more depth in section 4.1.2 of this Chapter

⁵²⁴ [1905] 2 KB 555

⁵²⁵ The insured clearly had an interest, as required by the principle of indemnity, in the debt that was due to them on account of their disbursements.

⁵²⁶ A proprietary action (real action) taken against the object that is the subject of the dispute (e.g. land), rather than against a person, see Oxford English Dictionary

⁵²⁷ See section 6 of the Admiralty Court Act 1840: "The High Court of Admiralty shall have jurisdiction to decide all claims and demands whatsoever in the nature of salvage for services rendered to or damage received by any ship or sea-going vessel, or in the nature of towage, or for necessaries supplied to any foreign ship or seagoing vessel, and to enforce the payment thereof, whether such ship or vessel may have been within the body of a county, or upon the high seas, at the time when the services were rendered or damage received or necessaries, furnished, in respect of which such claim is made."

⁵²⁸ For more details see *Moran, Galloway & Co v Uzielli* [1905] 2 KB 555, p556-564 per Walton J.

was unable to collect his debt on the loss of the insured property, the insured should be allowed to recover under his insurance policy.⁵²⁹

3.1.2.2. *Non-marine insurance*

In non marine indemnity insurance, the leading case is *Macaura v Northern Assurance Co.*⁵³⁰ The facts, in brief, were that the sole shareholder of a limited company, who was also a substantial creditor of the company, insured in his own name the timber owned by the company. The timber in question was standing on Macaura's land. The House of Lords held that he had no insurable interest in the timber that had been subsequently destroyed by fire. The reason was that the insured who was a shareholder had no legal or equitable interest in the property owned by the company. The insured and the company were separate legal bodies.

The decision of *Macaura* has received heavy criticisms from academics and judges.⁵³¹ This view is considered as too narrow.⁵³² The grounds for the decision of *Macaura* rest partly on the principle of the separate legal personality of a company from its members, and largely on the narrowness of the concept of insurable interest in English law.

3.1.2.3. *Extension of the concept by English courts*

Since the late twentieth century, the concept of insurable interest, to some extent, has been left to courts to interpret in English insurance laws. The courts have continuously expanded the concept to keep pace with the changes of economic activities.⁵³³

⁵²⁹ The issues of insurable interest of an unsecured creditor will be discussed at section 4.1.3 of this Chapter

⁵³⁰ [1925] A.C. 619

⁵³¹ *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208; *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p79; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p203; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p59; Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1167; R. Hasson, "Reform of the law relating to insurable interest in property- some thoughts on *Chadwick v Gibraltar General Ins*" (1983-1984) 8 Can Bus LJ 114, p116-117; J. Birds, "A shareholder's insurable interest in his company's property", (1987) J.B.L 309, p309-311; J. Davey, "The reform of gambling and the future of insurance law", (2004) Legal Study 507, p514; C. Nicoll, "Insurable interest: as intended?" (2008) J.B.L 432, p442; R. McLeod, "*Aqua-Land Exploration Ltd. v Guarantee Co. of North America et al.*: Insurable interest in an indemnity policy", (1966) 24 *U. of T. Fac. Law Rev.* 154, p159-160

⁵³² J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p59

⁵³³ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p35

One of the earliest extensions was for bailees (e.g. carriers of goods, warehouse keepers). The carriers are permitted to insure against the risk of loss of goods during transit to the full value of the goods, and are able to recover the full value.⁵³⁴ It is not limited only to the extent of their liability to the owner. This is of importance to the circumstances that the damage to, or destruction of, the goods is not caused by the carriers or may be caused by the carriers' negligence which is excluded under the contract for carriage of goods. Where the insurance money is greater than their liability, the carriers will hold the excess of their own loss in trust for the owner.

This extension is based on two grounds. The first one is that the carriers are in possession of the goods during transit, and are potentially liable for the full value.⁵³⁵ Another ground, which is more important, is that this extension is suited to commercial practice and commercial convenience.⁵³⁶ In *Petrofina (UK) Ltd v Magnaload Ltd*,⁵³⁷ Lloyd J stated that where "there were two persons, bailor and bailee, having concurrent interests in the same goods, so that it would be reasonable and natural and economical for one of them to insure for the benefit of both. In the sphere of insurance on goods, it would be unrealistic and productive of injustice to require from the party taking out the insurance an express declaration or conscious assumption of trusteeship. The existence of the intention is sufficient."

Another example of the extension of the concept relates to large offshore or construction projects, and the doctrine of "pervasive interest" was introduced. In such projects, normally,

⁵³⁴ In *Hepburn v Tomlinson [Hauliers]* [1966] 1 All ER 418 (House of Lords), the insured carried cigarettes for the maker and also insured them. Without fault or liability on the part of the insured, the cargo was stolen. The insurer resisted the claim on the ground that such insurance was a contract of indemnity and that the insured, having incurred no liability, had suffered no loss. The House of Lords held that, as a matter of construction, the insurance was not of liability but of goods. The carrier had an interest insuring the goods, and could recover the full value, provided that the insurance monies over and above the amount of his own loss (in this case none) were held on trust for the maker.; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p69

⁵³⁵ *Waters v Monarch Fire & Life Assurance Co* [1843-60] All ER Rep 654, p655-656 per Lord Campbell: "I think that a person entrusted with goods can insure them without orders from the owner, and even without informing him that there was such a policy. It would be most inconvenient in business if a wharfinger could not, at his own cost, keep up a floating policy for the benefit of all who might become his customers ... as the property is wholly destroyed, the value of the whole must be made good, not merely the particular interest of the plaintiffs. They will be entitled to apply so much to cover their own interest, and will be trustees for the owners as to the rest. The authorities are clear that an assurance made without orders may be ratified by the owners of the property, and then the assurers become trustees for them."

⁵³⁶ *Tomlinson v Hepburn* [1966] 1 Q.B 21 (Court of Appeal), p51 per Lord Pearce; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p159; D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p37-38; UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p114

⁵³⁷ [1984] QB 127, p135

there are one head-contractor and several sub-contractors who are involved in and have interests in the project. If the narrow approach is strictly followed, each contractor or sub-contractor has an insurable interest in the project to some extent. They are only allowed to take out insurance covering their own interests, and not allowed to take out insurance covering the interests of other sub-contractors. Their interests in part of the project shall satisfy the requirement that there must be legal or equitable relation between the insured and the property under *Macaura v Northern Assurance*.⁵³⁸

This assumption is important for the determination of insurers' rights to subrogate. If each contractor is only allowed to insure his respective interest, in the event of loss, each contractor or sub-contractor can only claim in respect of his individual loss, and, subsequently, the insurers are entitled to stand in the one contractor's shoes to bring an action against other contractors who are at fault, to recover their payment. On the other hand, if all contractors or sub-contractors are co-insured under a single policy, the insurers are not entitled to enjoy their subrogation rights because co-insureds cannot sue themselves.⁵³⁹

Because of the consistent trend towards extension of the insurable interest concept and the court's preference for granting sub-contractors an insurable interest in the whole of the construction project, the sub-contractor insureds are entitled to claim for not only claim their own loss, but also for the entire losses. The insureds shall hold on account in respect of the remainder for the benefit of the other insureds who have suffered loss.⁵⁴⁰

For example, in *Petrofina (UK) Ltd v Magnaload Ltd*,⁵⁴¹ the main contractors took out insurance to cover the construction of an oil refinery extension, in the name of the contractors, sub-contractors and site owners. Sub-contractors supplying heavy lifting equipment dropped a gantry, damaging the work in progress. The insurers then sued the sub-contractors for negligence, in the name of the contractors. The question was whether the sub-contractors had an insurable interest that extended to the whole of the contract works, or whether their interest was limited to the equipment owned by them. It was held that the sub-contractors were covered in respect of the entire contract works; and they had an insurable

⁵³⁸ [1925] A.C. 619

⁵³⁹ *Simpson v Thomson* (1877) 3 App. Cas. 279

⁵⁴⁰ *Petrofina (UK) Ltd v Magnaload Ltd* [1984] QB 127; *Stone Vickers Ltd v Appledore Ferguson Shipbuilders Ltd* [1991] 2 Lloyd's Rep 288; *Deepak Fertilisers & Petrochemicals Ltd v Davy McKee [London] Ltd* [1999] 1 All ER [Comm] 69; *National Oilwell [UK] Ltd v Davy Offshore Ltd* [1993] 2 Lloyd's Rep 582; *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587

⁵⁴¹ [1984] QB 127

interest in the whole site, which included property owned by any other co-insured or for which they were responsible. The main ground for the decision was that it is commercially convenient to allow all the parties to insure the whole site.⁵⁴²

The latest leading case on insurable interest, which continues the trend towards extension of the concept, is *Feasey v Sun Life Assurance Co of Canada*.⁵⁴³ The case was concerned with both life insurance and marine insurance. The Court of Appeal took the opportunity to re-examine previous cases and tested the requirement of insurable interest in a modern context.

Eventually, the Court moved away from the legal right approach. Lord Waller, who gave the leading judgment, stated: “something less a legal or equitable interest in the property ... has been thought to be sufficient”⁵⁴⁴ to create an insurable interest. He categorised the cases of insurable interest into four groups, three of which relate to property insurance: (i) where the subject matter insured is an item of property, the insured must have an legal or equitable interest in the property; (ii) where the subject matter appears to be a particular item of property, but where properly construed the policy extends beyond that item and covers such interest as the insured might possess; and (iii) where the insured faces loss by reason of the destruction of the insured subject matter, even though he has no close relationship with the subject matter - there is no need for the insured to have a legal or equitable relationship with the subject matter insured.⁵⁴⁵

In Lord Waller’s opinion, the concept of insurable interest should be interpreted broadly, and Lawrence J’s factual expectation approach should be followed. However, it is not the final decision of the Supreme Court, and the Supreme Court can change the verdict.

⁵⁴² *Ibid* p136 per Lloyd J.

⁵⁴³ [2003] 2 All.E.R. [Comm] 587

⁵⁴⁴ *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587, p610

⁵⁴⁵ The last category is a quite wide one. In order to support his arguments, Lord Waller summarised the appropriate principles in English authorities as follows: “(1) it is from the terms of the policy that the subject of insurance must be ascertained; (2) it is from all the surrounding circumstances that the nature of the insured’s insurable interest must be discovered; (3) there is no hard and fast rule that because the nature of an insurable interest relates to a liability to compensate for loss, that insurable interest could only be covered by a liability policy rather than a policy insuring property; (4) the question whether a policy embraces the insurable interest intended to be recovered is a question of construction. The subject or terms of the policy must be so specific as to force a court to hold that the policy has failed to cover the insurable interest, but a court will be reluctant so to hold; (5) it is not a requirement of property insurance that the insured must have a “legal or equitable” interest in the property. It is sufficient under s5 of MIA 1906 for a person interested in a marine adventure to stand in a “legal or equitable relation to the adventure”. That is intended to be a broad concept... (7) the interest in policies falling within s1 of LAA 1774 must exist at the time of entry into the policy, and be capable of pecuniary evaluation at that time”, see *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587, p613-614

To sum up, English insurance laws are complex and confusing. The requirement of insurable interest differs, depending on the type of insurance. Each type of insurance is governed by different statutes; some of which are a dead letter, and some of which create uncertainty about application of the doctrine. English courts have also faced difficulties in giving a comprehensive and precise concept of insurable interest, and in finding the best solution to the problem.⁵⁴⁶ Sometimes they changed their minds, and moved from one way to another, creating more uncertainty over application of the doctrine. Although the debate on the requirement of insurable interest has lasted for more than 200 years, the Supreme Court has not reached a final decision. Let's wait and see!

3.2. Vietnamese position:

This part will give a general picture of Vietnamese laws on insurable interest in indemnity insurance. Generally speaking, rules on insurable interest under Vietnamese laws are drafted following the English approach. The insured is also required to have a legal relation to the subject matter of insurance (the legal right approach).⁵⁴⁷ It could be said that the rules under Vietnam's laws are even stricter or narrower than those under English laws.

3.2.1. Statutory law:

Based on type of insurance, rules on insurable interest under Vietnamese insurance laws can be divided into two categories: rules on marine insurance, and rules on non-marine insurance. Different types of insurance are governed by different laws. For both marine insurance and non-marine insurance, there is a statutory requirement of insurable interest under Vietnamese insurance laws. Where the insured has no insurable interest in the subject matter of insurance, the insurance contract will be declared void.⁵⁴⁸

⁵⁴⁶ UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p99; D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p32

⁵⁴⁷ There is no equity law in Vietnam's laws, therefore, the equitable relation between the insured and the subject matter of insurance was not stipulated in the definition of insurable interest under Vietnam's Maritime Code 2005.

⁵⁴⁸ Article 22(1) of the Vietnam's Law on Insurance Business: "An insurance contract shall be void in the following circumstances: (a) The purchaser of insurance does not have an insurable interest;...". Where a contract is declared as void, the legal consequences are that: Article 137 of Vietnam's Civil Code 2005: "*Legal effect of invalidity of a civil transaction* (1). An invalid civil transaction shall not give rise to civil rights and obligations of the parties, or to changes and termination of such rights and obligations as from the time the transaction is entered into. (2). Where a civil transaction is valid, the parties shall restore everything to its original state and shall return to each other what they have received. If restitution cannot be made in kind, it may

Policies on marine insurance are governed by Vietnam's Maritime Code 2005.⁵⁴⁹ The definition of insurable interest in article 226 of Vietnam's Maritime Code 2005 is copied from section 5 of the MIA 1906. Article 226 provides that: "(1) A person with an insurable interest is a person who is interested in a subject-matter of insurance in a sea voyage. (2) A person is interested in a sea voyage when he/she is able to prove that he/she has any relation to the voyage or to any subject-matter of insurance at risk in it, in consequence of which such person may benefit by the safety and due arrival of the subject of insurance, or may not benefit by its loss or by damage to it or by the detention of it, or may incur liability in respect of it..."

The meaning of "insurable interest" under article 226 is the same as that of section 5 of the MIA 1906. It is also required that the insureds must have a legal relation to or legal liability arising out of the subject matter of insurance. There are only two minor differences. First, the words "in particular" are dropped from the original texts in section 5. It means that, in marine insurance, policyholders who fall outside the list in article 226 have no insurable interest. Unlike English law, there is no chance for the policyholders outside the list to show an insurable interest under Vietnamese laws.⁵⁵⁰ Second, the word "equitable" was not used in article 226 since there is no equity law under Vietnam laws.

Regarding the time when an insurable interest is required, the insured must have an interest at the time of loss,⁵⁵¹ and he needs not to show an insurable interest at the time of inception.⁵⁵²

Non-marine indemnity insurance policies are governed by Vietnam's Law on Insurance Business 2000. The concept of insurable interest is stipulated in the article 3(9). Instead of

be paid in money, except where the transacted property, benefits and income which had been received are confiscated in accordance with law. The party at fault must pay compensation for any loss."

⁵⁴⁹ Article 225, 226 and 227 of Vietnam's Maritime Code 2005

⁵⁵⁰ See section 2.2. The nature of insurable interest of this Chapter

⁵⁵¹ Article 226(3) of Maritime Code 2005: "The assured must have interest in the subject of insurance at the time of occurrence of the loss though the assured need not be interested in the subject of insurance when the insurance is effected ..."

⁵⁵² Although, in non-marine indemnity insurance, the insured must show an insurable interest both at the time of entering into the contract and at the time of loss (will be discussed later), the insured is required to have an insurable interest only at the time of loss. This is so because the general rule on priority of application of statute law is that specific laws prevail over general laws. Therefore, marine insurance policies are first governed by the Vietnam's Maritime Code; where the question in dispute is not covered by the Vietnam's Maritime Code, it will be governed by the Vietnam's Law on Insurance Business (marine insurance is more specific than general insurance); and then if it is not covered by the Vietnam's Law on Insurance Business, it will be governed by the Vietnam's Civil Code (insurance contract is more specific than civil contract or civil transaction); see also Article 12 of the Vietnam's Law on Insurance Business 2000 "... (3) Contracts of marine insurance shall be governed by the provisions of the Maritime Code; with respect to issues not covered by the Maritime Code, the provisions of this Law shall apply. (4) Issues relating to insurance contracts which are not covered by this Chapter shall be governed by the provisions of the Civil Code and the provisions of other relevant laws."

formulating an exhaustive definition, article 3(9) merely lists the rights which may create insurable interest. It states: “insurable interest means a right of ownership, right of possession, right of use, or property right;⁵⁵³ maintenance rights and obligations to the person insured against.”

In order to show an insurable interest, the insured must have rights in the insured property or rights derivable out of contracts about the property. However, article 3(9) does not mention anything about legal liabilities arising out of the subject matter of insurance, which completely and sufficiently constitute insurable interests. It is submitted that this could be a negligent omission.

In relation to the time of attachment of insurable interest, there is no provision in Vietnam’s Law on Insurance Business 2000 that clearly specifies at which time the insured must have an insurable interest. Article 22(1) only requires the insured to show an insurable interest in the subject matter of insurance; if not, the contract will be declared as void. Article 23(1) stipulates that the insurance contract shall be terminated if the purchaser of insurance no longer has an insurable interest.⁵⁵⁴ Taken the two articles together, it implies that the insured must have an insurable interest both at the time of making the contract and at the time of loss, and a lapse of insurable interest at any stage during the life of the policy will terminate the insurance contract.

3.2.2. Judicial practice:

Vietnamese courts make decisions according to statutory laws. Because the law relating to insurable interest is strict, so are the courts’ decisions. For example, if the English case of *Macaura v Northern Assurance Co.*⁵⁵⁵ was resolved by a Vietnamese court, the same

⁵⁵³ “Property rights” are defined in Article 181 of Vietnam’s Civil Code 2005 as “rights which can be valued in terms of money and may be transferred in civil transactions, including intellectual property rights”.

⁵⁵⁴ Article 23 of the Vietnam’s Law on Insurance Business 2000: “... an insurance contract shall also terminate in the following circumstances: (1). The purchaser of insurance no longer has an insurable interest;...” If the insurance contract terminates, the parties do not have to continue to perform their obligations. A party which has already performed its obligation may demand the other party to make payment, see Article 24 of the Vietnam’s Law on Insurance Business: “*Legal consequences of termination of insurance contracts:* (1). In the case of termination of an insurance contract pursuant to the provisions in article 23.1 of this Law, an insurer must refund to the purchaser of insurance that part of the paid insurance premium which corresponds to the remaining duration of the insurance contract, after deducting legitimate expenses relating to the insurance contract;...”

⁵⁵⁵ [1925] A.C. 619

judgment would have been reached. The reason is that the doctrine of separate legal personality is recognised under Vietnamese laws as well.⁵⁵⁶

However, due to the short history of development and non-comprehensiveness of Vietnamese insurance laws, the courts' judicial practices relating to disputes over insurable interest are influenced by industrial practices in the insurance market and by the development of civil law and contract law-which is in favour of freedom of contract. Those influences make courts' decisions, to some extent, more flexible and they depart from the requirement of insurable interest by statutory laws. This flexibility is justified by Vietnamese courts' power of discretion to interpret provisions under statutory laws.⁵⁵⁷ Nonetheless, this flexibility actually creates uncertainty over application of the principle of insurable interest. In addition, the non-comprehensiveness of Vietnam's insurance laws and judges' lack of knowledge of insurance law further muddy the water.

In Vietnam's insurance market, insurers usually use the standard forms of insurance policy drafted by giant international players, such as AIG, ACE, Lloyd, and Allianz. The local companies do business following the giant players' practices.⁵⁵⁸ Therefore, courts have occasionally interpreted the rules on insurable interest in a more flexible way in order to be in compliance with those commercial practices. Their flexible interpretation actually conflicts with statutory laws. For example, the contractor and the owner of a construction project was granted an insurable interest in the whole of the properties involved in the project, which conflicted with article 3 of Vietnam's Law on Insurance Business.⁵⁵⁹

⁵⁵⁶ Article 38(1)(b) of Vietnam's Law on Enterprises 2005: "A member shall be liable for the debts and other property obligations of the enterprise within the amount of capital that it has undertaken to contribute to the enterprise". Article 63 of Vietnam's Law on Enterprises 2005: "A one member limited liability company is an enterprise owned by one organization or individual (hereinafter referred to as *company owner*); the company owner shall be liable for all debts and other property obligations of the company within the amount of the charter capital of the company."; see also article 77(1)(c), article 130(1)(c) of Vietnam's Law on Enterprises 2005

⁵⁵⁷ Do Van Dai, *Luat hop dong Viet Nam: ban an va binh luan an*, (NXB Chinh tri quoc gia, 2008) [Trans: Do Van Dai, *Vietnamese contract laws: judgments and commentaries*, (National Politics Publishing House, 2008)], p51; Vo Tri Hao, "Vai tro giai thich phap luat cua toa an", (2003) *Tap chi Khoa hoc phap ly* 12 [Trans: Vo Tri Hao, "The role of legal interpretation of the courts", (2003) *Journal of Legal Science* 12], p13-14; Tuong Duy Luong, "Vai suy nghi ve viec tong ket thuc tien xet xu, huong dan ap dung thong nhat phap luat cua toa an nhan dan toi cao", (2007) *Tap chi Nha nuoc va Phap luat* 11 [Trans: Tuong Duy Luong, "Some thoughts on synthesizing judging experience, guidance for the consistent application of laws by the People's Supreme Court", (2007) *Journal of State and Law* 11], p16; P. Nicholson, "Vietnamese jurisprudence: informing court reform" in J. Gillespie and P. Nicholson (eds), *Asian socialism & legal change: the dynamics of Vietnamese and Chinese reform*, (Asia Pacific Press, Canberra, 2005)

⁵⁵⁸ The reason for this is that it is easier to take out reinsurance contract.

⁵⁵⁹ Article 3(9) of Law on Insurance Business 2000: "Insurable interest means a right of ownership, right of possession, right of use, or property right; maintenance rights and obligations to the person insured against."

3.2.3. Insurance law vs. other laws:

The trend towards the supremacy of freedom of contract under Vietnam's civil laws also contributes to inconsistency in interpretation of the rules on insurable interest.⁵⁶⁰ Sometimes, if terms of a contract between the parties are expressly stipulated, the courts would uphold the intention of the parties on the ground of freedom of contract, even if this intention conflicts with the statutory requirement of insurable interest. Indeed, the courts wrongly apply the principle of freedom of contract due to lack of knowledge of insurance laws, and they "ignore" the fundamental principle that "specific laws prevail over general laws".⁵⁶¹

Some cases are examined to illustrate the problems. For example, concerning loss of goods prior to shipment, the rules on insurable interest were applied in two different ways, which contradict each other.⁵⁶² In *Vinashin Petroleum Investment & Transport Joint Stock Co. v Bao Minh Insurance Corp*,⁵⁶³ the insurance contract provided that the voyage to be covered was from the seller's warehouse in Bangkok, Thailand to the buyer's warehouse in Hochiminh, Vietnam. The term in the contract for sale of goods between the buyer and the seller was C&F Bangkok port Incoterms 2000. The cargo was damaged due to an accident during transit from the seller's warehouse to the Bangkok port. It was held that the insured (VPIT) was entitled to recover under the policy because the parties agreed in their contract that the voyage to be covered is from seller's warehouse to buyer's warehouse.

The court gave the judgement in favour of the insureds on the ground of freedom of contract. The intention of the parties to the insurance contract was upheld. The freedom of contract is recognised in article 4 of Vietnam's Civil Code 2005 and in article 11 of Vietnam's Commercial Law 2005. They provide that parties to a civil or commercial contract have the right to freely reach agreements if such agreements are not prohibited by or inconsistent with law. This right is respected and protected by law, and all lawful agreements shall bind the

⁵⁶⁰ Article 4 in Chapter II: Fundamental principles under Vietnam's Civil Code 2005: "*Principle of free and voluntary undertaking and agreement*: The law guarantees the freedom to undertake and agree on the establishment of civil rights and obligations if such undertakings and agreements do not breach matters prohibited by law and are not contrary to social ethics.

In civil relations, parties shall be entirely voluntary and no party may force upon, prohibit, coerce, intimidate or hinder any other party.

All lawful undertakings and agreements shall bind the parties and must be respected by individuals, legal entities and other subjects."

⁵⁶¹ See section 3.1.1 of Chapter 2

⁵⁶² *Vinashin Petroleum Investment & Transport Joint Stock Co. v Bao Minh Insurance Corp* [2007] at Hochiminh City's People Court vs. *Thai Duyen Trading & Transport Co. v AIG Vietnam* [2006] at Haiphong's People Court

⁵⁶³ [2007] at Hochiminh City's People Court

parties. Therefore, the court believed that where the parties to the insurance contract expressly stipulated that the voyage to be covered was from the seller's warehouse to the buyer's warehouse, the cargo should be protected during the whole transit. If the cargo was lost during movement onshore before loading at the port of departure, the buyer should be entitled to recover under the insurance policy.

However, the principle of free and voluntary undertaking and agreement was applied in the wrong way in this case. Although the parties to the insurance contract agreed to extend the insurance cover beyond the ship's rail (to the seller's warehouse), the existence of such cover does not mean that a C&F buyer, who had no insurable interest when the cargo was lost, was entitled to make a valid claim. The court was wrong in thinking that the requirement of insurable interest may be contracted out by the parties.

Indeed, the court "forgot" the fundamental principle that "specific laws prevail over general laws", which should be applied in this case. Under Vietnam's legal system, there is a general rule on the order of priority in applying legislation. There are two aspects to this rule. First, specific law prevails over general law, where the two laws conflict with each other. Second, where the specific law does not contain any provision governing the question in a dispute, the general law is applied.

For example, if a dispute relates to marine insurance, and there are two provisions, which may govern the question in the dispute, in both Vietnam's Maritime Code 2005 and Law on Insurance Business 2000, and the two provisions conflict with each other, then the provision in Maritime Code 2005 is applied.

If there is no provision in law on marine insurance (Maritime Code 2005) which governs the question, the rules on general insurance (Law on Insurance Business 2000) are applied.⁵⁶⁴ If there is no such provision in law on general insurance either, then the rules on commercial contract apply (Commercial Law 2005). If there is no provision in law on commercial contract either, then the rules on civil contract apply (Civil Code 2005).

Applying the principle of order of priority to this case, as it was concerned about marine insurance, the provisions relating to marine insurance under Maritime Code 2005 are first

⁵⁶⁴ Article 12 of the Vietnam's Law on Insurance Business 2000 "...(3) Contracts of marine insurance shall be governed by the provisions of the Maritime Code; with respect to issues not covered by the Maritime Code, the provisions of this Law shall apply. (4) Issues relating to insurance contracts which are not covered by this Chapter shall be governed by the provisions of the Civil Code and the provisions of other relevant laws."

employed. Article 226 of the Code requires that the insureds must have an insurable interest in the cargo at the time of loss. In addition, because there is no provision in Maritime Code 2005, governing the issue of legal consequence of lack of insurable interest, article 22(1) of Vietnam's Law on Insurance Business 2000, which governs the issue, is applied. It provides that where a policyholder has no insurable interest in the subject matter of insurance, the insurance contract shall be void.⁵⁶⁵ These two provisions prevail over article 4 of Vietnam's Civil Code 2005 and article 11 of Vietnam's Commercial Law 2005 on principle of freedom of contract. It means that the statutory requirement of insurable interest cannot be contracted out by the parties to the contract.

In this case, the cargo was lost before being shipped on board, and, in accordance with the C&F Incoterms 2000, the risk of loss still remained with the seller. Since the risk had not passed to the insureds (VPIT), they had no legal relation to the cargo, and had no insurable interest in it when the loss occurred. Therefore, the insureds' claim should be denied.

By contrast, the rules on insurable interest were applied in the correct way in *Thai Duyen Trading & Transport Co. v AIG Vietnam*.⁵⁶⁶ In this case, the insurance contract stipulated that the voyage to be covered was from Singapore port to Haiphong port. A container of malt was lost during loading at Singapore port.⁵⁶⁷ The insurer denied the claim on the ground that the risk had not passed to the buyer. The Haiphong People's Court gave the judgment in favour of the insurer. This decision was made by following the doctrine of insurable interest adopted in marine insurance, as discussed above.

3.2.4. Industrial practice:

In recent years, a number of large offshore and construction projects have been carried out in Vietnam. These projects are covered by the branches of the giant international insurance companies. By following their practice, the owners of such projects or the contractors⁵⁶⁸ are allowed to take out a co-insurance policy covering both their own properties, their liabilities,

⁵⁶⁵ Article 22(1) of the Vietnam's Law on Insurance Business: "An insurance contract shall be void in the following circumstances: (a) The purchaser of insurance does not have an insurable interest;..."

⁵⁶⁶ [2006] at Haiphong's People Court

⁵⁶⁷ The term in the contract for sale of goods between the buyer and the seller was FOB Singapore port Incoterms 2000

⁵⁶⁸ Sub-contractors are not allowed to do so because insurers refuse to enter into such contracts with sub-contractors.

and the properties and liabilities of their sub-contractors; they are co-insureds under a single policy.⁵⁶⁹ The insurers agree to waive their rights of subrogation in the event of loss.⁵⁷⁰

Co-insurance is quite a new practice in the Vietnamese insurance market. This practice reflects the factual expectation approach. The contractors and owners of project have an insurable interest in the entirety of the insured properties involved in the construction project.⁵⁷¹ This is now a common practice in Vietnam. The reason for this widespread adoption is that their liabilities to their insureds are often covered by reinsurance contracts with foreign insurance companies.

The Vietnamese courts' attitude to this matter is not very clear. It is possible that they will uphold the intention of the parties or perhaps they will apply the legal requirement of insurable interest as stated by statutes to strike an insurable interest from contractors or sub-contractors. However, it is guessed that the former view should be supported. There are three reasons to support it. First, the principle of freedom of contract is recognised under Vietnamese laws of contract. Second, the large foreign insurers do indemnify their insureds in such circumstances and do accept to reinsure Vietnamese insurers' liabilities. Third, a general rule on interpretation of insurance contract is that if a term or condition in an insurance contract is unclear, it should be interpreted against the insurers.⁵⁷²

Conclusion

To conclude, in indemnity insurance, there is a statutory requirement of insurable interest under Vietnamese insurance laws. It is required that the insured must have a legal relation to the subject matter of insurance, and the insurable interest must be legally recognised. In marine insurance, the insureds only need to show an insurable interest at the time of loss. In

⁵⁶⁹ In standard forms of the policy, the insureds are defined as: "the Head contractors and all subsidiaries (including branches), affiliated or associated companies, consultants and their respective agents, officers and employees, and all their participants, co-ventures, contractors and sub-contractors that exist now or exist in the future as the head contractors' respective rights and interests in connection with the Insureds' business stated hereunder."

About insurers' liability: "This Policy is extended to cover the Insureds against any Third Party Liabilities arising from or in connection with the use, operation or otherwise of equipments by the Insureds in ports and/or supply bases in the territory of Vietnam."; see the standard forms of ACE Vietnam, Bao Viet, Bao Minh.

⁵⁷⁰ "The Insurers waives their rights of subrogation against the Insureds and its affiliates and any officer, employee, agent, servant or contractor of Insureds and its affiliates."

⁵⁷¹ It is the doctrine of "pervasive interest" under English insurance law.

⁵⁷² Article 21 of the Vietnam's Law on Insurance Business 2000: "*Interpretation of contracts of insurance*: If an insurance contract contains provisions which are unclear, those provisions shall be interpreted in favour of the purchaser of insurance." In the opinion of the majority of Vietnamese judges, the insurers are the persons who draft the policy, therefore, they should be binding with what they have proposed and where the terms in the policy are not clear, the terms should be interpreted in favour of the policyholders.

non-marine indemnity insurance, the insureds have to demonstrate their interest at both the time of contract and the time of loss. Their interest must continuously exist throughout the policy. If not, the policy can be unilaterally terminated by the insurers. It is submitted that the rules on insurable interest in Vietnamese insurance laws, like those in English laws, are very strict and need reform.

4. DOES THE “LEGAL RIGHT” APPROACH MEET THE NEEDS OF THE MODERN INSURANCE MARKET?

At this stage we will discuss whether the “legal right” approach meets the needs of modern economic activities. The discussion will focus on the following issues, namely: whether the approach is consistent with or departs from the principle of indemnity; whether the approach balances the interests of both insurers and insureds; and whether the rules on insurable interest are simple and easy to apply.

The “legal right” approach has been accepted for more than two hundred years under English law and for more than thirty years under Vietnamese law. The approach came from the judgment of Lord Eldon in the case of *Lucena v Craufurd*.⁵⁷³ It requires that the insured must have a legal or equitable relation to the subject matter of insurance. Under Vietnamese laws, there is no equity law; therefore, the insured must show a legal relation to the subject matter insured.

The legal right approach is out-of-date, and unsuitable for modern economic activities. It has been long criticised for its strictness. In many situations, the approach deprives the insured of the right of insuring his property. For example, a sole shareholder of a company cannot insure the company’s property although he has an economic interest in the properties. If the company’s property is destroyed, the sole shareholder will suffer an economic loss because he has lost a part of the money that he has invested in the company. But his claim will be rejected because he has no legal interest in the company’s property.

An oil company has economic interests in the properties near the company; because if the properties nearby are damaged or destroyed due to the companies’ production activities, the company might be under a duty to make compensation to the owners of the nearby properties

⁵⁷³ [1806] 2 Bos. & P.N.R. 269

as it is required by the law of the country in which the company is doing business. If this duty is not clearly required by law,⁵⁷⁴ there may be a principle of honour or a high public expectation that the company should do so. If the company do not, it may lose its reputation in the local community, possibly leading to economic ramifications.⁵⁷⁵

In the context of modern economics, the categories of policyholders' interests in the insured property have been expanded. Policyholders may have a number of different economic interests in the insured properties, other than legal or equitable interests. For instance, owners of a project may have an interest in a plan that belongs to the architects if loss of the plan results in a delay in the construction progress. Contractors or owners of the project may have an interest in the properties of sub-contractors on the ground that they are co-insureds under a single policy covering the entirety of the properties involved in the construction project.⁵⁷⁶ FOB or C&F buyers may suffer an actual economic loss, if the payment for the goods has been made in advance, and the goods have been lost in transit from the seller's warehouse to the port of loading, and the seller becomes insolvent so the buyers cannot get their money back from the seller. They have no insurable interest on the goods before shipment according to the legal right approach because the risk of loss of goods only passes to them on shipment.⁵⁷⁷

As the legal right approach does not embrace all of the insureds' interests in the insured property, it excludes any interests of the insureds which are not legally recognised. This may cause injustice to the insureds where their interests are not legal interests. Moreover, this approach prevents the insureds from recovering their actual economic losses. Therefore, it has departed from the principle of indemnity. It is submitted that this departure should not exist. The requirement of insurable interest should run in parallel with the fundamental economic nature of insurance contracts- to fully indemnify insureds for their actual economic losses.

In addition, the legal right approach causes several other problems, such as giving insurers an opportunity to use the principle of insurable interest as a technical defence against the insureds' claims, creating difficulties for both insurers and insureds in understanding and

⁵⁷⁴ Which rarely happens at the present because of the increasing awareness of the consequences of environmental damage

⁵⁷⁵ C. Nicoll, "Insurable interest: as intended?" (2008) J.B.L 432, p446

⁵⁷⁶ Discuss later at section 5.3.1 of this Chapter

⁵⁷⁷ For more details see section 4.1.2 of this Chapter

applying the rules on insurable interest, producing uncertainty over application of the rules, and penalising only the insureds for breach of the principles of insurable interest.

Since Vietnamese insurance laws also adopt the legal right approach, the problems caused in Vietnam may be the same as those in England. Therefore, the problems which English laws have faced when developing and implementing the legal right approach will be critically analysed in order to understand in depth the advantages and disadvantages of the approach. This understanding will help to deal with the problems which are new to Vietnamese insurance laws, but have been long discussed and tackled in English laws.⁵⁷⁸ If the legal right approach is adopted by other countries' insurance laws, similar problems will arise. It is necessary now to discuss the problems and recommend some better solutions to reform Vietnamese insurance laws in this area.

4.1. Preventing insureds from recovering their economic losses:⁵⁷⁹

From the point of view of indemnification, preventing insureds from recovering their actual economic losses is the most serious problem with the legal right approach, and makes it inconsistent with the principle of indemnity. The circumstances which clearly illustrate the problem will be critically analysed.

4.1.1. The interests of a shareholder:⁵⁸⁰

4.1.1.1. English law:

*Macaura v Northern Assurance Co*⁵⁸¹ is a typical example of the situation where a shareholder is prohibited from recovering. In this case the sole shareholder of a company, who was also a substantial creditor of the company, insured in his own name the timber

⁵⁷⁸ For example, the English experience in resolving the problems concerned with the co-insurance of complex construction project involving multiple contractors and sub-contractors is valuable for Vietnam laws.

⁵⁷⁹ ARLC 20, p72

⁵⁸⁰ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p63; F Rose, *Marine Insurance: Law and Practice*, (LLP, London, 2004), p43; J. Birds, "A shareholder's insurable interest in his company's property", (1987) J.B.L 309; D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p31; G. Salzman, "The law of insurable interest in property insurance", (1966) Ins.L.J 394, p401; R. McLeod, "*Aqua-Land Exploration Ltd. v. Guarantee Co. of North America et al.*: Insurable interest in an indemnity policy", (1966) 24 *U. of T. Fac. Law Rev.* 154; ARLC 20, p72; Pinzur, "Insurable interest: a search for consistency", (1979) 46 *Ins.Counsel J.* 109, p121; R. Hasson, "Reform of the law relating to insurable interest in property- some thoughts on *Chadwick v Gibraltar General Ins*" (1983-1984) 8 *Can Bus LJ* 114; C. Nicoll, "Insurable interest: as intended?" (2008) J.B.L 432; L. Stuesser, "Insurable interest: the Supreme Court of Canada adopts the factual expectancy test", (1987-1988) 13 *Can Bus LJ* 227

⁵⁸¹ [1925] A.C. 619

owned by the company. The House of Lords held that he had no insurable interest in the timber on the basis that a shareholder had no legal or equitable interest in the property owned by the company. The shareholder and the company were separate legal bodies.

The *Macaura*'s decision emphasized that, in order to show an insurable interest, the relation between the insured and the subject matter of insurance must be recognised by laws. If not, a shareholder has no insurable interest in corporate properties, or at any rate, cannot simply insure on the properties in his own name. This is too strict. The shareholder was denied an indemnity even though he had suffered an actual economic loss,⁵⁸² which is a departure from the principle of indemnity.

4.1.1.2. Vietnamese law:

In Vietnam, there is no reported case on this issue. There are two reasons for this: (i) only a few cases relating to insurable interest have been reported, and (ii) Vietnamese insurers always write down the name of the company on insurance policies as the insured or the beneficiary.⁵⁸³ Where the purchaser of insurance is different from the insured or the beneficiary, an authorisation letter from the company is required. If there is no such letter, the insurance contract is treated as invalid.⁵⁸⁴

Since Vietnamese courts make decisions according to statutory laws,⁵⁸⁵ in order to show how the courts deal with a case similar to *Macaura*, the provisions governing shareholder' interests should be examined here.

Article 3(9) of Law on Insurance Business 2000 lists the rights which may give an insured an insurable interest, including: right of ownership, right of possession, right of use, and

⁵⁸² J. Birds, "A shareholder's insurable interest in his company's property", (1987) J.B.L 309, p311

⁵⁸³ Under Vietnamese insurance laws, it is required to clearly draw a distinction between the person who takes out the policy and the person who get benefits under it. Article 3 of Law on Insurance Business 2000 provides that: "(6). **Purchaser of insurance** means an organization or individual entering into a contract of insurance with an insurer and paying an insurance premium. The purchaser of insurance may at the same time be the insured person or the beneficiary. (7). **Insured person** means an organization or individual having their property, civil liability or life insured in accordance with an insurance contract. The insured person may at the same time be the beneficiary."

⁵⁸⁴ Article 145 of Vietnam's Civil Code 2005: "*Consequences of civil transactions entered into and performed by unauthorized individuals*: (1). A civil transaction entered into and performed by an unauthorized individual shall not give rise to rights and obligations with respect to the principal, unless the representative or principal agree... (2). An individual who transacts with an unauthorized individual has the right to terminate unilaterally the performance of, or to rescind the civil transaction entered into and to demand compensation for any loss..."

⁵⁸⁵ See section 3.1.1 of Chapter 2

property right.⁵⁸⁶ To show an insurable interest, the relation between a shareholder and the company's property must fall within the list.

A shareholder and the company are different legal persons because the doctrine of separate legal personality is recognised under Vietnam's company laws.⁵⁸⁷ Article 38(1)(b) of Vietnam's Law on Enterprises 2005 stipulates that a shareholder is only liable for the debts and other property obligations of the company within the amount of capital that he has undertaken to contribute to it. The shareholder's properties, his responsibilities, and his liabilities are separate from those of the company. Therefore, the shareholder has no such right as listed in Article 3(9), having no insurable interest in the company's properties.

4.1.1.3. Is a shareholder entitled to the recovery?

Denying a sole shareholder recovery for his actual economic loss of the company's property has been seriously criticised by commentators. Pinzur asserts that the two rights of a shareholder, right to dividends and right to share in the final distribution of the corporate property, are clearly prejudiced by the destruction of or damage to the property of the company.⁵⁸⁸

Birds criticises the legal right approach for providing a technical defence to insurers, allowing them to escape their contractual liability.⁵⁸⁹ The insurers are the persons who have comprehensive knowledge of insurance laws, and should know that a shareholder has no right to insure against the risk of loss of corporate property in accordance with the legal requirement of insurable interest. At the time of entering into the insurance contract, they should explain this clearly to their customers. They only raise the issue in order to refuse to make payment when the loss occurs. If this technical defence is still available, some insurers

⁵⁸⁶ "Property rights" are defined in Article 181 of Vietnam's Civil Code 2005 as "rights which can be valued in terms of money and may be transferred in civil transactions, including intellectual property rights".

⁵⁸⁷ Article 38(1)(b) of Vietnam's Law on Enterprises 2005: "A member shall be liable for the debts and other property obligations of the enterprise within the amount of capital that it has undertaken to contribute to the enterprise". Article 63 of Vietnam's Law on Enterprises 2005: "A one member limited liability company is an enterprise owned by one organization or individual (hereinafter referred to as *company owner*); the company owner shall be liable for all debts and other property obligations of the company within the amount of the charter capital of the company."; see also article 77(1)(c), article 130(1)(c) of Vietnam's Law on Enterprises 2005

⁵⁸⁸ Pinzur, "Insurable interest: a search for consistency", (1979) 46 *Ins.Counsel J.* 109, p121, G. Salzman, "The law of insurable interest in property insurance", (1966) *Ins.L.J.* 394, p401; D. Rhidian Thomas stated that: "Although a shareholder does not have an insurable interest in the property of the company, ..., a shareholder does have an insurable interest in the value of his share and in the commercial adventures of the company", see D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p31

⁵⁸⁹ J. Birds, "A shareholder's insurable interest in his company's property", (1987) *J.B.L.* 309, p309

may issue more of this type of policy to get premiums, and then try to escape their liability in the event of loss. This puts insurers into a position of “gaining something or losing nothing”.

Not allowing a shareholder to take out insurance on his company’s properties only punishes small companies. The problem will not arise in large companies, which always have their own insurance. This problem only arises in relation to small companies, in which the shareholders may not have a thorough knowledge of insurance laws and therefore purchase insurance in their own name instead of the company’s name.

Allowing rather than disallowing a shareholder to recover brings greater social benefits to small companies,⁵⁹⁰ especially in Vietnam’s economy in which the majority of companies are small private companies: these companies, not state-owned companies, create the majority of jobs. If the loss of the company’s property occurs, insurance money will be very helpful in keeping such small companies in operation, and thereby helping employees keeping their jobs. If the insurance is denied, the shareholder may get into serious difficulties, may struggle to stay in business, or in the worst scenario, may lose his business entirely.⁵⁹¹

Meanwhile, there are a number of concerns about the consequences of allowing shareholders to take out insurance on corporate property. It is submitted that those consequences are not very serious in any case. First, admittedly, there is concern that allowing this practice may lead to uncertainty because too many policies might be issued on the same subject matter insured.⁵⁹² However, in such cases the principle of double insurance will intervene. This limits the insurers’ liability to the actual value of the insured property, and each insurer is only liable to pay for a proportion of the loss.

Second, a shareholder may take out an insurance policy with the sum insured above the valuation of his own interest. If he does so, the principle of indemnity will intervene. He must hold the amount in excess of his own interest on trust for the company or other shareholders.

⁵⁹⁰ L. Stuesser, “Insurable interest: the Supreme Court of Canada adopts the factual expectancy test”, (1987-1988) 13 Can Bus LJ 227, p236

⁵⁹¹ Mr Kosmopoulos, a sole owner of his leather goods business in *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208 shut down his company because of 10 year litigation, although he eventually won the case; see L. Stuesser, “Insurable interest: the Supreme Court of Canada adopts the factual expectancy test”, (1987-1988) 13 Can Bus LJ 227, p238

⁵⁹² Per Lord Eldon in *Lucena v Craufurd* [1806] 2 Bos. & P.N.R. 269; 127 E.R. 630, p651-652: “If moral certainty be a ground of insurable interest, there are hundreds, perhaps thousands, who would be entitled to insure. First the dock company, then the dock-master, then the warehouse-keeper, then the porter, then every other person who to a moral certainty would have anything to do with the property, and of course get something by it.”

Third, there is concern that allowing such a practice would increase wagering in the guise of insurance.⁵⁹³ However, if a shareholder can prove his actual economic loss, it is not a wager at all.⁵⁹⁴

Fourth, a shareholder may purchase insurance with the intention of obtaining unfair benefit from it at the expense of other shareholders or creditors of the company. However, company laws contain sufficient provisions and remedies to prevent the shareholder from obtaining the unfair benefit.⁵⁹⁵ For example, the corporate veil will be lifted to protect the interests of third parties.⁵⁹⁶

As to the insurable interest of a shareholder, the legal right approach is too harsh to the insured shareholders and departs from the principle of indemnity. In other jurisdictions, a shareholder is granted an insurable interest in corporate property. For example, in America, the overwhelming majority of cases hold that a shareholder has an insurable interest in the property of the company.⁵⁹⁷ The issue of difficulties of valuating interests of a shareholder has been proved not severe.⁵⁹⁸ In a modern economy, the value of shares can be calculated on the stock market. The Supreme Court of Canada, in *Constitution Ins. Co. of Canada v Kosmopoulos*,⁵⁹⁹ where the facts were indistinguishable from those in *Marauca*, followed the

⁵⁹³ Per Lord Eldon in *Lucena v Craufurd* [1806] 2 Bos. & P.N.R. 269

⁵⁹⁴ Per Wilson J. in *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R. 208; J. Birds, “A shareholder’s insurable interest in his company’s property”, (1987) J.B.L. 309, p311

⁵⁹⁵ J. Birds, “A shareholder’s insurable interest in his company’s property”, (1987) J.B.L. 309, p311

⁵⁹⁶ Per Wilson J. in *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R. 208

⁵⁹⁷ *Riggs v Commercial Mutual Insurance Co* [1890] 125 N.Y. 7; 25 N.E. 1058; *Liverpool and London and Globe v Bolling* [1940] 10 S.E. 2d 578; *Pacific National Fire Insurance Co. v Watts* [1957] 97 So.2d 797; *Van Cure v Hartford Fire Insurance Co.* [1969] 253 A.2d 663; *Royal Insurance Co v Sisters of the Presentation* [1970] 430 F.2d 759

⁵⁹⁸ Lord Buckmaster in *Macaura v Northern Assurance Co.* [1925] A.C. 619, p627, said: “If he [the shareholder] were at liberty to effect an insurance against loss by fire of any item of the company’s property, the extent of his insurable interest could only be measured by determining the extent to which his share in the ultimate distribution would be diminished by the loss of the asset- a calculation almost impossible to make. There is no means by which such an interest can be definitely measured and no standard which can be fixed of the loss against which the contract of insurance could be regarded as an indemnity.” However, in *Wilson v Jones* [1867] L.R. 2 Ex 139, English court granted the shareholder an insurable interest based on an interest in the adventure of the corporation.

⁵⁹⁹ [1987] 304 D.L.R. 4th 208. The facts of the case, in brief, were that Mr Kosmopoulos was a sole owner of a small business on leather goods. On the advice of his solicitor, Mr. Kosmopoulos incorporated a company, Kosmopoulos Leather Goods Ltd, and he was sole shareholder and director of the company. He obtained insurance for the business in his own name through an insurance agent. The leather store was damaged by fire, water and smoke. The insurers denied coverage and the primary issue to be resolved was whether Mr Kosmopoulos had an insurable interest in the company’s property. Wilson J., who gave the majority judgment, made a valuable review of the relevant history of the law of insurable interest in property and examined the three policies underlying the requirement of insurable interest, namely: the policy against wagering under the guise of insurance, the policy to prevent temptation to destroy the insured property, and the policy favouring limitation of indemnity. Consequently, it was held that the shareholder had an insurable interest in the company’s property.

American decisions and refused to follow any longer the decision in *Marauca*. The court reached its decision by adopting a broad view of the requirement of insurable interest (the factual expectation approach).⁶⁰⁰

To conclude, the legal right approach has prevented a shareholder from recovering for his actual economic loss, which is inconsistent with the principle of indemnity. In accordance with the principle of indemnity, an insured should be fully indemnified or compensated for his actual economic loss, but no more than his actual loss. It has been proved that not allowing a shareholder to take out insurance on corporate property is not suitable to modern economic activities, and allowing a shareholder to do so does not raise any serious problem, either for insurance laws or for commercial practices.

4.1.2. Insurable interest of a FOB or C&F buyer:

In marine insurance, the legal right approach prevents FOB or C&F buyers from recovery for the loss of goods before shipment, although they have taken out insurance covering the risk of the loss.⁶⁰¹

In a simple international contract for sale of goods, the seller transports the goods to the port of loading, and hands them over to the carrier; then the carrier carries the goods to the port of discharge and delivers to the buyer. However, in the context of modern international transport of goods, the goods may leave the seller's hands earlier and reach to the buyer's hands later. They may be handed over to the carrier at the seller's inland warehouse, and delivered at the buyer's inland warehouse.

The FOB or C&F buyers take out insurance covering the whole transit- a warehouse to warehouse clause. During the voyage from the seller's warehouse to the port of loading, the goods may be destroyed or damaged or stolen. In the buyers' opinion, they are entitled to recover for the loss. However, in accordance with the legal right approach, they are not entitled to do so.

⁶⁰⁰ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p59-60

⁶⁰¹ H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p81; ALRC Discussion Paper 63, at 7.19, 7.25, 7.27, 7.30, see also ALRC Report 91, at 11.59; M. Taylor, "Is the requirement of an insurable interest in the Marine Insurance Act still valid", (2000) 11 *Ins. L.J* 1; *Iglis v Stock* [1885] 10 App Cas 263; *Colonial Ins. Co of New Zealand v Adelaide Marine Ins. Co.* [1886] 12 App. Cas. 128; *Anderson v Morrice* [1875] All ER Rep Ext 2066

Under the FOB or C&F terms, the risk prior to shipment remains with the sellers.⁶⁰² Since the risk has not passed to the buyers, the buyers have no legal or equitable relation to the goods at the time of loss.⁶⁰³ Consequently, they have no insurable interest in them as required by the legal right approach, and their claim against the insurers is invalid.

It may be argued that, since the risk of loss of goods prior to shipment still remains with the sellers, they must bear the loss. If the buyers have made the payment for the price of goods in advance, they must take an action against the sellers to recover their payment. Nonetheless, if the sellers are insolvent or have financial difficulties, the buyers with the insurance policy in their hands cannot get their money back from either the insurers or the sellers. They have suffered an actual economic loss, but it is not sufficient to constitute an insurable interest as required by the legal right approach. The “warehouse to warehouse” clause in the policy does not provide them the protection for which they intended to seek at the time of inception. On the other hand, the insurers, who have offered the protection from “warehouse to warehouse”, are able to get the premiums and refuse to fulfil their contractual promises, escaping from their contractual obligation.

This brings up the question of how FOB or C&F buyers, who have an insurance policy with a warehouse to warehouse clause, get financial protection against the risk of loss of the goods prior shipment. There are two options available to them: (i) add a “lost or not lost” clause to the policy, or (ii) use a “FOB or C&F pre-shipment” clause. However, both of the clauses are in breach of the legal requirement of insurable interest. The problems relating to “warehouse to warehouse”, “lost or not lost”, and the “FOB or C&F pre-shipment” clause are critically analysed in turn.

4.1.2.1. Current Vietnamese and English rules on FOB or C&F buyers’ insurable interest in the goods during the voyage from the sellers’ warehouse to the ship’s rail

Under both current Vietnamese and English laws on marine insurance, FOB buyers have no insurable interest in the goods prior to shipment because the risk of loss of the goods has not

⁶⁰² The risk passes from the sellers to the buyers when the goods have passed the ship’s rail at the port of loading, see Incoterm 2010.

⁶⁰³ *Fuerst Day Lawson v Orion Ins* [1980] 1 Lloyd’s Rep 656

passed to them at that time- they have no legal or equitable relation to the goods as required by statutory laws.⁶⁰⁴

In an English case, *Fuerst Day Lawson v Orion Ins*,⁶⁰⁵ the C&F buyer insured a cargo of scented oil in drums with his insurer under an all risks policy with a warehouse to warehouse clause. The cargo was substituted with water before shipment. On discharge, it was discovered that the drums contained water, with a thin film of oil for deception purposes. The insured made a claim to recover for his loss. It was held that the insured had no insurable interest.

Similarly, in the Vietnamese case of *Thai Duyen Trading & Transport Co. v AIG Vietnam*,⁶⁰⁶ the insurance contract stipulated that the voyage to be covered was from the seller's inland warehouse in Singapore to Haiphong port. A container of malt was lost during loading at Singapore port, before it passed the ship's rail. It was held that the insured was not entitled to recover for his loss because the risk of loss had not passed to him.

It is clear that FOB or C&F buyers, who have made in advance the payment for the price of the goods, will suffer an economic loss when the goods are damaged or destroyed before shipment, and the sellers are insolvent and unable to pay back the payment. The "warehouse to warehouse" clause does not provide the financial protection they need. Their claim will be rejected only because they have no legal interest in the goods before shipment. On the other hand, the insurers, who issue an insurance cover with the "warehouse to warehouse" clause, are able to retain the premiums and escape their contractual liability in the event of loss.

*4.1.2.2. Does the "lost or not lost" clause give the FOB or C&F buyers the financial protection they need?*⁶⁰⁷

An Australian case highlighted the problems relating to a FOB or C&F buyer's insurable interest in the goods prior to shipment. It showed that the buyer is uninsured against the loss of the goods prior to loading, unless he takes out a policy containing both a "warehouse to

⁶⁰⁴ See section 5 of MIA 1906; article 226 of Vietnam's Maritime Code 2005; article 22 of Vietnam's Law on Insurance Business 2000

⁶⁰⁵ [1980] 1 Lloyd's Rep 656; see also: *Anderson v Morice* [1875] L.R. 10 C.P. 609; *Piper v Royal Exchange Assurance* [1932] 44 Lloyd's Rep 103; ALRC Report 91, para 11.19; ALRC Discussion Paper 63, para. 7.17; S Hodges, *Cases and Materials on Marine Insurance Law*, (Cavendish Publishing Limited, London, 1999), p55-56; Lorenzon, F. and Baatz, Y., *CIF and FOB contracts*, (5th edn, Sweet & Maxwell, London, 2012), p189

⁶⁰⁶ [2006] at Haiphong's People Court

⁶⁰⁷ H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p71

warehouse” clause and a “lost or not lost” clause,⁶⁰⁸ and that neither the “warehouse to warehouse” policy nor the “lost or not lost” clause in isolation is sufficient to give the buyer on FOB or C&F terms an insurable interest.⁶⁰⁹

In *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd*,⁶¹⁰ the insured had an insurance policy for consignments of leather that he had purchased on FOB terms from some suppliers. The goods were loaded in containers but most of them were stolen before the containers were loaded on board the ship and fresh seals were fraudulently attached to the containers. The buyer had made payment for the goods before shipment. The insurance policy contained a “warehouse to warehouse” clause and a “lost or not lost” clause. The insurers denied the buyer’s claim on the grounds that the insured did not have an insurable interest at the time of loss.

Neither the “warehouse to warehouse” policy nor “lost or not lost” clause in isolation is sufficient to give the FOB buyer an insurable interest.

In accordance with the legal right approach, an insured buyer on FOB terms does not have an insurable interest in the goods during transit from the seller’s warehouse to the port of loading, since the risk has not passed yet.

Although there was a “warehouse to warehouse” clause in the policy, the clause could not operate to extend the cover to an earlier point in time in the absence of an insurable interest.⁶¹¹ The insurer was not under any duty to indemnify the insured where the risk in the goods had not passed to the insured.⁶¹²

Similarly, the “lost or not lost” clause alone could not protect the insured where the loss occurs before shipment. The loss of the goods prior to shipment did not fall on the insured, it fell on the seller. It is a rule that the insurers’ liability only arises if the insured buyer has suffered a loss. The insured had no interest in the goods prior to loading, so he suffered no

⁶⁰⁸ M. Taylor, “Is the requirement of an insurable interest in the Marine Insurance Act still valid”, (2000) 11 Ins. L.J 1, p3

⁶⁰⁹ ALRC Report 91, at 11.42; see also M. Taylor, “Is the requirement of an insurable interest in the Marine Insurance Act still valid”, (2000) 11 Ins. L.J 1, p 8-11

⁶¹⁰ [1991] 25 NSWLR 699

⁶¹¹ *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* [1990] 103 FLR 70, p89

⁶¹² *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* [1990] 103 FLR 70, p88; ALRC Discussion Paper 63, at 7.24

loss by their disappearance. The buyer had to recover the purchase price from the sellers, not from the insurers.⁶¹³

If, however, the “warehouse to warehouse” clause and “lost or not lost” clause work together, it would be sufficient to give a FOB or C&F buyer protection. This is an exception to the requirement that, in marine insurance, an insured must have an insurable interest at the time of loss. This allows an insured to recover for the loss of the goods, although he may not have acquired an interest until after the loss.⁶¹⁴

The Australian Court of Appeal held that the insured was able to recover, relying on the combination of the “lost or not lost” clause and the “warehouse to warehouse” clause in the policy. It stated that the insured had suffered a loss even though the insured did not bear the risk when the goods were stolen. It was sufficient that the insured suffered financial loss- the loss of the goods prior to shipment. The fact that the buyer had contractual remedies against the seller did not prevent him from claiming on his policy.⁶¹⁵

Although it was fair to allow the FOB buyer to recover for his loss (based on the factual expectation approach), it is clear that the ground for the court’s decision was against the legal right approach. The buyer had no legal or equitable relation to the cargo before shipment, so he had no insurable interest as required by the legal right approach. It also shows the fact that where there is a commercial need for a certain type of insurance, the parties to an insurance contract may attempt to find the way out of the legal requirement of insurable interest.

Is the combination of “warehouse to warehouse” clause and “lost or not lost” clause the best solution to protect FOB or C&F buyers?

Although both of the clauses are incorporated into the insurance contract, FOB or C&F buyers may still be denied the recovery for the loss of goods before shipment in the two following circumstances.

⁶¹³ *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* [1990] 103 FLR 70, p88; ALRC Discussion Paper 63, at 7.25

⁶¹⁴ Section 6 of MIA 1906; article 226(3) of Vietnam’s Maritime Code 2005; section 12 of MIA 1909 (Australia)

⁶¹⁵ *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* [1991] 25 NSWLR 699, p711; ALRC Discussion Paper 63, at 7.27

First, the “lost or not lost” clause does not operate if the insureds never acquire an insurable interest in any of the goods.⁶¹⁶ Under Article 226(3) of Vietnam’s Maritime Code 2005, it is implied that, in order to make a valid claim according to the “lost or not lost” clause, the insureds are required to obtain an insurable interest after the loss of the goods occurs.⁶¹⁷ The article provides that: “where the subject-matter is insured under the ‘lost or not lost’ condition, the assured may recover although he may not have acquired his interest until after the loss, unless the assured was aware of the loss, and the insurer was not.” Where the goods have been totally destroyed, or the loss of the goods may frustrate the contract of sale in accordance with its terms,⁶¹⁸ or the goods that were insured have been fraudulently substituted by other goods, and consequently, the goods which were insured are never shipped, the insured buyers will never obtain an insurable interest in the insured goods. Therefore, the insurers are still able to refuse to indemnify the insureds for their losses.

An example of the above-mentioned situation can be shown by the English case of *Fuerst Day Lawson v Orion Ins.*⁶¹⁹ In this case, the “lost or not lost” clause could not assist the insureds in making a valid claim against the insurers. The reason for this is that the goods which were shipped were not the goods which were insured, and therefore, the risk under the policy never attached.

Second, radical differences in understanding the meaning and the scope of the “lost or not lost” clause may prevent buyers’ recovery. The reasons for this are that, under Vietnamese insurance law, there is no clear explanation about the meaning and the scope of the clause, and that Vietnamese insurers do not often offer a policy with a “lost or not lost” clause.

In commercial practice, Vietnamese insurers’ common understanding and usage of the clause is that the clause is applied in the situation that before the contract of insurance is concluded, the loss of the goods, which were unknown to both insurers and insureds, has occurred, and then the insureds would acquire an insurable interest in the goods after the loss. In addition, the clause is commonly applied when the goods, which have been lost during the voyage at

⁶¹⁶ALRC Report 91, para 11.41-11.42, p8

⁶¹⁷Article 226(3) of Vietnam’s Maritime Code 2005: “The assured must have interest in the subject-matter insured at the time of occurrence of the loss though he need not be interested when the insurance is effected. Where the subject-matter is insured under the ‘lost or not lost’ condition, the assured may recover although he may not have acquired his interest until after the loss, unless the assured was aware of the loss, and the insurer was not.”

⁶¹⁸ *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* [1991] 25 NSWLR 699; S Hodges, *Cases and Materials on Marine Insurance Law*, (Cavendish Publishing Limited, London, 2012), p80

⁶¹⁹ [1980] 1 Lloyd’s Rep 656; this case has been discussed above at

sea, are resold from one buyer to another buyer, and the first buyer in the chain has acquired an insurable interest in the goods.⁶²⁰

According to Vietnamese insurers, this situation is stipulated in article 226(3) of Vietnam's Maritime Code 2005 and clause 11 of Institute Cargo Clauses 1982 or 2009.⁶²¹ Those clauses are used for marine cargo insurance by a number of the Vietnamese insurers.⁶²² Moreover, in their opinion, this understanding is in conformity with English law and practices which govern the Institute Cargo Clauses.

The second situation in which the clause operates may be unfamiliar to Vietnamese insurers. The contract of insurance is concluded before the occurrence of the loss, and the loss occurs before the insurable interest passes to the insureds, but it subsequently does pass.⁶²³ This is the vulnerable situation that the FOB or C&F buyers are placed in. Almost all of the Vietnamese insurers believe that they do not intend to offer a policy covering the risk of loss of goods prior to shipment because the buyers have no insurable interest in the goods at that time.

Indeed, it should be noted that the "lost or not lost" clause operates in both of the two situations.⁶²⁴ The differences in understanding the meaning and the scope of the clause put obstacles in the way of FOB or C&F buyers trying to recover the loss of the goods before shipment.

⁶²⁰ Tran Trong Khoai, Doan Vu Huong, *Giao trinh Bao hiem*, (NXB Giao duc, 2008) [Trans: Tran Trong Khoai, Doan Vu Huong, *Textbook on insurance*, (Education Publishing House, 2008)], p192; Nguyen Van Dinh, *Giao trinh Bao hiem*, (NXB Dai hoc Kinh te quoc dan, 2006) [Trans: Nguyen Van Dinh, *Textbook on Insurance*, (Publisher of National Economics University, 2006)], p393; see also *Mead v Davison* [1835] 3 A&E 303; *Sutherland v Pratt* [1843] 11 M&W 296; S Hodges, *Law of Marine Insurance*, (Cavendish Publishing Limited, London, 1996), p21; M. Taylor, "Is the requirement of an insurable interest in the Marine Insurance Act still valid", (2000) 11 Ins. L.J 1, p9; ALRC Report 91, para. 11.38 p8

⁶²¹ Clause 11 of Institute Cargo Clauses: "(11.1) In order to recover under this insurance the Assured must have an insurable interest in the subject-matter insured at the time of the loss. (11.2) Subject to 11.1 above, the Assured shall be entitled to recover for insured loss occurring during the period covered by this insurance, notwithstanding that the loss occurred before the contract of insurance was concluded, unless the Assured were aware of the loss and the Underwriters were not."

⁶²² Bao Viet, Bao Minh, PVI, PJICO, Vien Dong, Bao hiem Nha Rong, PTI, BIC, MIC, VNA-Insurance, SVIC

⁶²³ M. Taylor, "Is the requirement of an insurable interest in the Marine Insurance Act still valid", (2000) 11 Ins. L.J 1, p9; ALRC Report 91, para. 11.38 p8

⁶²⁴ The clause assists the FOB or C&F buyers only where: (1) the loss occurs before the contract of insurance is concluded but after the risk or insurable interest has passed to the insured or (2) the loss occurs before the insurable interest passes to the insured but it subsequently does pass; see also M. Taylor, "Is the requirement of an insurable interest in the Marine Insurance Act still valid", (2000) 11 Ins. L.J 1, p9; ALRC Report 91, para. 11.38 - p8; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p71-72

4.1.2.3. Does the “FOB or C&F pre-shipment” clause protect the FOB or C&F buyers?

In Australia, in order to offer the FOB or C&F buyers insurance against the risk of loss of the goods before shipment, marine insurers issue a standard pre-shipment cover which is called “FOB/ C&F Pre-shipment Clause.”⁶²⁵

The pre-shipment clause overcomes some of the problems that arise out of the combination of the “warehouse to warehouse” and “lost or not lost” clause. First, it does not depend on the terms of the contract of sale; thus, passing of risk or passing of property has no impact on application of the clause.⁶²⁶ Second, it attaches from the beginning of the transit, which is similar to the “warehouse to warehouse” clause.⁶²⁷ Therefore, there is no need to identify the time when the loss occurs, and the insurers are not able to refuse to make a payment on the ground that the loss occurs before shipment and the insureds have no insurable interest at that time. Third, it is not dependent upon whether or not the insureds subsequently acquire an insurable interest after the loss of the goods occurs.⁶²⁸

However, there is a grave problem with the pre-shipment clause.⁶²⁹ It does not have a statutory basis like the “lost or not lost” clause. The clause is considered as commercially rather than legally enforceable against the insurers because it is in breach of the statutory requirement of insurable interest.⁶³⁰ Therefore, it is open for courts to declare the policies with the clause null and void.

⁶²⁵ Such clauses are often in the following terms: “Notwithstanding the provisions of the contract of sale where the Interest Insured is purchased on FOB, C&F or similar basis, this insurance attaches from the time the Interest Insured **leaves the warehouse or place of storage for the commencement of transit**. If loss or damage occurs which is payable under this Clause, the Assured agrees to **use all reasonable means to first recover the full amount of loss or damage from the exporter or supplier** in accordance with the terms of purchase, **before calling on this policy for payment**. The underwriters are entitled to become subrogated to the Assured’s rights of recourse against the exporter or suppliers.” This policy is issued by Associated Marine Insurers Agents Pty Ltd

⁶²⁶ ALRC Report 91, para. 11.41-11.47

⁶²⁷ *Ibid*

⁶²⁸ *Ibid*

⁶²⁹ For other problems with the pre-shipment clause, such as ambiguity about when the policy with pre-shipment clause first attaches, and the extent of the insureds’ obligation to use all reasonable means to first recover from the sellers before making a claim under the policy, see M. Taylor, “Is the requirement of an insurable interest in the Marine Insurance Act still valid”, (2000) 11 *Ins. L.J* 1, p10-11

⁶³⁰ ALRC Report 91, para.11.47, p9

4.1.2.4. Should the FOB or C&F buyers and the insurers be free to negotiate on insurance against the risk of loss of the goods before shipment?

There are four arguments for the greater freedom of the FOB or C&F buyers and the insurers to enter into an insurance contract covering the risk of loss of the goods prior to shipment.

Firstly, the parties to an insurance contract should be entitled to contract in such a way as to cut the connection between cover for pre-shipment loss and the passing of risk or passing of property under the contract of sale, if this is commercially desirable.⁶³¹

Indeed, there is such a demand because cargo theft is on the rise worldwide.⁶³² Vietnam has also seen an increase in cargo theft.⁶³³ In Vietnam, this crime normally involves insiders' knowledge and collusion, either with the drivers or others in the trucking or logistics companies. A recent case in point is that truck-drivers work in collusion with thieves to cut the backs of container without breaking the carrier's seals.⁶³⁴ On the other hand, the fact that insurers are willing to issue cover against the risk of loss prior to shipment is strong evidence of the market demand. In addition, there is no convincing reason why FOB or C&F buyers should be prevented from insuring against pre-shipment losses.⁶³⁵

It is submitted that where the parties precisely intend to extend the cover for the risk of loss from warehouse to warehouse in their contract, the freedom of contract should be the first factor to be considered, and the parties should be allowed to do so. Moreover, when a "warehouse to warehouse" clause is stipulated in an insurance policy, it is logical to assume that the period of cover is from the seller's warehouse to the buyer's warehouse, and if there is a loss of the goods during that voyage, the insureds should be indemnified. The insurers should be well aware of the possibility of the loss occurring between the seller's warehouse and the port of loading; and, at the time of entering into the contract, they should know that the FOB buyer has no insurable interest in the goods before they are shipped on board the

⁶³¹ ALRC Report 91, para.11.39, p8

⁶³² <http://wrin.tv/index.php/component/content/article/3-headline/288-freightwatch-says-cargo-theft-is-on-the-rise> accessed on 1st January 2013; see also: "FreightWatch International: Global Threat Assessment" (21st February 2011)

⁶³³ "Bung phat an cap hang trong container xuat khau" [Trans: "An outbreak of cargo theft from containers"] available at <<http://www.thanhvien.com.vn/pages/20130111/bung-phat-an-cap-hang-trong-container-xuat-khau.aspx>>; "Nhom 'rut ruot' container sa luoi" [Trans: "Gangs of cargo theft from containers arrested"] available at <<http://www.anninhthudo.vn/An-ninh-doi-song/Nhom-rut-ruot-container-sa-luoi/320306.antd>>

⁶³⁴ "Thu doan trom tai san trong container" [Trans: "Tricks relating to cargo theft from containers"] available at <<http://www.thanhvien.com.vn/pages/20121117/thu-doan-trom-tai-san-trong-container.aspx>>

⁶³⁵ ALRC Report 91, para.11.65, p12

carrying vessel. It is unfair to the inexperienced insureds if they are refused recovery for their actual financial loss because of the narrow interpretation of the concept of insurable interest. Indeed, preventing the FOB buyers from recovering is a departure from the principle of indemnity. It is submitted that the insurers should be bound by what they have agreed in the contract.

If insurers take the view that the risk of loss prior to loading is high, they can increase premiums in order to take the risk, i.e., higher premiums for greater liability. If the insurers do not wish to provide cover for the loss prior to shipment, they are free to choose not to do so.⁶³⁶ The availability and the cost of the cover for loss before shipment will be determined by the insurance markets.⁶³⁷ However, whenever they agree to provide the cover, they should not be allowed to escape their contractual obligation.

Secondly, it is sometimes difficult to identify when and where loss of, or damage to, the goods occurs,⁶³⁸ particularly with containerisation in transportation of goods. There are two reasons for this: (i) several individuals are involved in the handling process after the goods leave the sellers' hands, and the goods often pass through numerous transit entities prior to shipment. Therefore, there is a big time gap between the time the goods leave the sellers' hands and the time when they pass the ship's rail;⁶³⁹ and (ii) where the goods are transported in containers, the buyers have little or no opportunity to inspect the goods prior to shipment because the containers are already sealed.⁶⁴⁰ The contents of the containers cannot be seen. The buyers only get a chance to inspect the goods and discover the loss when they reach the destination port. At that time, it is certain that the buyers have suffered an actual economic loss, but it is uncertain as to why, and how, and when the loss occurred. Therefore, it is difficult to ascertain whether the FOB buyer insureds have an insurable interest in the cargo at the time of loss. In addition, having an insurable interest is a statutory requirement that must be fulfilled in order to make a valid claim against the insurers. It is suggested that if this statutory requirement is abolished, these practical difficulties in identifying when and where the loss occurs also vanishes because the insureds are no longer required to do so.

⁶³⁶ ALRC Report 91, at 11.93

⁶³⁷ ALRC Report 91, para. 11.39, p8

⁶³⁸ ALRC Discussion Paper 63, para. 7.15 and para.7.19-7.20 p4

⁶³⁹ D. Galbraith, "An Unmeritorious Defence – The Requirement of Insurable Interest in the Law of Marine Insurance and Related Matters" (1992) 5(3) *Ins LJ* 177, 181; ALRC Discussion Paper 63, para. 7.20, p4

⁶⁴⁰ M. Taylor, "Is the requirement of an insurable interest in the Marine Insurance Act still valid", (2000) 11 *Ins. L.J* 1, p13

Thirdly, it may be argued that the FOB or C&F buyers should take an action against the sellers to recover for their loss in accordance with the contract of sale, and it is not the insurers who have to pay.⁶⁴¹ However, the idea behind insurance policies covering pre-shipment loss is to give the insured the choice of making a claim against either the sellers or the insurers when it is not clear at what point in time the loss has occurred.⁶⁴² It is most unfortunate for the FOB buyers when they cannot recover from the sellers because the sellers are insolvent, nor can they recover from the insurers simply because the requirement of insurable interest is not strictly satisfied.⁶⁴³ In this scenario, insurance does not play its important roles, that of indemnifying the insureds for their actual economic loss and helping them to secure financial stability to maintain their business.

In addition, recovering from the sellers is not an easy job, especially in a situation where the buyers have to bring an action to a court in a foreign country. There are several difficulties, for example, contractual remedies against the sellers are subject to conflicting authorities, and the applicable laws to the dispute may be different from the laws with which they are familiar in their home country.⁶⁴⁴

Furthermore, after indemnifying the insureds, the insurers still have a right to subrogate against the sellers to recover for what they have paid. Any remedies available to the buyers against the sellers or the carriers are also available to the subrogated insurers.⁶⁴⁵

Fourthly, it may be argued that, in order to avoid the risk of loss prior shipment, the FOB or C&F buyers can delay their payment until the complete cargo has passed the ship's rail. However, it should be noted that buyers may have limited leverage to negotiate that the payment should be delayed after shipment,⁶⁴⁶ particularly with those from a relatively small importation market on the international scale, like Vietnam.

⁶⁴¹ ALRC Report 91, at 11.78

⁶⁴² H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p?; ALRC Report 91, at 11.45

⁶⁴³ H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p?

⁶⁴⁴ For discussion in more details on problems of recovery of the FOB or C&F buyers from the sellers or the carriers, see M. Taylor, "Is the requirement of an insurable interest in the Marine Insurance Act still valid", (2000) 11 Ins. L.J 1, p15-20

⁶⁴⁵ ALRC Report 91, at 11.64

⁶⁴⁶ M. Taylor, "Is the requirement of an insurable interest in the Marine Insurance Act still valid", (2000) 11 Ins. L.J 1, p13

Alternatively, it is argued that the buyers should negotiate different terms in the contract for sale of goods⁶⁴⁷ in which the sellers are under a duty to take out an insurance policy against the buyer's risk of loss of the goods during carriage. Therefore, where the goods are damaged or lost before reaching the destination port, the buyers can recover under the sellers' policy.⁶⁴⁸ However, in industries where competition is very intense, the FOB terms are preferable. The buyers can save considerable costs and, more importantly, they have more flexibility to arrange and negotiate their own terms of insurance and carriage contracts. In addition, there are important national economic reasons to encourage Vietnamese importers to arrange insurance with their domestic insurers.

In conclusion, the legal right approach puts legal obstacles in the way of the FOB or C&F buyers trying to recover for the loss of goods prior to shipment. Although a combination of the "lost or not lost" clause and the "warehouse to warehouse" clause can give the buyers a chance to recover for the loss, it creates confusion and technical difficulties for inexperienced insureds, and it is not clear whether or not the buyers are entitled to a recovery if the goods are totally destroyed or lost or stolen.

It is suggested that those obstacles should be removed. The underlying purpose of an insurance bargain is that the insureds should be indemnified for their actual loss, and the insurer should keep his promise to pay when the loss occurs. It is unfair to the insureds if the insurer is allowed to use his technical defence to refuse to pay when the loss which has been specified in the policy occurs.

4.1.3. Insurable interest of an unsecured creditor:⁶⁴⁹

As a general rule, a secured creditor has an insurable interest in the property of his debtor, which is used as security for the debtor's loan, to the extent of the debt charged on it.⁶⁵⁰ In

⁶⁴⁷ For example: "CIF", "CIP", "DDU", "DDP" in ICC Incoterms 2010

⁶⁴⁸ For more details on problems with indemnity under the seller's policy, see M. Taylor, "Is the requirement of an insurable interest in the Marine Insurance Act still valid", (2000) 11 Ins. L.J 1, p11-13

⁶⁴⁹ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p78-79; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p84; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p165; Pinzur, "Insurable interest: a search for consistency", (1979) 46 Ins.Counsel J. 109, p119; J. Stockton, "An analysis of insurable interest under article two of the Uniform Commercial Code", (1963-1964) 17 Vand. L. Rev 815, p826; R. Hasson, "Reform of the law relating to insurable interest in property- some thoughts on *Chadwick v Gibraltar General Ins*" (1983-1984) 8 Can Bus LJ 114, p117

⁶⁵⁰ Section 14(1) of MIA 1906 provides that: "Where the subject-matter insured is mortgaged, the mortgagor has an insurable interest in the full value thereof, and the mortgagee has an insurable interest in respect of any sum due or to become due under the mortgage."; see also: *Irving v Richardson* [1831] 2 B&Ad 193

contrast, an unsecured creditor has no insurable interest in his debtor's property,⁶⁵¹ even though the loss of it may diminish his chance of obtaining the balance of the debt. According to the legal right approach, an unsecured creditor's interest is merely an expectation of repayment; and therefore, his interest is too remote and too uncertain to make it insurable.⁶⁵² It is submitted that this is another example of the situation that the legal right approach denies insureds the recovery for their actual economic losses.

4.1.3.1. Current English and Vietnamese rules on insurable interest of an unsecured creditor

In accordance with the legal right, an unsecured creditor does not have a sufficient insurable interest in the debtor's property. He has no legal or equitable relation to, or any legal liability arising from, the debtor's property. Once again, *Macaura v Northern Assurance Co*⁶⁵³ is an outstanding example of the absurdity of the application of the "legal right" approach. The insured, who was a sole owner of the company and was also a substantial creditor of the company, insured in his own name timber owned by the company. It was held that he had no right to the company's property in the sense of a mortgage or charge over it or some other proprietary security interest, and therefore he could not recover the loss under the policy. This view is considered too narrow.⁶⁵⁴ The creditor could not even recover the loss of the debt that the company owed him.

In Vietnamese law, there is no provision that gives any detailed rule on insurable interest of an unsecured creditor. There is only a provision relating to the mortgage of insured property in the Vietnamese Civil Code 2005.⁶⁵⁵ However, it can be said that an unsecured creditor has no insurable interest in his debtor's property under Vietnamese insurance laws because he has no right, which may give an insurable interest, as listed in article 3(9) of Vietnam's Law on Insurance Business 2000.

⁶⁵¹ *Moran, Galloway & Co v Uzielli* [1905] 2 KB 555, 562; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p83

⁶⁵² *Wilson v Jones* [1867] L.R. 2 Ex 139; *Moran, Galloway & Co v Uzielli* [1905] 2 KB 555; *Macaura v Northern Assurance Co.* [1925] A.C. 619; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p78-79

⁶⁵³ [1925] A.C. 619

⁶⁵⁴ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p59

⁶⁵⁵ Article 346 of Vietnam's Civil Code 2005: "*Mortgages of insured property*: (1). Where mortgaged property is insured, the insured sum shall also form part of the mortgaged property. (2). The mortgagee must notify the insurer that the insured property is being mortgaged. The insurer shall pay the insured sum directly to the mortgagee on occurrence of an insured event. If the mortgagee failed to notify the insurer that the insured property was mortgaged, the insurer shall pay the insured sum in accordance with the insurance contract and the mortgagor shall be obliged to make payment to the mortgagee."

4.1.3.2. Australian and Canadian approaches to insurable interests of an unsecured creditor:

Marauca is not the only case which illustrates the unfairness to unsecured creditors and the departure from the principle of indemnity when applying the “legal right” approach. It should be noted that the rules on insurable interest of an unsecured creditor have been changed to the factual expectation approach under Australian and Canadian laws. Nevertheless, some old cases should be discussed to show the excessive rigidity of the legal right approach.

In an Australian case,⁶⁵⁶ a creditor wished to buy a property of his debtor, and it was arranged between them that certain sums of money which were lent to the debtor in connection with maintenance of the property were to be deducted from whatever price would be eventually agreed upon. As the debtor could not afford to insure the property, the creditor took out a policy in his own name. The property was damaged by fire. The creditor made a claim against his insurer but it was rejected on the ground that the creditor had no insurable interest in the property owned by the debtor.

It is suggested that it was totally inequitable to the insured where he could not even rely on the policy to recover the amount equivalent to sums which he had actually spent on the maintenance of the property. An unsecured creditor should have an insurable interest in the property of the debtor because he has an expectation of benefit from the continued existence of the debtor’s property.⁶⁵⁷

A Canadian case of *Aqua-Land Exploration Ltd. v. Guarantee Co. of North America*⁶⁵⁸ is another example. In this case, Aqua-Land agreed with B and C to attempt to put the latter’s invention of a new type of drilling tower to practical use. In order to do this, they agreed to establish a private company, Marine Drilling. Marine Drilling entered into an informal agreement with Accurate Machine to construct a drilling tower; no formal agreement had been signed. Aqua-Land paid in advance a certain sum of money to Accurate Machine to give the latter sufficient funds to finish construction. Aqua-Land took out an insurance policy on the drilling tower.⁶⁵⁹ The drilling tower was destroyed during a storm while it was being

⁶⁵⁶ *Truran Earthmovers Pty Ltd v Norwich Union Fire Insurance Society Ltd* [1976] 17 SASR 1; see ALRC 20, p72; see also ALRC Discussion 63, para. 7.8

⁶⁵⁷ Pinzur, “Insurable interest: a search for consistency”, (1979) 46 *Ins.Counsel J.* 109, p119

⁶⁵⁸ [1966] 54 D.L.R 299

⁶⁵⁹ The policy was as follows: “On property of every description pertaining to the Assured’s drilling operations on Structure No.2, consisting principally but not limited to Casings, Pipe Equipment, Compressors, Hydraulic Jacks, Tools, Platforms, Binoculars, Cabins, Camp Supplies and Equipment, the property of the Assured or the

towed out to drilling site. The Ontario Court of Appeal held that the insured had an insurable interest in the drilling tower. However, when the case came to the Canadian Supreme Court, it was held that the insured had no insurable interest.⁶⁶⁰ This case was heavily criticised by commentators for its support for a narrow concept of insurable interest.⁶⁶¹ It was asserted that: “A corporation that has advanced USD 30,000 to designers of a marine drilling rig is not affronting any social anti-gambling norms by insuring the rig. If there is a “gamble” involved, it is in backing technological development- a highly regarded activity.”⁶⁶²

4.1.3.3. *Should an unsecured creditor have an insurable interest in his debtor’s property?*

There is assumption that an unsecured creditor has no insurable interest because he does not require any particular property as security, and does not look to any particular property for satisfaction of the debt.⁶⁶³ However, it is submitted that this assumption should not deprive an unsecured creditor of being granted an insurable interest in the debtor’s property. If he can prove that he has suffered an actual economic loss, he should be entitled to take out an insurance policy and to make a valid claim under it.

Another argument for rejecting the unsecured creditor’s insurable interest is that the debtor’s property may be destroyed but the unsecured creditor’s right to the debt still survives.⁶⁶⁴ The unsecured creditor still has the right to require the debtor to repay, and it will be satisfied if the debtor’s financial resources are sufficient to cover for the debt. It is true that the destruction of the debtor’s property does not release him from the duty to repay the debt, and it cannot legally impair the creditor’s right to collect.⁶⁶⁵ However, if the debtor has only a few pieces of property, the destruction of those properties does in fact diminish the creditor’s

property of others for which the Assured may be responsible, including personal effects of the Assured’s employees...”

⁶⁶⁰ For a critical comment in very details on the decision, see R. McLeod, “*Aqua-Land Exploration Ltd. v. Guarantee Co. of North America et al.*: Insurable interest in an indemnity policy”, (1966) 24 *U. of T. Fac. Law Rev.* 154. McLeod cited, at p156, the case of *Clark v Scottish Imperial Insurance* [1880] 4 S.C.R 192, in this case, a ship which was being built for the insured burned while still in the possession of the shipbuilder. The insured did not have a contract to purchase, but on the basis of the money he had advanced in return for the privilege of selling the ship for the builder, he was held to have had an insurable interest in the ship.

⁶⁶¹ R. McLeod, “*Aqua-Land Exploration Ltd. v. Guarantee Co. of North America et al.*: Insurable interest in an indemnity policy”, (1966) 24 *U. of T. Fac. Law Rev.* 154; R. Hasson, “Reform of the law relating to insurable interest in property- some thoughts on *Chadwick v Gibraltar General Ins*” (1983-1984) 8 *Can Bus LJ* 114

⁶⁶² C. Brown and J. Menezes, *Insurance Law in Canada*, (Carswells, Toronto, 1982), p71

⁶⁶³ Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 *Col.I.R.* 1162, p1186

⁶⁶⁴ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p164

⁶⁶⁵ E. Patterson & H. McIntyre, “Unsecured creditor’s insurance”, (1931) 31 *Col LR* 212, p225

chance of collecting his debt and does impair the economic value of the creditor's chose in action.⁶⁶⁶

It is also argued that there are several other options for an unsecured creditor to secure against the risk of loss by insuring the debt itself, or by taking credit insurance,⁶⁶⁷ or by requiring the debtor, as a condition of credit, to insure his property with a clause binding the insurer that loss should be payable to the creditor. However, these options may not provide adequate financial protection for unsecured creditors.

Credit insurance is practically limited to debtors who have a fairly high credit rating.⁶⁶⁸ And credit insurers may require the creditor to take some of the risk himself.⁶⁶⁹ Consequently, the creditor may not be fully repaid for his debt.

Requiring the debtors to procure a policy with a clause binding the insurer that loss should be payable to the creditor is not a good solution either. Normally, a standard clause of that policy provides that "loss, if any, payable to X [the creditor] as interest may appear" or "loss, if any, payable to X [the creditor]". There are several problems which prevent the creditors from obtaining the insurance proceeds.⁶⁷⁰ If the debtor infringes certain conditions or a warranty in his policy, the creditor cannot recover.

Moreover, even if he does not commit a breach of condition which nullifies the insurance, he may use the insurance proceeds for purposes other than repayment of his debt, or the types of risk which are covered under the policy are not broad enough to cover the risk which has caused the loss. In this scenario, the unsecured creditor may end up with nothing.⁶⁷¹

To sum, where unsecured creditors seek financial protection from their insurance, and the insurers agree to provide such protection, there is no clear reason to prevent them from doing so.

⁶⁶⁶ E. Patterson & H. McIntyre, "Unsecured creditor's insurance", (1931) 31 Col LR 212, p225

⁶⁶⁷ *Anglo-Californian Bank v London & Provincial Marine & General Ins Co* [1904] 10 Com Cas 1; see also Schedule 2 to the Insurance Companies Act 1982; For example, an unsecured creditor who has a right to royalties on an invention which the debtor is to exploit in the debtor's factory may insure the royalties against fire at the factory; see *National Filtering Oil Co v Citizens Insurance Co* [1887] 13 NE 337; Pinzur, "Insurable interest: a search for consistency", (1979) 46 Ins.Counsel J. 109, p119

⁶⁶⁸ E. Patterson & H. McIntyre, "Unsecured creditor's insurance", (1931) 31 Col LR 212, p214

⁶⁶⁹ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p166

⁶⁷⁰ E. Patterson & H. McIntyre, "Unsecured creditor's insurance", (1931) 31 Col LR 212, p229-234

⁶⁷¹ E. Patterson & H. McIntyre, "Unsecured creditor's insurance", (1931) 31 Col LR 212, p215

4.1.4. Insureds with limited interests:⁶⁷²

4.1.4.1. Current English rules on insurable interest of an insured with limited interests in the insured property

Under English law, a limited legal or equitable interest is insurable.⁶⁷³ Where insurance is effected by a person with a limited interest, the amount recoverable by him under the policy can be no more than what he has lost.⁶⁷⁴ However, an insured with limited interests is entitled to take out insurance covering not only his own interests, but also interests of other parties.⁶⁷⁵

Where the insured was under no duty to insure on behalf of anyone else and there is nothing to show that he intended to do so, the presumption is that he intended to cover his own interest only and nothing more.⁶⁷⁶

Where the insured is under an obligation to insure the interests of others, it must be assumed that any policy taken out by him is intended to cover both his own interests and the interests of the others.⁶⁷⁷ If the interests of others are also covered, the insured can recover in excess of his own interest, but must then account the amount in excess of his actual loss to the other interested parties.⁶⁷⁸ For example, a warehouseman or a carrier can insure goods entrusted to

⁶⁷² R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p147; ALRC 20, p73 (critically analysis on the problem of the principle of insurable interest in respect of limited interest); J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p68; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p88; D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p41; M. Templeman, “Insurable interest: a suitable case for treatment?” in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p187; Lee Kiat Seng, “Insurable interest in Singapore”, (1997) *Singapore Journal of Legal Studies* 499, p521; C. Nicoll, “Insurable interest: as intended?” (2008) *J.B.L* 432, p444

⁶⁷³ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p147; S.8 of MIA 1906. The MIA 1906 gives three examples of the insurability of limited interests: a defeasible interest, a contingent interest, and a partial interest of any nature insurable;

⁶⁷⁴ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p147-148

⁶⁷⁵ Bowen L.J. in *Castellain v. Preston* (1883) 11 QBD 380, p398 stated that: “a person having a limited interest may insure either for himself, and to cover his own interest only, or he may insure so as to cover not only his own limited interest, but also the interest of all others who are interested in the property.”; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p88

⁶⁷⁶ *Armitage v Winterbottom* [1840] 1 Man.&G 130, R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p150

⁶⁷⁷ *National Oilwell v Davy Offshore* [1993] 2 Lloyd’s Rep. 582

⁶⁷⁸ *DG Finance Ltd v Scott* [1999] Lloyd’s Rep. IR 387; D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p41; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p88

his care for their full value and recover in full in the event of a total loss; however, he must hold on trust the amount in excess of his own liability for the owners of the goods.⁶⁷⁹

4.1.4.2. Current Vietnamese rules on insurable interest of an insured with limited interests in the insured property

Under Vietnamese law, the insured with limited interest is not allowed to take out insurance on property itself for its full value in his own name, because he has interests in only part of the property. He is only entitled to insure his own interest.⁶⁸⁰

The insured with limited interests is only able to purchase insurance covering both his own interest and the interests of other parties if he acts as an agent for the others. Therefore, the two following conditions must be satisfied: (i) the other parties must give the insured authority in writing to act on his behalf to enter into the insurance contract;⁶⁸¹ and (ii) it must be specified in the policy that the beneficiaries are the insured and the other parties.⁶⁸² In the event of loss, if the two conditions are fulfilled, the insured is entitled to recover for the full value of the insured property, but must account to the other parties the amount in excess of his own actual loss. If one of the conditions is not fulfilled, he is not entitled to recover for the full value.

⁶⁷⁹ *Waters v Monarch Fire & Life Assurance Co* [1856] 5 El.&Bl. 870; *Tomlinson (Hauliers) v Hepburn* [1966] A.C 451; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p88

⁶⁸⁰ Article 3(9) of Vietnam's Law on Insurance Business 2000: "Insurable interest means a right of ownership, right of possession, right of use, or property right; maintenance rights and obligations to the person insured against."

⁶⁸¹ Article 139 of Vietnam's Civil Code 2005: "*Representation*: (1). Representation means an individual (hereinafter referred to as the *representative*) acting in the name and for the benefit of another person (hereinafter referred to as the *principal*) enters into and performs a civil transaction within the scope of representation. (2). Individuals, legal entities and other subjects may enter into and perform civil transactions through a representative. An individual may not allow another person to represent him or her if the law stipulates that the individual must personally enter into and perform such transaction. (3). The representation relationship shall be established in accordance with law or in accordance with an authorization. (4). A principal has rights and obligations arising from a civil transaction established by a representative..." And Article 142 of Vietnam's Civil Code 2005: "*Authorized representation*: (1). Authorized representation means representation which is established pursuant to a power of attorney between the representative and the principal. (2). The parties may agree on the form of authorization, except where the law stipulates that there must be a written power of attorney." Regarding to form of insurance contract, Article 14 of Vietnam's Law on Insurance Business provides: "*Forms of insurance contracts*: (1) An insurance contract must be made in writing. (2). Proof of entering into an insurance contract shall be a certificate of insurance, an insurance policy, a telegram, a telex, a facsimile and other forms stipulated by law." Therefore, the form of authorization to enter into insurance contract, which is given the tenant insured by the owner, must be in writing.

⁶⁸² In this circumstance, the beneficiary, who can get the insurance money, is different from the insured, who enters into insurance contract and pays the premiums. See standard forms of insurance on property of Bao Viet, Bao Minh,...

Vietnamese law is even harsher to insureds than English law. Under Vietnamese law, where the insured is under an obligation to insure the interests of others, there is no presumption that any policy taken out by him is intended to cover both his own interests and the interests of the others. Even if the insured takes out insurance in his own name, covering both his interests and the interests of the others, and the premiums are charged on the full value of the insured property, he is only entitled to recover for his own losses, and the value in excess of his own interest is declared null and void.⁶⁸³

4.1.4.3. Should an insured with limited interests be allowed to take out insurance in his own name, covering the full value of the insured property?

An Australian case of *British Traders' Insurance Co. Ltd v Monson*⁶⁸⁴ is worthy of discussion here. In this case, the tenant of a property which was later destroyed had insured it for its full value. At the time of proposing insurance, the tenant had an option to purchase and intended to buy the property. However, the purchase was unsuccessful and a lease had been entered into instead. The owners of the property had cancelled their own insurance policy, effected with the same insurer. This cancellation had been done on the advice of the insurer's agent. The Supreme Court of Tasmania allowed the insured to recover the full value of the insured property. On appeal, however, the High Court of Australia held that the insured could only recover for his loss and nothing for the benefit of his landlord.

This was unfair to the tenant insured because the insurer was allowed to break his contractual promise, regardless of the fact that, at the time of entering into the insurance contract, he had accepted premiums based on the full value of the property, and had clearly promised to indemnify for the full value in the event of loss.⁶⁸⁵ Moreover, at the time of contract, the

⁶⁸³ Article 42 of Vietnam's Law on Insurance Business 2000: "*Contract of property insurance above value*: (1). A contract of property insurance above value means a contract in which the sum insured is greater than the market value of the insured property at the time of entering into the contract. An insurer and a purchaser of insurance may not enter into a contract of property insurance above value. (2). In the case where a contract of property insurance above value is entered into due to the unintentional wrongful act or omission of the purchaser of insurance, the insurer must refund to the purchaser of insurance the amount of paid insurance premium corresponding to the insured sum which exceeds the market value of the insured property, after deducting legitimate related expenses. Upon occurrence of the insured event, the insurer shall only be responsible to indemnify for damage not exceeding the market value of the insured property."

⁶⁸⁴ [1964] 111 CLR 86

⁶⁸⁵ ALRC 20, p76. To criticise the decision of Australian High Court, the ALRC 20 cited an English case of *Hepburn v Tomlinson [Hauliers]* [1966] 1 All ER 418 (House of Lords); in this case, bailees had insured a consignment of cigarettes which had been stolen without negligence on the part of the bailees. The insurer argues that the bailees had insured only their limited interest which was potential liability for their own negligence, not the property itself. The English House of Lord interpreted the policy as one covering the property in question rather than the bailees' limited personal interest. It was held that, as a matter of

insurer always has a right to limit his liability to the value of the insured's interest, but in this case, he had chosen not to do so.

It is submitted that there was no clear reason to prevent the insured tenant from recovering for the full value of the insured property, and holding the amount in excess of his own actual loss on trust for the owner, which is not contrary to the principle of indemnity.

Another example is a hypothetical case which was put up for discussion by the UK Law Commissions in the Issue Paper 4. A mother insures the full value of house contents in her own name. However, one room in the house is filled with belongings owned by her son, who leaves them there while he is at university. The value of these is included within the total value of the policy. The house and all the contents are totally destroyed by fire. Can the mother recover the value of her son's property?

Even if the legal right approach is adopted, the mother can still recover the value if a legal formality is completed. If the mother makes an insurance contract as an agent for her son, the son can recover the loss as the insured.⁶⁸⁶ Similarly, under Vietnamese insurance laws, if both of the above-mentioned two conditions are fulfilled, the mother can recover the value of her son's property.

Alternatively, if the insurance contract stipulated that the mother is a bailee, she may recover in her own name.⁶⁸⁷ The reasons for this are that she was in possession of her son's property and it was commercially convenient for the parties to do so. However, the mother must hold the amount in excess of her own interest for her son, and she cannot retain it for herself.

From the two examples above, it can be concluded that the most important factor which should be considered is the construction of the insurance policy. The insurers should be under a duty to ensure that the words of the policy reflect exactly the intention of the parties. Where the parties to the insurance contract clearly specify that the insurers agree to take the risk of loss of both a third party's property and the property of the insured, the insured should be

construction, the insurance was not of liability but of goods. The bailees had an interest insuring the goods, and could recover the full value, provided that the insurance monies over and above the amount of his own loss were held on trust for the owner.

⁶⁸⁶ *North British Insurance Co v Moffatt* [1871] L.R. 7 C.P. 25, p30-31 per Keating J.; see also: R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p150; C. Nicoll, "Insurable interest: as intended?" (2008) J.B.L 432, p446

⁶⁸⁷ C. Nicoll, "Insurable interest: as intended?" (2008) J.B.L 432, p446

entitled to recover the full value, and the insurer should not be allowed to break his promise by arguing that the insured has no insurable interest in the third party's property.

It is strongly submitted that even if the doctrine of insurable interest is eliminated, the position of the parties does not change,⁶⁸⁸ because: (i) The principle of indemnity is a sufficient barrier to prevent an insured from obtaining unjust benefits from his insurance policy since, in order to recover for the loss under the policy, the insured must prove his actual loss. Any amount in excess of his actual loss will account to third parties who have an interest in the insured property. (ii) The insurers are still protected by the principle of utmost goodfaith. It is required that the insured must disclose all material circumstances to the insurers. And then, if all of the information is notified to the insurers, they have a right to choose whether or not to take the risk, or whether to limit their liability to the insured's own interest. If wrong information is given, the insurance contract may be void. Therefore, the parties should pay more attention to what is written down in their contract to ensure that their intention is properly and clearly stated.

4.1.5. Insurable interest of a bona fide purchaser of stolen goods.⁶⁸⁹

Possession of property can be a strong ground for finding sufficient insurable interest because the right to possess is usually found with other rights, such as ownership. Absolute ownership is the solid predictable foundation of an insurable interest.⁶⁹⁰ A person who has absolute ownership of a property certainly has an insurable interest in it. Absolute ownership is the simplest type of insurable interest⁶⁹¹ and is recognised by insurance laws all over the world.

On the other hand, mere right to possess is unusual, but may be found in some circumstances, for instance, that of a bona fide purchaser of stolen goods. Mere possession of property may not be sufficient to give an insurable interest to the person in possession of the insured

⁶⁸⁸ The insured with limited interest is entitled to recover the value of a third party's property if the contract allows him to do so, and he must hold the amount in excess of his own interest on trust for the third party.

⁶⁸⁹ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p66; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p157; Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1166; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p60; L. Cash, "Insurance- A bona fide purchaser has an insurable interest in stolen property", (1979-1980) 10 Mem.St.U.L.Rev 390; J.D.W, "*Castle Cars Inc. v United States Fire Insurance Co.*: the bona fide purchaser's insurable interest in stolen property", (1982) 68 Va.L.Rev 651; R. Hasson, "Reform of the law relating to insurable interest in property- some thoughts on *Chadwick v Gibraltar General Ins*" (1983-1984) 8 Can Bus LJ 114

⁶⁹⁰ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1166

⁶⁹¹ Complete ownership is a simplest type of insurable interest. E. Patterson & H. McIntyre, "Unsecured creditor's insurance", (1931) 31 Col LR 212, p220

property because he has no legal or equitable relation to or no legal liability for causing damage to or destruction of it.⁶⁹² Insurable interest of a bona fide purchaser of stolen goods will be critically analysed.

4.1.5.1. Current English and Vietnamese rules:

The question of whether possession of stolen goods by a bona fide purchaser can be sufficient to constitute an insurable interest is answered differently from one jurisdiction to another. No case has been clearly reported on this issue in English law. However, several notable English academics agree that a bona fide purchaser of stolen goods has an insurable interest.⁶⁹³

A large number of such cases have been dealt with in America. In the majority of the cases, American courts held that a bona fide purchaser of stolen goods has an insurable interest in them.⁶⁹⁴ In Canada, an innocent purchaser of stolen goods was denied an insurable interest in the case of *Chadwick v. Gibraltar General Insurance Co.*⁶⁹⁵ This judgment was criticised as a bad decision.⁶⁹⁶

Under Vietnamese laws, a civil transaction in stolen goods is invalid because the goods have been taken away from the true owner against his wish, irrespective of the fact that the goods are moveable or immovable, and are required to be registered, or are not required to be registered.⁶⁹⁷ Accordingly, a bona fide purchaser of stolen goods has no insurable interest in them.

⁶⁹² John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p66

⁶⁹³ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p66; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p157; Birds doubts that an innocent purchaser of stolen goods, without good title to them, has an insurable interest, see J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p61

⁶⁹⁴ *Castle Cars v United States Fire Insurance Co.* [1981] 273 S.E. 2d 793; *Riley v. Mid-Century Ins. Exch.* [1981] 118 Cal. App. 3d 195; *Butler v. Farmers Ins. Co.* [1980] 616 P.2d 46; *Duncan v. State Farm Fire & Cas. Co.* [1979] 587 S.W.2d 375; *Granite State Ins. Co v Lowe* [1978] 362 So.2d 240; *Reznick v. Home Ins. Co.*, [1977] 360 N.E.2d 461; *Scarola v. Insurance Co. of N. Am.* [1972] 340 N.Y.S.2d 630; *Grimm v. Prudence Mut. Cas. Co.* [1971] 243 So. 2d 140; *Barnett v. London Assurance Corp.* [1926] 138 Wash. 673, 245 P. 3. However, there were a few cases followed the legal right test approach and denied an insurable interest to a bona fide purchaser of stolen goods; see *Insurance Company of North America v Cliff Pettit Motors Inc.* [1974] 513 S.W.2d 785; *Herrington v. American Sec. Ins. Co.* [1971] 184 S.E.2d 673; *Gordon v. Gulf Am. Fire & Cas. Co.* [1965] 149 S.E.2d 725; *Giles v. Citizens' Ins. Co.* [1924] 32 Ga. App. 207, 122 S.E. 890

⁶⁹⁵ [1981] 34 O.R.2d 488; see also: *Thompson v Madill* [1986] 13 C.C.L.I 242

⁶⁹⁶ For more details, see R. Hasson, "Reform of the law relating to insurable interest in property- some thoughts on *Chadwick v Gibraltar General Ins*" (1983-1984) 8 Can Bus LJ 114

⁶⁹⁷ The Vietnamese regulations on ownership, classifications of property types into movable and immovable property have been modelled on French law; see also: Nguyen Ngoc Dien, "Cau truc ky thuat cua he thong phap luat bat dong san Vietnam: mot goc nhin Phap" (2007) *Tap chi Nghien cuu lap phap* 18 [Trans: Nguyen Ngoc Dien, "The technical structure of Vietnamese real estate law: one aspect from French laws", (2007) *Journal of*

An absurd situation may thus arise. If a stolen car is destroyed by fire, neither the true owner nor the bona fide purchaser can make a claim against their insurers for the loss.⁶⁹⁸ The true owner cannot do so under his policy because, under Vietnamese insurance laws, his policy was terminated at the time when the car was stolen.⁶⁹⁹ The bona fide purchaser who was in possession of the car likewise could not make a claim under his policy because he has no insurable interest in it. It means that both of the two insureds had paid premiums for the same risk, but neither of them could recover for the loss from their insurers. The legal right approach clearly prevents a bona fide purchaser from recovering for his actual economic loss.

4.1.5.2. Whether a bona fide purchaser should have an insurable interest in stolen goods.

Legislative Studies 18], p19-20; Article 132 of the Vietnam's Civil Code 2005: "*Invalidity of civil transactions due to deception or threat*: Any party which participates in a civil transaction as a result of deception or threat has the right to petition a court to declare such transaction invalid. Deception in a transaction means an intentional act of a party or of a third party for the purpose of misleading the other party as to the subject, nature of the entity, or contents of the civil transaction which has caused the other party to enter into the transaction..." Although, an innocent purchaser has some protection as it provides in the Article 138 of the Vietnam's Civil Code 2005: "*Protection of interests of bona fide third parties with respect to invalid civil transactions*: (1). Where a civil transaction is invalid but the transacted property is moveable property ownership of which is not required to be registered and such property has already been transferred to a bona fide third party through another transaction, then the transaction with respect to the third party is still valid, except for the case stipulated in article 257 of this Code. (2). Where the transacted property is immovable property, or moveable property ownership of which is required to be registered, and the transacted property has been transferred to a bona fide third party through another transaction, then the transaction in relation to that third party is invalid, except where the bona fide third party received the property via an auction or via a transaction with another party pursuant to a verdict or decision of an authorized State body being the owner of such property but thereafter such person is not the owner of the property as a result of the verdict or decision being amended or rescinded.", **the true owners still have priority to ownership of the stolen goods** since the goods have been taken away from them against their wish. Article 257 and 258 of the Vietnam's Civil Code 2005 are applied (for example, where a car is stolen, article 258 is applied since a car is a moveable property which is required to be registered; therefore, the true owners always have priority to claim the ownership of the car), and it provides that: Article 257: "*Right to reclaim moveable property, ownership of which is not required to be registered, from a bona fide possessor*: The owner shall have the right to reclaim moveable property, ownership of which is not required to be registered, from a bona fide possessor in a case where such possessor obtained the moveable property through a contract without compensation to a person without the right to dispose of such property. In a case where such contract includes compensation, then the owner has the right to reclaim such moveable property if it was stolen, lost or in other circumstances in which possession of it was obtained contrary to the wish of the owner." Article 258: "*Right to reclaim moveable property, ownership of which is required to be registered, or immovable property from a bona fide possessor*: The owner shall have the right to reclaim moveable property, ownership of which is required to be registered, or immovable property except where a third party is a bona fide possessor of such property through an auction or through a transaction pursuant to a verdict or decision of an authorized State body which made such person the owner of the property but at a later date such person was not the owner of the property due to the verdict or decision being amended or rescinded."

⁶⁹⁸ R. Hasson, "Reform of the law relating to insurable interest in property- some thoughts on *Chadwick v Gibraltar General Ins*" (1983-1984) 8 Can Bus LJ 114, p117

⁶⁹⁹ Article 23(1) of the Vietnam's Law on Insurance Business 2000: "*Termination of insurance contracts*: In addition to the circumstances for termination of contracts pursuant to the provisions of the *Civil Code*, an insurance contract shall also terminate in the following circumstances: (1). The purchaser of insurance no longer has an insurable interest;..." Since the car has been stolen, the true owner of the car no longer has an insurable interest in it; see also: Hiep hoi bao hiem Viet Nam, *Cam nang bao hiem phi nhan tho*, (NXB Tai chinh, 2007) [Trans: Association of Vietnamese Insurance, *Guidelines on non-life insurance*, (Finance Publishing House, 2007)], p36

It is submitted that a bona fide purchaser should be granted an insurable interest for the two following reasons. First, the bona fide purchaser is in possession of the property, and holds a right of lawful possession against all others rather than the true owner.⁷⁰⁰ When the true owner is unknown and does not claim possessory rights in the stolen property, no one can have a claim superior to that of the bona fide purchaser.⁷⁰¹ Second, the bona fide purchaser has economic benefits from the continued existence of the stolen property- i.e. the continued availability of its use to him.⁷⁰² Therefore, denying an insurable interest to a bona fide purchaser is preventing him from recovering for his actual economic losses, and is pointlessly harsh to him who has done no wrong.⁷⁰³

It has been argued that granting an innocent purchaser of stolen goods an insurable interest would make him more careless or not take precaution about the property that he is going to buy. However, it is pointed out that a purchaser still cares about this point because of his potential liability to the true owner for conversion. If it can be proved that the goods have been stolen, and the true owner can be easily identified, the bona fide purchaser has to return the goods to the true owner. He may eventually lose his money.⁷⁰⁴

4.2. Other problems relating to the legal right approach:

4.2.1. Creation of uncertainty over application of the principle of insurable interest:

The law on insurable interest in indemnity insurance is uncertain. It is asserted that the law on insurable interest is messy, illogical and difficult to analyse.⁷⁰⁵ There are several pieces of

⁷⁰⁰ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p66. (It is technically correct that the true owner still has title to the stolen property.)

⁷⁰¹ L. Cash, "Insurance- A bona fide purchaser has an insurable interest in stolen property", (1979-1980) 10 *Mem.St.U.L.Rev* [stands for Memphis State University Law Review] 390, p398

⁷⁰² J.D.W, "Castle Cars Inc. v United States Fire Insurance Co.: the bona fide purchaser's insurable interest in stolen property", (1982) 68 *Va.L.Rev* [stands for Virginia Law Review] 651, p659

⁷⁰³ J.D.W, "Castle Cars Inc. v United States Fire Insurance Co.: the bona fide purchaser's insurable interest in stolen property", (1982) 68 *Va.L.Rev* 651, p662

⁷⁰⁴ J.D.W, "Castle Cars Inc. v United States Fire Insurance Co.: the bona fide purchaser's insurable interest in stolen property", (1982) 68 *Va.L.Rev* 651, p667

⁷⁰⁵ R. Merkin, "Reforming insurance law: is there a case for reverse transportation?", available at <http://lawcommission.justice.gov.uk/docs/ICL_Merkin_report.pdf>, p78; The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008), para?; UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p104; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p65

law involving and regulating different types of insurance,⁷⁰⁶ and inconsistent judgments have been seen.⁷⁰⁷

In *Macaura*,⁷⁰⁸ it was held that a sole shareholder and unsecured creditor of a company had no insurable interest in the company's property on the ground that he had no legal or equitable relation to the property, but, in *Kosmopoulos*⁷⁰⁹ - a Canadian case with facts indistinguishable from those of *Macaura*, it was held that the sole shareholder had an insurable interest in the company's property on the ground that he had suffered pecuniary interest. In line with *Kosmopoulos*, in another English case of *Wilson v Jones*,⁷¹⁰ a shareholder in a telegraph company formed in order to lay a transatlantic telegraph cable, who had no personal or contractual interest in the cable, took out a policy insuring against the failure of laying the cable. It was held that he had an insurable interest on the basis that the policy was not on the cable, but on the insured's interest in the adventure of laying the cable.

On one hand, a possessor who has no right of enjoyment of the property or no legal liability in respect of it has no insurable interest.⁷¹¹ On the other hand, a possessor who has no legal or equitable relation to the subject matter insured, but has been granted an exclusive right to control of it, has an insurable interest.⁷¹²

As a general rule, an unsecured creditor has no insurable interest in his debtor's property.⁷¹³ However, in *Moran, Galloway & Co v Uzielli*,⁷¹⁴ it was held that a creditor who had no legal or equitable relation to a vessel but had a right "in rem"⁷¹⁵ against the property had insurable interest.⁷¹⁶

In sum, the determination of the existence of insurable interest is based on the degree of relationship rather than the kind of relationship between the insureds and the insured

⁷⁰⁶ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p142-143

⁷⁰⁷ M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p203

⁷⁰⁸ *Macaura v Northern Assurance Co.* [1925] A.C. 619

⁷⁰⁹ *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208

⁷¹⁰ [1867] L.R. 2 Ex 139

⁷¹¹ *Macaura v Northern Assurance Co.* [1925] A.C. 619

⁷¹² *Sharp and Roarer Investments Ltd v Sphere Drake Insurance plc, Minster Insurance Co Ltd and EC Parker and Co Ltd [The Moonacre]* [1992] 2 Lloyd's Rep 501

⁷¹³ *Macaura v Northern Assurance Co.* [1925] A.C. 619; *General Accident Fire & Life Ass. Co. v Midland Bank* [1940] 2 K.B. 388

⁷¹⁴ [1905] 2 KB 555

⁷¹⁵ See section 3.1.2 of this Chapter

⁷¹⁶ For the facts of and analysis on the case, see section 3.1 of this Chapter; see also *Cepheus Shipping Corp. v Guardian Royal Exchange Assurance (The Capricorn)* [1995] 1 Lloyd's Rep 622; *O'Kane v Jones [The Martin PJ]* [2004] 1 Lloyd's Rep 389, [2003] EWHC 2158

properties.⁷¹⁷ A judgement can be changed by a single fact. This creates uncertainty over application of the principle of insurable interest.

4.2.2. Creation of difficulties for the parties in understanding and applying the rules:

As there are several pieces of law involving and regulating different types of insurance, this creates difficulties for both the insured and the insurer to contract with certainty.⁷¹⁸ The problems relating to the principle of insurable interest are more serious and complicated in the context of complex commercial transaction or project in which there are several parties involved,⁷¹⁹ because their interests are mixed, and sometimes it is difficult to make a clear-cut assessment.

4.2.3. Creation of a technical defence for insurers

It has been long recognised that the principle of insurable interest is a technical defence for insurers. In 1884, Brett M.R in the case of *Stock v Inglis*⁷²⁰ made a well-known statement: "... it is the duty of a court always to lean in favour of an insurable interest, if possible, for it seems to me that after underwriters have received the premium, the objection that there is no insurable interest is often, as nearly as possible, a technical objection, and one which has no real merit, certainly not as between the assured and the insurer." In 2003, Waller L.J., in the latest leading case on insurable interest,⁷²¹ agreed that it is a technical defence; he cited Brett's statement with approval. Several learned academic writers have the same opinion.⁷²²

⁷¹⁷ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p484; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p187

⁷¹⁸ M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p216

⁷¹⁹ *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587; EWCA Civ 885; *Deepak Fertilisers & Petrochemicals Ltd v Davy McKee [London] Ltd* [1999] 1 All ER [Comm] 69; *National Oilwell [UK] Ltd v Davy Offshore Ltd* [1993] 2 Lloyd's Rep 582; *Petrofina (UK) Ltd v Magnaload Ltd* [1984] QB 127 [1884] 12 Q.B.D 564, p571

⁷²¹ *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587; EWCA Civ 885

⁷²² D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p34; J. Birds, "A shareholder's insurable interest in his company's property", (1987) J.B.L 309, p309; UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), para1.45; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p202; J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p495; Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1163; ALRC 20, p72, ALRC Discussion Paper 63, para 7.14; ALRC Report 91, para 11.22; D. Galbraith, "An Unmeritorious Defence – The Requirement of Insurable Interest in the Law of Marine Insurance and Related Matters" (1992) 5(3) Ins LJ 177

The legal right approach provides a technical defence to insurers because it allows insurers to escape their contractual liability, refusing to give an indemnity in the event of loss.⁷²³ The insurers are the persons who have comprehensive knowledge of insurance laws. At the time of entering into an insurance contract, they should know whether or not an insured has an insurable interest in the insured property, or sometimes, in complex situations, they should notice that the insured may not have an insurable interest in the insured property. Whenever they doubt whether an insurable interest exists, they should explain or bring notice to their customers, or perhaps refuse to issue an insurance policy to cover the risk that is proposed by the insureds. If they choose to assume the risk and take the premiums, they should be bound by their contractual promises.

However, in practice, when the insurance contract is made, the insurers do not raise the issue or explain clearly to their customers. When the loss occurs, they raise the issue of lack of insurable interest in order to refuse to make a payment or to avoid proving fraud on the part of the insureds, in cases where the insurers suspect fraud, but it is very difficult to prove, or where they do not want to prove it. After raising the issue, they merely sit back and await the outcome.

If the judges rule that there is no insurable interest, the insurers can breach their contractual promises without paying any damage. They are legally entitled to breach the contract. If the judges hold that an insurable interest exists, they just do what they anticipated or what they were supposed to do, which is to make a payment under the policy. It is asserted that this technical defence of insurers is contrary to social and economic expectations.⁷²⁴

4.2.4. Prevention of the parties from entering into insurance policy covering new types of interest:

In the modern economy, economic conditions have changed and proprietary interests have been expanded. The legal right approach prevents insurers and insureds from entering into insurance policies covering new types of interest. When an interest is not recognised by laws, both insurers and insureds hesitate to effect a new type of insurance policy. For example, in accordance with the legal right approach, a FOB buyer has no insurable interest in the goods prior to shipment. Thus, both the FOB buyers and the insurers are not certain about insurance

⁷²³ J. Birds, "A shareholder's insurable interest in his company's property", (1987) J.B.L 309, p309

⁷²⁴ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1163

covering the risk of loss before shipment. Where the insurers promise to cover the risk of loss, it is a promise based on honour, not a legally binding one.

Another example is sub-contractors' interest in a large complex construction project. Insurers and insureds had to wait for a long time for the courts' decision in order to be sure whether or not a sub-contract has an insurable interest in the whole project, although it was commercially convenient to do so. At the moment, they are still waiting for the courts to give a decision on whether or not the potential liability of a sub-contractor for damage after completion of a project is sufficient to amount to an insurable interest.⁷²⁵ The debate still continues.

4.2.5. Penalising only policyholders for lack of insurable interest:⁷²⁶

The remedy for breach of the requirement of insurable interest is unclear. It seems that only the policyholders who have suffered a loss are penalised.⁷²⁷ The consequence of lack of insurable interest is that the policy is held to be void, the policyholders will not have their claims paid, and their premium may not be even returned.

On the other hand, the current Vietnamese laws allow the insurers, who suffer no loss (apart from the administrative cost of dealing with the claim) to write risks, collect premiums, assume no risk, and then refuse to pay claims on the grounds of lack of insurable interest. No penalty is imposed on the insurers.

Indeed, in commercial practices, insurers usually take great care to ensure that insureds who do not have a sufficient insurable interest in the subject matter of insurance are not allowed to take out insurance policies. However, an insurer in financial difficulties might not take the same approach due to a conflicting duty to shareholders.⁷²⁸ The cases of *Hebdon v West* and *Feasey v Sun Life Assurance Co of Canada* are typical examples of that situation. It is

⁷²⁵ UK Law Commission, Insurance Contract Law: Post Contract Duties and other Issues, (Law Com Consultation Paper No 201, 2012), p122-123; *Deepak Fertilisers & Petrochemicals Ltd v Davy McKee [London] Ltd* [1999] 1 All ER [Comm] 69; *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587; EWCA Civ 885

⁷²⁶ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p31; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p215

⁷²⁷ M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p215

⁷²⁸ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p32

suggested that if the requirement of insurable interest is eliminated, the possibility of insurers issuing the “wrong” insurance contracts would be excluded.

5. THE “FACTUAL EXPECTATION” APPROACH:⁷²⁹

As the legal right approach has brought injustice to insureds, and is inconsistent with the principle of indemnity, and cannot keep pace with the changes of modern economic conditions, a fairer approach which is known as the “factual expectation” approach has been adopted. In England, the leading case which is considered as a departure from the legal right approach and adoption of the factual expectation approach is *Feasey v Sun Life Assurance Co of Canada*.⁷³⁰ Similarly, in Canada, *Constitution Insurance Co of Canada v Kosmopoulos*,⁷³¹ is a famous case which has eliminated nearly two hundred years of powerful precedent for the legal right approach, and overturned it in favour of the factual expectation approach. In America, the factual expectation approach has been adopted in a number of states.⁷³²

“Factual expectation” is the simplest expressed. The factual expectation approach is based on the insured’s economic interest in the preservation of the insurance subject matter. The

⁷²⁹ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p59-60; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p145-146; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p58; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p142; C. Nicoll, “Insurable interest: as intended?” (2008) J.B.L 432, p441; D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006); p34; J. Birds, “Insurable interest- orthodox and unorthodox approaches”, (2006) J.B.L 223, p230; Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 Col.I.R. 1162; J.D.W., “Castle Cars Inc. v United States Fire Insurance Co.: the bona fide purchaser’s insurable interest in stolen property”, (1982) 68 Va.L.Rev 651; Pinzur, “Insurable interest: a search for consistency”, (1979) 46 Ins.Counsel J. 109, p118; L. Stuesser, “Insurable interest: the Supreme Court of Canada adopts the factual expectancy test”, (1987-1988) 13 Can Bus LJ 227; R. Hasson, “The Supreme Court in flames: fire insurance decision after Kosmopoulos”, (1995) 33(4) Osgoode Hall. L.J 679; Note, “Necessity for pecuniary interest”, (1971) Duke.L.J 479; J. Ziegel, “Shareholder’s insurable interest- another attempt to scuttle the *Macaura v Northern Assurance Co*. Doctrine *Kosmopoulos v Constitution Insurance Co*”, (1984) 62 Can.Bar.Rev [stands for Canadian Bar Review] 95

⁷³⁰ [2003] 2 All.E.R. [Comm] 587

⁷³¹ [1987] 34 D.L.R 208

⁷³² New York, Florida, Washington, New Jersey, Virginia, Alabama, Arizona,... see also: Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 Col.I.R. 1162; R. Pinzur, “Insurable interest: a search for consistency”, (1979) 46 Ins.Counsel J. 109, p125; J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474; D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p42

requirement of legal or equitable interest is not necessary to constitute an insurable interest. Something less than a legal or equitable interest is sufficient.⁷³³

In accordance with the factual expectation approach, an insurable interest exists when an insured will suffer a detriment or loss if the property is damaged or destroyed, but receives some benefit or advantage by its continued existence.⁷³⁴ In *Lucena v Craufurd*, Lawrence J. stated that the approach “is applicable to protect men against uncertain events which may in any wise be of disadvantage to them.”⁷³⁵ This is a wide approach.

The expansion of the concept of insurable interest is of importance in the situation where the insured is reliant upon a particular subject-matter for certain purposes, but without having any legal or equitable ownership of it or any right to possess it.⁷³⁶ A sole shareholder, for example, will have an insurable interest in the properties of his company, and a FOB buyer in the goods before they are shipped at the loading port.

Expansion of the concept of property interest is a driving force for the expansion of the concept of insurable interest. The definition of insurable interest has changed dramatically over the years to keep up with the changing market.⁷³⁷ In the modern economy, an interest in property is not only restricted to legal or equitable interest. A property interest can be legal or equitable, a present possessory right or future interest, vested or contingent, and it may exist regardless of the likelihood that its possessor will ever realize and actually enjoy the specific property.⁷³⁸

⁷³³ Per Lord Waller in *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587, see also: *The Moonacre* [1992] 2 Lloyd’s Rep 501; *Petrofina (UK) Ltd v Magnaload Ltd* [1984] QB 127; *Stone Vickers Ltd v Appledore Ferguson Shipbuilders Ltd* [1991] 2 Lloyd’s Rep 288; *National Oilwell [UK] Ltd v Davy Offshore Ltd* [1993] 2 Lloyd’s Rep 582; *Deepak Fertilisers & Petrochemicals Ltd v Davy McKee [London] Ltd* [1999] 1 All ER [Comm] 69

⁷³⁴ Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 Col.I.R. 1162, p1172; R. Pinzur, “Insurable interest: a search for consistency”, (1979) 46 Ins.Counsel J. 109,

⁷³⁵ *Lucena v Craufurd* [1806] 2 Bos. & P.N.R. 269, 301; see also *National Filtering Oil Co v Citizens Ins Co* [1887] 13 NE 337, Finch J. stated: “if there be a right in or against the property which some court will enforce ... a right so closely connected with it and so much dependent for value upon the continued existence of it alone, as that a loss of the property will cause pecuniary damage to the holder of the right against it, he has an insurable interest.”

⁷³⁶ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p144

⁷³⁷ R. Merkin, “Reforming insurance law: is there a case for reverse transportation?”, para 8.6 available at <http://www.lawcom.gov.uk/docs/merkin_report.pdf>

⁷³⁸ R. Pinzur, “Insurable interest: a search for consistency”, (1979) 46 Ins.Counsel J. 109, p112

However, the factual expectation approach cannot solve all of the problems relating to the concept of insurable interest.⁷³⁹ There are some difficulties in valuating certain types of expectation interest, and the concept of “factual expectation interest” is fairly vague in some circumstances, resulting in inconsistencies in application of the approach. Therefore, it might not be an ideal solution for reforming the provisions governing insurable interest under Vietnamese insurance laws.

In the following part of this section, the factual expectation approach will be critically analysed. There are three points which will be considered in turn, namely: application of the factual expectation approach, advantages of the factual expectation approach in comparison with the legal right approach, and finally, uncertainty over the application of factual expectation approach.

5.1. Application of factual expectation approach:

The concept of insurable interest under the factual expectation approach is much wider than that under the legal right approach. In order to determine the existence of an insurable interest, the factual expectation approach gives absolute emphasis on pecuniary interest.⁷⁴⁰ If a risk of loss is capable of being valued in monetary terms,⁷⁴¹ it is sufficient to constitute an insurable interest. The cases which are discussed below will show how the courts value a risk of loss in monetary terms and insureds are granted an insurable interest.

5.1.1. English cases:

In the leading case of *Lucena v Craufurd*,⁷⁴² the wide concept of insurable interest was formulated by Lawrence J.⁷⁴³ This wide concept was adopted by English courts in some famous cases: *Wilson v Jones*,⁷⁴⁴ *Moran, Galloway & Co v Uzielli*,⁷⁴⁵ and *The Moonacre*.⁷⁴⁶

⁷³⁹ D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p36

⁷⁴⁰ D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p34

⁷⁴¹ D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p34; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p142-143

⁷⁴² [1806] 2 Bos. & P.N.R. 269

⁷⁴³ *Ibid*, p302: “A man is interested in a thing to whom advantage may arise or prejudice happen from the circumstances which may attend it; and whom it importeth that its condition as to safety or other quality should continue. Interest does not necessarily imply a right to the whole or part of the thing, nor necessarily and exclusively that which may be the subject of privation, but the having some relation to, or concern in, the subject of the insurance; which relation or concern, by the happening of the perils insured against, may be so

In *Wilson v Jones*,⁷⁴⁷ a shareholder in a telegraph company, who had no personal or contractual interest in the cable, took out a policy insuring against the failure of laying the cable. It was held that he had an insurable interest in the adventure of laying the cable.

If the court had strictly followed the legal right approach, and the subject matter of insurance had been the property of the company (the cable itself), the insured would have had no insurable interest. However, in this case, the court applied the factual expectation approach, and the subject matter of insurance was the commercial adventure of successfully laying the cable; therefore, the insured had an insurable interest.⁷⁴⁸

In *Moran, Galloway & Co v Uzielli*, it was held that an unsecured creditor, who had no legal or equitable relation to the insured ship, but had the right to bring an action “*in rem*”,⁷⁴⁹ had an insurable interest in the ship. Similarly, in *The Moonacre*, a shareholder, who had no legal or equitable relation to the insured vessel, but was granted an exclusive right to control of it, had an insurable interest.

The latest leading case which followed the trend of expansion of the concept of insurable interest is *Feasey v Sun Life Assurance Co of Canada*.⁷⁵⁰ This case has been considered as the

affected as to produce a damage, detriment or prejudice to the person insuring. And where a man is so circumstanced with respect to matters exposed to certain risks or dangers, as to have a moral certainty of advantage or benefit, but for those risks or dangers he may be said to be interested in the safety of the thing. To be interested in the preservation of a thing, is to be so circumstanced with respect to it as to have benefit from its existence, prejudice from its destruction. The property of a thing and the interest derivable from it may be very different. Of the first the price is generally the measure; but by interest in a thing, every benefit and advantage arising out of or depending on such a thing may be considered as being comprehended.”

⁷⁴⁴ [1867] L.R. 2 Ex 139

⁷⁴⁵ [1905] 2 KB 555

⁷⁴⁶ [1992] 2 Lloyd’s Rep 501

⁷⁴⁷ [1867] L.R. 2 Ex 139

⁷⁴⁸ C. Nicoll, “Insurable interest: as intended?” (2008) J.B.L 432, p441

⁷⁴⁹ See section 3.1.2 of this Chapter

⁷⁵⁰ [2003] 2 All.E.R. [Comm] 587; EWCA Civ 885; This case arose out of an insurance effected by a P and I Club, insuring members of the club in respect of their liabilities for personal injury or death suffered by employees of members and others on board their vessels. Originally the club reinsured their own liabilities under a conventional reinsurance with a Lloyd’s syndicate (number 957). There could be no insurable interest problems under that sort of arrangement since anyone, including an insurer, has an unlimited insurable interest against legal liabilities that they might incur. However, in 1995, because of changes in the Lloyd’s rules regarding liability insurance, the reinsurance between the club and Syndicate 957 was changed, in effect becoming what looked like a first party rather a third party insurance. Syndicate 957 agreed to pay a fixed sum to the club in respect of relevant injuries and death, the sort of arrangement that looks like classic life and personal accident insurance. It was not tied to the amount of the legal liability of the members of Steamship Mutual. The Court of Appeal held that, according to the construction of the policy, it was not an insurance that operated only once the liability of Steamship Mutual was established, rather cover for losses that Steamship Mutual might incur once liability was established. Lord Waller, who gave the leading majority judgment, at [2003] 2 All.E.R. [Comm] 587; EWCA Civ 885, para [97], concluded that: “In an insurance of a specific identified life, it will be difficult to establish a legal or equitable relation without a pecuniary liability recognised by law arising on the death of that particular person. There is however no authority which deals with a policy on

most important one which critically reviewed the concept of insurable interest in a modern commercial context. Lord Waller thoroughly re-examined the case law on insurable interest over the last 200 years. He categorised the cases into four groups, three of which relate to property insurance: (i) where the subject matter insured is an item of property, the insured must have a legal or equitable interest in the property;⁷⁵¹ (ii) where the subject matter is property, but the policy extends beyond the property and covers such interest as the insured might possess;⁷⁵² (iii) where the insured faces loss by reason of the destruction of the insured subject matter, even though he has no close relationship with the subject matter.

Lord Waller stated that, in property insurance, “something less than a legal or equitable or even pecuniary interest has been thought to be sufficient” to constitute an insurable interest.⁷⁵³ Therefore, an insurable interest exists if: (i) the insured has legal or equitable title to the subject matter; or (ii) the insured is in possession of the subject matter - for example, a bailee, a bona fide purchaser of stolen property; or (iii) the insured is not in possession of the subject matter but may be either responsible for, or suffer a loss in the event of, any damage to the subject matter - for example, a sub-contractor.⁷⁵⁴ This is a broad definition of insurable

many lives and over a substantial period [as as the case with Steamship Mutual] and where it can be seen that a pecuniary liability will arise by reference to those lives and the intention is to cover that legal liability. He then stated that insurable interest should be interpreted broadly, as with the decisions on “pervasive interest”. Steamship Mutual had a pecuniary liability in respect of the lives covered, and the intention was to cover that liability; this was sufficient to find an insurable interest. Analysis on this case see J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), 49-50; UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p121-122; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p90

⁷⁵¹ For example: *Macaura v Northern Assurance Co.* [1925] A.C. 619

⁷⁵² For example: *Wilson v Jones* [1867] L.R. 2 Ex 139

⁷⁵³ For example: *The Moonacre* [1992] 2 Lloyd’s Rep 501; *Petrofina (UK) Ltd v Magnaload Ltd* [1984] QB 127; *Stone Vickers Ltd v Appledore Ferguson Shipbuilders Ltd* [1991] 2 Lloyd’s Rep 288; *National Oilwell [UK] Ltd v Davy Offshore Ltd* [1993] 2 Lloyd’s Rep 582; *Deepak Fertilisers & Petrochemicals Ltd v Davy McKee [London] Ltd* [1999] 1 All ER [Comm] 69

⁷⁵⁴ Waller LJ’s view was that his final category explained the numerous cases involving insurance of construction works by a subcontractor. In his view, the most obvious basis of such insurable interest was not the possible liability faced by the subcontractor in the event of his causing damage to the works, but **rather his pecuniary loss** in the event that the works were damaged and he was unable to fulfil his contract. However, a subcontractor also had an insurable interest in his own liability and if the policy was worded so as to cover insurable interest in liability, then it ought to be so construed even though the policy referred primarily to the property itself.; see also: Case comment, “Insurable interest and reinsurance agreements”, (2003) *Ins.L.M* 7; H. Yeo, Y. Jiao and J.Chen, “Insurable interest rule for property insurance in the People’s Republic of China”, (2009) *J.B.L* 776, 781; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p90; The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008), p38

interest, and it is similar to Lawrence's definition in *Lucena*,⁷⁵⁵ meeting the need of commercial convenience.

According to Lord Waller, in order to determine the existence of an insurable interest, the most important factor which should be considered is the construction of the policy. As the parties to a contract of insurance have freedom to contract, they should be binding to the terms and conditions on which they have agreed. If the insureds have disclosed all of the material facts or information at the time of inception, and the insurers have agreed to take the risk, the insurers should not be allowed to refuse to pay on the basis of lack of insurable interest at the time of loss. This is a fairer approach. It leads to more sensible results to both the insureds and the insurers.⁷⁵⁶

5.1.2. *Canadian cases:*

In the case of *Kosmopoulos v Constitution Ins. Co.*,⁷⁵⁷ in which the facts were undistinguishable from those of *Macaura v Northern Assurance Co.*, the Canadian Supreme Court dispensed with the legal right approach, and had made a remarkable effort to state that the "factual expectation test" was a better approach which could meet requirements of commercial practice. In this case, the Court allowed a plaintiff, who owned all of the shares in a company, and had insured the company's property in his own name rather than the company's name, to recover under his insurance policy. To reach that conclusion, the Court had not only relied on the logic of academic commentators but had also critically examined the three policies underlying the requirement of insurable interest.⁷⁵⁸

The factual expectation approach was also applied in *Commonwealth Construction Co Ltd v Imperial Oil Ltd.*⁷⁵⁹ This case concerned a sub-contractor's insurable interest. It was held that,

⁷⁵⁵ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p38

⁷⁵⁶ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p72; J. Birds, "Insurable interest- orthodox and unorthodox approaches", (2006) J.B.L 223, p230; H. Yeo, Y. Jiao and J.Chen, "Insurable interest rule for property insurance in the People's Republic of China", (2009) J.B.L 776, 781

⁷⁵⁷ [1987] 1 SCR 2

⁷⁵⁸ (i) the policy against wagering under the guise of insurance; (ii) the policy to prevent temptation to destroy the insured property; (iii) the policy favouring limitation of indemnity. Those policies will be critically analysed later at section 6.2 of this Chapter

⁷⁵⁹ [1977] 69 DLR (3d) 558, the case was about a composite policy which covered all-risks to a construction venture. Imperial entered into a contract for building a fertiliser plant with Wellman-Lord for the latter to carry out the construction. Part of the construction was sub-contracted to Commonwealth. Commonwealth started a fire in the process of performing its sub-contract, resulting in damage to the works. The insurer indemnified Imperial for its loss, and then brought a subrogated action against Commonwealth to recoup its payment. The question arose as to whether the insurer could bring a subrogated action against one of the co-insureds.

in cases of composite policies, “if the different interests are pervasive and if each relates to the entire property, albeit from different angles, ... there is no question that the several insureds must be regarded as one”.⁷⁶⁰ Therefore, a sub-contractor has an insurable interest in the entirety of the insured properties that are involved in a construction project. The two grounds for the court to give the judgment were: (i) the analogy between the position of contractors or sub-contractors and the position of bailees,⁷⁶¹ and (ii) the common goal of all parties involved in the construction venture- joint efforts to complete the construction.⁷⁶²

5.1.3. American cases:

In America, the case of *National Filtering Oil Co v Citizens' Insurance Co*⁷⁶³ has been cited as a precedent for the factual expectation theory.⁷⁶⁴ It was about a fire insurance policy which covered the oil refinery premises of a manufacturer-patent licensee as well as specific royalties. The royalties were based upon a percentage of the monetary value of the total output of the oil refinery, and paid by the licensee to the insured-licensor. The insured-licensor was contractually prevented from transferring the patent rights to other parties. It was held that the licensor-insured had an insurable interest in its licensee's building, irrespective that the royalties were contingent and dependent upon market condition and the licensee's conduct. The insured's royalties would be dismissed if the licensee's building was damaged, causing a reduction in production.

It is submitted that the judgement is right. The insureds only benefit from the royalty contract if the insured property still exists. They cannot get the anticipated royalties if the property is destroyed. If the insureds sustain a direct loss from destruction of the insured property, it should be sufficient to constitute an insurable interest. The insureds do not need to demonstrate a legal or equitable relation to the property in order to have an insurable interest.

⁷⁶⁰ *Ibid*, p 561 per De Grandpré J.

⁷⁶¹ See also *State of the Netherlands v Youell* [1997] 2 Lloyd's Rep 440, p449 per Rix J.: “by a pervasive interest is meant the right to claim an insurable interest in the whole property, analogous to the well-known right of a bailee to insure for the total value of the property bailed and not merely to the extent of his liability interest as bailee: if the property is lost or destroyed, the bailee can recover for the whole value of the property even though he may be under no liability to the owner, and he holds the proceeds of insurance in trust for the owner.”

⁷⁶² See also: John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p82

⁷⁶³ (1887) 106 NY 535

⁷⁶⁴ R. Pinzur, “Insurable interest: a search for consistency”, (1979) 46 Ins.Counsel J. 109, p118

A possessor or operator of real property who had no judicially enforceable property right was also granted an insurable interest. In *Liverpool & London Globe Ins. Co v Bolling*,⁷⁶⁵ a land and building owner allowed his former daughter-in-law to occupy the property rent free and to operate it as a business. The owner showed intention to convey the property to the woman later, but no promise enforceable in equity appeared. When the insured property was destroyed by fire, the court allowed her full recovery on the ground that she had economic support from the productivity of the premises.

Concerning shareholders' insurable interest, unlike Vietnamese and English law, American law recognises that a shareholder has an insurable interest in the corporate property.⁷⁶⁶ The reason for this is that corporation is the owner of its assets and property, and the shareholder is an owner of the corporation.

Moreover, based on a factual expectation, Pinzur asserted that the shareholders "have equitable rights of a pecuniary nature, growing out of their situation as stockholders, which may be prejudiced by the destruction of the corporate property... It is very plain that both these rights of stockholders- viz., the right to dividends and the right to share in the final distribution of the corporate property- may be prejudiced by its destruction."⁷⁶⁷

An expectancy of future benefit could be a sufficient ground for finding an insurable interest. In *Hudson v Glens Falls Ins. Co.*,⁷⁶⁸ the insured contracted with a farmer to raise the latter's crops. The title to the crops remained with the farmer as security for the contract until the insured fully performed his contractual obligations. The hay was destroyed by fire. It was held that the insured had a sufficient insurable interest in the hay because he could retain possession against all but the farmer. He had an expectation of benefit from the contract.

In summary, the factual expectation approach gives the law on insurable interest considerable flexibility, and broadens the potential range of legitimate insurance. Based on the pecuniary interest of the insureds, and the capability of the risk of loss being valued in monetary term, insurable interests can be found in accordance with the factual expectation approach; whereas there is no insurable interest if the legal right approach is adopted.

⁷⁶⁵ [1940] 10 S.E. 2d 578

⁷⁶⁶ *Riggs v Commercial Mutual Ins. Co.* [1890] 125 NY 7, 25 NE 1058

⁷⁶⁷ Pinzur, "Insurable interest: a search for consistency", (1979) 46 *Ins.Counsel J.* 109, p121; *Riggs v Commercial Mutual Ins. Co.* [1890] 125 NY 7, p12-13, 25 NE 1058, p1060

⁷⁶⁸ [1916] 218 NY 133, 112 NE 728

5.2. Whether the factual expectation approach is better than the legal right approach⁷⁶⁹

5.2.1. Being more consistent with the principle of indemnity

The factual expectation approach is more consistent with the principle of indemnity.⁷⁷⁰ It should be remembered once again that the purpose of the principle of indemnity, the spine of the law of indemnity insurance, is to put insureds in the position in which they would have been if the loss had not occurred.⁷⁷¹ By broadening the potential range of legitimate insurance, the factual expectation approach gives the law more flexibility and offers to the insureds more possibility for recovering their actual economic losses.

In the context of the modern economic environment, differences between the legal right approach and factual expectation approach are of importance where insureds take out insurance on a particular subject matter for certain purposes, but they have no legal or equitable relation to it.⁷⁷² The factual expectation approach allows the insureds to recover for their actual economic losses, whereas the legal right approach does not do so.⁷⁷³ Several further examples of this situation can be given.⁷⁷⁴

Insureds who established a company that contracted with builders to build the company's property, and had advanced a certain amount of money to the builders in order to finish the construction of the company's property, should have the right to take out insurance on the company's property, and the right to make a valid claim under the insurance policy on the loss of the company's property.⁷⁷⁵ Although the insureds had no legal or equitable relation to the company's property, when the property is destroyed, they had suffered an actual economic loss- the amount money that had been paid in advance.

Insureds who contracted with architects to design their buildings and had no ownership of the architects' plans should be entitled to take out insurance on the plans in their own name if the

⁷⁶⁹ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1185

⁷⁷⁰ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p35

⁷⁷¹ M. Clarke, *Policies and Perceptions of Insurance Law in the Twenty First Century*, (OUP,2007), p220

⁷⁷² R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p144-145

⁷⁷³ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p37

⁷⁷⁴ Some examples of this situation have been discussed at section 5.1 of this Chapter

⁷⁷⁵ See *Aqua-Land Exploration Ltd. v. Guarantee Co. of North America* [1966] 54 D.L.R 299

insurers agreed to cover for the risk of loss of the plans, and the parties to the insurance contract have expressly stipulated their intention in the contract.⁷⁷⁶

Insureds who are the owners of ice-cream parlour that is next to a cinema should be able to insure the cinema against the risk of loss of profit if the cinema is destroyed.⁷⁷⁷ Although the owners of the ice-cream parlour have no legal or equitable relation to the cinema, they may suffer a loss of profit on the occurrence of the destruction of the cinema. It can be argued that it is practically too difficult to measure the expected commercial profit from the parlour. However, this difficult should not prevent the insureds from recovering for their actual economic loss. Where insurers agree to cover for the risk of loss, a fixed amount of compensation on occurrence of the insured events can be stipulated in the policy. This agreed valuation is conclusive between the parties to the policy. It should be emphasized that where both parties freely enter into a contract, they should be bound by their contract. The insureds should be able to make a valid claim under the policy, and the insurers should not be allowed to break their contractual promise on the ground that the insureds have no insurable interest in the insured property. Where the insurers take the view that the risk of loss of profit is uncertain and unpredictable, they can simply choose not to issue the cover.

It can be concluded that, in the absence of the factual expectation approach, the insureds in the above-mentioned situations cannot make a valid claim under their policies, and are prevented from recovering for their actual economic losses.

5.2.2. Formulating a wider concept of insurable interest

In comparison with the legal right approach, the factual expectation approach formulates a wider concept of insurable interest which can keep pace with the expansion of the property right concept. This is so for two reasons: (i) the approach is largely based on economic analysis rather than the legal relationship between the insureds and the insured properties,⁷⁷⁸ which runs more closely parallel with the principle of indemnity, and (ii) it follows the more flexible concept of economic loss in the modern economic environment.⁷⁷⁹

⁷⁷⁶ See *Glengate-KG Properties v Norwich Union Fire Ins Society* [1996] 1 Lloyd's Rep 614

⁷⁷⁷ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p144-145

⁷⁷⁸ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p34-35

⁷⁷⁹ ALRC 20, p73; Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, at p1184-1185, stated that: "Procurement of a policy of insurance is an investment prompted by commercial foresight. This foresight involves recognition of a **desire economic**

The rationale behind the need for the wider concept has been pointed out by Harnett and Thornton. They stated: “the property right conception is analytically not separate from the factual expectation of damage but...while the physical owner is the most probable loser, others may similarly suffer pecuniary setback upon the destruction of the insured property, and often to a greater extent than a nominal owner. Recognition of this has led to an expansion of the property right concept.”⁷⁸⁰

5.2.3. Leaning towards finding insurable interest where possible

English case law has established a principle that courts should have a preference for finding insurable interest where possible. In *Moran, Galloway & Co v Uzielli*,⁷⁸¹ Walton J. stated that: “the definition of insurable interest has been continuously expanding, and dicta in some of the older cases, which would tend to narrow it, must be accepted with caution.” In *Stock v Inglis*,⁷⁸² Brett MR also pointed out: “in my opinion it is the duty of a Court always to lean in favour of an insurable interest, if possible, for it seems to me that after underwriters have received the premium, the objection that there was no insurable interest is often, as nearly as possible, a technical objection, and one which has no real merit, certainly not as between the assured and the insurer.”

The legal right approach, which is based on the insureds’ proprietary title to, or right in, the insured property, does not embrace the type of insurance contracts in which the insureds may not have a legal or equitable relation to the insured property as required by laws, but do suffer economic disadvantages when it is damaged or destroyed.⁷⁸³ Therefore, this leads to some ridiculous and unjust situations in which insureds have been denied recovery simply because

relationship to a thing capable of destruction or damage, and the prudence of allocating certain monetary sums to ensure financial protection in the event of a catastrophic occurrence...There is an **essential subjectivity to property insurance protection**... As to policy-holders, generally, insurance is an investment in probabilities and assurances... Based on economic analysis... there is only one true concept of insurable interest, and that is the factual expectation of damage. Restated, this conception is that insurable interest exists if the insured, independently of the policy of insurance, **will gain economic advantage from the continued existence of the insured property or will suffer economic disadvantage on damage to the property**. The property right conception is analytically not separate from the factual expectation of damage but...while the physical owner is the most probable loser, others may similarly suffer pecuniary setback upon the destruction of the insured property, and often to a greater extent than a nominal owner. Recognition of this has led to an expansion of the property right concept...”

⁷⁸⁰ *Ibid*, p1184-1185

⁷⁸¹ [1905] 2 KB 555 at p563

⁷⁸² (1884) 12 QBD 564 at 571

⁷⁸³ M. Templeman, “Insurable interest: a suitable case for treatment?” in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p204

the nature of their interest is not in the narrow list of legal or equitable requirement.⁷⁸⁴ However, it has been proved that a proprietary title to, or right in, property is only a typical type of insurable interest,⁷⁸⁵ something other than a proprietary interest can be sufficient to amount to an insurable interest.⁷⁸⁶ The legal right approach was only suitable in the business conditions of two hundred years ago. Since then, business conditions in the modern economy have changed considerably;⁷⁸⁷ therefore, it is no longer suitable.

5.2.4. Whether this approach creates difficulties in measuring the loss

There is a concern that the broader concept of insurable interest can result in difficulties in measuring the loss suffered by the insureds. However, those difficulties should not prevent the expansion of the concept of insurable interest.⁷⁸⁸ Courts have been faced with the difficulties of measuring loss for long time, and have been resolving them quite well.⁷⁸⁹ There are two ways which may be taken into account to solve those difficulties, namely, using value policies and applying the laws governing the insured properties. Where the parties to the contract fix a certain amount representing the actual loss in a value policy, this amount will be binding to both parties. Where there is no such fixed amount in the policy, the laws governing the insured properties will give a guideline for measuring the loss. For example, in marine insurance, there is a custom that imaginary profit in a cargo is ten percent of the value of the cargo;⁷⁹⁰ thus loss of profit can be ascertained.

5.2.5. Whether this approach leads to the situation that too much insurance taken out on the same insured property

There was another concern that too much insurance on the same property could be taken out if the factual expectation approach is adopted. In *Lucena*, Lord Eldon expressed his concern about too many people being able to purchase insurance. He stated: “if moral certainty be a

⁷⁸⁴ Harnett, p1185; *Macaura v Northern Assurance Co.* [1925] A.C. 619; *Fuerst Day Lawson v Orion Ins* [1980] 1 Lloyd’s Rep 656; *Aqua-Land Exploration Ltd. v. Guarantee Co. of North America* [1966] 54 D.L.R 299; *British Traders’ Insurance Co. Ltd v Monson* [1964] 111 CLR 86

⁷⁸⁵ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p58; Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 Col.I.R. 1162, p1175

⁷⁸⁶ *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587; EWCA Civ 885

⁷⁸⁷ R. McLeod, “*Aqua-Land Exploration Ltd. v. Guarantee Co. of North America et al.*: Insurable interest in an indemnity policy”, (1966) 24 *U. of T. Fac. Law Rev.* 154, p159

⁷⁸⁸ R. Pinzur, “Insurable interest: a search for consistency”, (1979) 46 *Ins.Counsel J.* 109, p116

⁷⁸⁹ For example, in *Wilson v Jones* [1867] L.R. 2 Ex 139, the interests of individual shareholder in the adventure of a corporation were evaluated.

⁷⁹⁰ D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p29

ground of insurable interest, there are hundreds, perhaps thousands, who would be entitled to insure. First the dock company, then the dock-master, then the warehouse-keeper, then the porter, then every other person who to a moral certainty would have anything to do with the property, and of course get something by it.”⁷⁹¹ However, this concern is unnecessary. There are five reasons to undermine it.

First, in *Kosmopoulos*, Wilson J. disagreed with Lord Eldon, and argued that a broadening of the concept of insurable interest would allow for **the creation of more socially beneficial insurance policies**, with no increase in risk to the insurer.⁷⁹² She continued her argument by putting a question of “why should the porter in Lord Eldon’s example not be able to obtain insurance against the possibility of being temporarily out of work as a result of the sinking of the ships?”⁷⁹³ She believed that actually the narrow concept of insurable interest restricts legitimate insurance.⁷⁹⁴ It is clear and unarguable that there should be more social advantage from encouraging insurance than from discouraging it. Certainly, one of the social advantages is that the insureds can buy financial stability from the insurers, and the latter have more opportunities to do their business and make profit.

Second, an increase in insurance will not create any increase in risk to the insurers because they have ability to manage and assess any new types of risk. They are able to calculate the total potential liability which may arise out of the occurrence of an insured event. This is a principal task and daily job for all insurers. An individual cannot know about the probability of his property being damaged or destroyed, but the insurers can obtain data and statistics on a large scale to calculate this probability and the potential liability.

By collecting those data, it also helps the insurers to measure the frequency of occurrence of a particular event and the cost of the event should it in fact occur, which gives them useful information in deciding which types of risk can be taken, which types of policy can be issued,

⁷⁹¹ *Lucena v Craufurd* [1806] 2 Bas. & P.N.R. 269, 127 E.R. 630, p651-652

⁷⁹² *Kosmopoulos v. Constitution Insurance Co.* [1987] 1 S.C.R. 2, para.24, p18

⁷⁹³ *Kosmopoulos v. Constitution Insurance Co.* [1987] 1 S.C.R. 2, para.24, p18; see also: *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587, p635

⁷⁹⁴ *Kosmopoulos v. Constitution Insurance Co.* [1987] 1 S.C.R. 2, para.24, p18; for example, it was hard to justify a distinction between insurance against loss of income caused by illness, which is allowed, and loss of income caused by destruction of the employer’s workplace, which is not; see also M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p145

and the appropriate premium to be charged. Alternatively, if they cannot estimate the likelihood of the loss occurring, then they can simply choose not to enter into a contract.⁷⁹⁵

Third, the insureds' limitation of financial resource also undermines Lord Eldon's concern. Lord Eldon argued that if the broader concept of insurable interest applies, any seaman can insure the ship on which he sailed.⁷⁹⁶ Nonetheless, there is the fact that no ordinary seaman has sufficient resource to insure any ship, and that the insurers usually wish to deal with or enter into contract with the master or the owner of the ship.⁷⁹⁷ This reality will reduce the excessive amount of insurance.

However, if an insurer and a seaman actually agree to enter into such an insurance contract, there is no clear reason to prevent the parties from doing so, and the contract should not be considered as void by law when the insured perils occur. The insurer should not be allowed to break his promise on the ground that the insured has no insurable interest in the insured property, and the insured should be allowed to recover if he can prove that he has suffered an actual loss.

Fourth, if the insurers wish to avoid the excessive amount of insurance, they themselves are able to do so in three ways:⁷⁹⁸ (i) by refusing to cover the risk, (ii) by increasing the premiums to opt out some insureds who do not have a genuine desire for financial protection,⁷⁹⁹ and (iii) by inserting protective or exclusion clauses into the policy to limit liability. The insurers always have the rights of freedom of contract in their hands, and they themselves have power to draft the insurance policy. Therefore, where they wish to limit the liability or types of risk or subject matter which can be insured, the limitation can be stipulated in the policy. Those terms and conditions must be brought to the notice of the insureds. This will help the insureds to achieve a better understanding of their insurance contract. Such a situation would be better than one where, at the time of entering into the insurance contract, the insureds have no awareness of the possibility that their policy can be

⁷⁹⁵ *Kosmopoulos v. Constitution Insurance Co.* [1987] 1 S.C.R. 2, para.23, p17

⁷⁹⁶ *Lucena v Craufurd* [1806] 2 Bas. & P.N.R. 269, 127 E.R. 630, p652

⁷⁹⁷ R. Hasson, "The Supreme Court in flames: fire insurance decision after *Kosmopoulos*", (1995) 33(4) *Osgoode Hall. L.J* 679, p682

⁷⁹⁸ *Kosmopoulos v. Constitution Insurance Co.* [1987] 1 S.C.R. 2, para.23, p17, Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 *Col.I.R.* 1162, p1175

⁷⁹⁹ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 *Col.I.R.* 1162, p1175

void due to lack of insurable interest, and at the time of loss, they are denied a recovery for their actual economic loss, finding the policy in their hands worthless.

Fifth, the principle of disclosure and the principle of double insurance give the insurers additional protection against the risk of an excessive amount of insurance, and prevent the insureds from obtaining more than the actual losses they have suffered.⁸⁰⁰

The insureds' duty to disclose all material circumstances and to declare the nature of their interests helps the insurers to assess the risk to be taken,⁸⁰¹ making the decision on whether or not to write a policy. If they wish to take the risk, they can decide what premium should be charged.⁸⁰² Moreover, if the insureds do not properly fulfil their duty of disclosure, the insurers may declare the insurance contract void.

Where there are two or more policies covering the same risk, the principle of double insurance will play its role. The principle of indemnity will limit the maximum recovery for insureds to the amount representing their actual economic loss, and each insurer is only liable for a rateable proportion of the loss.⁸⁰³ Therefore, the insureds cannot obtain unjust enrichment from their insurance policy.

5.3. Uncertainty surrounds the factual expectation approach

In the normal course of business, individuals often come to depend for their success on the existence of some outside activity, such as a building, a public utility, or other institution in which they have no property interest, with which they have never entered into contractual relationships, and over which they have no control. Although the possibility of economic loss upon a fortuitous destruction of the vital outside property is great, the courts have been almost uniform in denying recovery.⁸⁰⁴

⁸⁰⁰ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p28

⁸⁰¹ *Kosmopoulos v. Constitution Insurance Co.* [1987] 1 S.C.R. 2, para.23, p17

⁸⁰² *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587, p635

⁸⁰³ S.32 of MIA 1906; see Chapter 24 in John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p743

⁸⁰⁴ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1174; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p76; J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p487

As discussed above, the legal right approach has created problems relating to insurable interests of head-contractors or sub-contractors in large construction or offshore projects.⁸⁰⁵ Each contractor or sub-contractor only has a limited interest in the construction project. Therefore, they do not have an insurable interest in the whole of the contract works. It means that each party shall take out a policy covering its respective interest; many small policies must be issued, resulting in loads of paper work and overlapping claims in the event of an accident. Premiums on each small policy could be quite high, and in the worst scenario, high premiums might prevent small sub-contractors from purchasing insurance due to lack of financial means.

In the event of loss, after having indemnified the contractors who have suffered the loss, insurers may bring subrogation proceedings against the contractors who are at fault. However, in commercial practice, a single policy in which all the parties jointly insured the whole site can be effected. Consequently, the insurers are not allowed to exercise their subrogation rights because the contractors or sub-contractors cannot sue each other for their loss⁸⁰⁶.

The factual expectation approach can overcome the problem by granting a sub-contractor an insurable interest in the entire project works. In order to do so, the courts have relied on the doctrine of “pervasive interest”⁸⁰⁷. A number of grounds to find for such interests have been sought. However, these grounds are not totally convincing and are open to debate.

Besides that, there are difficulties in measuring the actual losses suffered by insureds because certain types of expectation interest are unlikely to be calculated in monetary terms. This difficulty can be the basis of denying the existence of an insurable interest.⁸⁰⁸

⁸⁰⁵ See 3.1 and 3.2 of this Chapter; the problems arise as to whether or not a sub-contractor, who only has a limited interest in the construction project, may have an insurable interest in the whole of the construction project.

⁸⁰⁶ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p828; ALRC 20, p73 (critically analysis on the problem of the principle of insurable interest in respect of limited interest); J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p68; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p88; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p159-160; M. Templeman, “Insurable interest: a suitable case for treatment?” in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p187; Lee Kiat Seng, “Insurable interest in Singapore”, (1997) *Singapore Journal of Legal Studies* 499, p524-531; C. Nicoll, “Insurable interest: as intended?” (2008) J.B.L 432, p441; Brownie, “Co-insurance and subrogation”, *Ins.L.J* 48

⁸⁰⁷ D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p40-42; C. Nicoll, “Insurable interest: as intended?” (2008) J.B.L 432, p443

⁸⁰⁸ R. Pinzur, “Insurable interest: a search for consistency”, (1979) 46 *Ins.Counsel J.* 109, p116

5.3.1. Difficulties in establishing firm grounds to determine existence of an insurable interest.

The factual expectation approach has been adopted with inconsistencies.⁸⁰⁹ There are many situations in which inconsistencies can be found; for example, with similar facts, the courts reach the similar judgments but giving different grounds.

The grounds for granting a sub-contractor an insurable interest in the whole of the construction project can be summarised as follows: (i) analogy between the position of contractors or sub-contractors and that of bailees, (ii) potential liability for damage to or destruction of the insured property, (iii) loss of the opportunity to do the work and to be remunerated for it, (iv) commercial convenience and (v) construction of the insurance policy. Those reasons were given and critically examined in several cases concerning the context of large construction projects. However, the courts have not made a final decision about which reasons are the most reliable and important for determining the existence of a pervasive interest. This leads to uncertainty about the position of sub-contractors, who have contracts relating to the construction project, but do not work on the construction site, as to whether they are protected by the single policy covering the risk of loss of the insured properties on the construction site as a whole, or whether an insurance policy covering their own interests or their potential liability should be purchased.

In order to grant a sub-contractor an insurable interest in the entirety of a construction project, the pervasive insurable interest doctrine was first introduced by the Canadian Supreme Court in *Commonwealth Construction Co Ltd v Imperial Oil Ltd*,⁸¹⁰ and later, it was employed by English courts in *Petrofina v Magnaload*.⁸¹¹ In these two cases, the grounds for granting a pervasive insurable interest to a sub-contractor were (i) the analogy between the position of

⁸⁰⁹ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1167; R. Pinzur, "Insurable interest: a search for consistency", (1979) 46 Ins.Counsel J. 109, p122

⁸¹⁰ [1977] 69 DLR (3d) 558. The case concerned a composite policy which covered all-risks to a project on building a fertiliser plant. A sub-contractor caused a fire which resulted in damage to the works. After indemnifying the owner of the project for its loss, the insurer brought a subrogated action against the sub-contractor. The question arose as to whether the insurer could bring a subrogated action against one of the co-insureds. It was held that the insurer was not allowed to exercise the subrogation rights on the ground that the sub-contractor had an insurable interest in the whole of the contract works. De Grandpré J., at p 561, stated that, in cases of composite policies, "if **the different interests are pervasive** and if each relates to the entire property, albeit from different angles, ... there is no question that the several insureds must be regarded as one and that **no subrogation is possible**."

⁸¹¹ [1984] QB 127

contractors or sub-contractors and that of bailees,⁸¹² and (ii) commercial convenience: that a single policy can be taken out covering all parties working on the construction site for any loss of or damage to the contract works.

The first ground: The former ground is highly debatable.⁸¹³ Sub-contractors do not have possessory or proprietary rights in the whole contract works as bailees do in the goods. The foundation for bailees' insurable interest builds on their possession of the goods, while sub-contractors do not have such an equivalent foundation.⁸¹⁴

The ground that there is analogy between the position of contractors or sub-contractors and that of bailees was also given in the case of *Stone Vickers Ltd v Appledore Ferguson Shipbuilders Ltd*.⁸¹⁵ This case was an extension of application of the doctrine of pervasive interest to a sub-contractor who may not take part in on-site work. It was held that the supplier of a tail shaft to be incorporated in a vessel, who himself carried out no work to the vessel, may be adversely affected by loss or damage to the vessel or other contract works. Therefore, the supplier had an insurable interest in the whole contract works and was a co-insured under the head-contractor's policy.

However, it is very doubtful that this ground could be applied to sub-contractors who never set foot on the site of the construction project or who never carry out work to the project. Unlike bailees, they are not in possession of the entirety of the insured property at all, and possess no legal or equitable rights to the properties belonging to other sub-contractors. Therefore, this ground seems not plausible to explain the reason why they have an insurable interest in the whole of the contract works.

⁸¹² *Petrofina (UK) Ltd v Magnaload Ltd* [1984] QB 127, p136-137; see also *State of the Netherlands v Youell* [1997] 2 Lloyd's Rep 440, p449 per Rix J.: "by a pervasive interest is meant the right to claim an insurable interest in the whole property, analogous to the well-known right of a bailee to insure for the total value of the property bailed and not merely to the extent of his liability interest as bailee: if the property is lost or destroyed, the bailee can recover for the whole value of the property even though he may be under no liability to the owner, and he holds the proceeds of insurance in trust for the owner."; see also UK Law Commission, Insurance Contract Law: Post Contract Duties and other Issues, (Law Com Consultation Paper No 201, 2012), p116

⁸¹³ UK Law Commission, Insurance Contract Law: Post Contract Duties and other Issues, (Law Com Consultation Paper No 201, 2012), p116

⁸¹⁴ M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p207; see A. Olubajo, "Pervasive insurable interest: a reappraisal", (2004) *Construction Law Journal* 45, p47, the reason for saying that the position of a sub-contractor is similar to that of a bailee is that there is a common goal of all parties involved in the construction venture- joint efforts to complete the construction. I say if it is joint effort, the policy should be liability insurance rather than property insurance.

⁸¹⁵ [1991] 2 Lloyd's Rep 288

The next controversial ground is sub-contractors' potential liability. It was held that the sub-contractors' pervasive interest in the whole of the contract works was derived from their potential liability,⁸¹⁶ by which their interests are not limited to the property owned by them or for which they are responsible, and can be extended to the whole of the insured property.⁸¹⁷ For example, they shall be liable for damage to, or destruction of, the properties involved in the project if the construction works caught fire due to their fault or negligence. This thesis argues that potential liability is not suitable to current economic activities, and there is a need to dismiss this ground to help insurance law to become more transparent.

At the first glance, this ground is fairly reasonable where the sub-contractors have performed their contractual work on the construction site, and they have been negligent in causing damage to or loss of the construction works.⁸¹⁸ They should be granted an insurable interest in the entirety of the properties involved in the project, as shown in the case of *Petrofina*.

However, this ground is not totally convincing where the sub-contractors have carried out no work on the site, and supplied defective parts which caused damage to the works. For example, in *Stone Vickers Ltd v Appledore Ferguson Shipbuilders Ltd*,⁸¹⁹ it was argued that because the supplier would be economically adversely affected where it was responsible for loss to the construction project or other contract works, which was caused by their defective part, it amounted to recognition of their insurable interest in the insured property. Actually, in this case, the ground the court relied on was not founded on common sense and a common legal point of view. Although it is undeniable to acknowledge that the recognition of the insurable interest of the supplier is absolutely reasonable, the justification of the court is not convincing. It bases merely on the potential liability rather than on the interest in property, which cannot reflect fully the account of granting the supplier an insurable interest.⁸²⁰

⁸¹⁶ *Petrofina (UK) Ltd v Magnaload Ltd* [1984] QB 127; *National Oilwell [UK] Ltd v Davy Offshore Ltd* [1993] 2 Lloyd's Rep 582; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p206 (bo)

⁸¹⁷ In *Stone Vickers Ltd v Appledore Ferguson Shipbuilders Ltd* [1991] 2 Lloyd's Rep 288, p301 per Colman J.: "whether the supplier of a part to be installed in the vessel or contract works under construction might be adversely affected by loss of or damage to the vessel or other works by reason of the incidence of any of the perils insured against by the policy in question. If the answer is in the affirmative **there is no reason why such a sub-contractor should not also have sufficient interest in the whole contract works** to be included as co-assured under the protection of the head contractor's policy."

⁸¹⁸ *Petrofina (UK) Ltd v Magnaload Ltd* [1984] QB 127

⁸¹⁹ [1991] 2 Lloyd's Rep 288

⁸²⁰ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p82; see also *Canadian Pacific v Base Security Services* [1991] 77 D.L.R 178; *Hopewell v Ewbank Preece* [1998] 1 Lloyd's Rep. 448

The reasoning in *Stone Vickers* can be seriously challenged at two points. First, it can be argued that the sub-contractor's potential liability for loss or damage to the construction project could only confer an insurable interest for the purpose of liability insurance, not for the purpose of property insurance.⁸²¹ This reasoning should be better applied to the situation where several parties are co-insured under a liability policy than to the situation where they are co-insured under a property policy.⁸²² Second, suppose this reasoning would be right, it raises a question of when the extension of the application will end, because a sub-contractor may enter into a contract with a sub-sub-contractor, and so on. If this end can be drawn, the next question arises as to what are the reasons for it? It is submitted that those reasons can be always open for discussion because (i) there is an undeniable fact that some sub-contractors who perform no work on the construction site but have significant economic interests in the whole of the contract works might not be counted or not allowed to take out insurance covering their economic interests, and (ii) the foundation of those reasons is built on degree of relation between a sub-contractor insured and the insured property, which is extremely uncertain. Any boundary that is sought to be formed will be crossed.

In addition, the courts themselves are inconsistent in explaining the ground of potential liability and the extension of the application of the doctrine of pervasive insurable interest. After the case of *Stone Vickers*, the ground of potential liability was reconsidered and confirmed by English Court of Appeal in *National Oilwell [UK] Ltd v Davy Offshore Ltd*.⁸²³ It was held that the potential liability can be applicable to sub-contractors that take no part in on-site work. However, in *Deepak Fertilisers & Petrochemicals Ltd v Davy McKee [London] Ltd*,⁸²⁴ the Court of Appeal did not follow the suggestion made in *National Oilwell [UK] Ltd v Davy Offshore Ltd*. Rather, they stated that sub-contractors had no insurable interest in the entirety of the construction project after its completion.⁸²⁵ To be more specific, it held that the sub-contractors, after the completion of the construction project, had not been economically adversely affected by its damage or destruction if they were not responsible for the loss; therefore, they should have to effect a liability policy, and could not rely on the property

⁸²¹ M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p207

⁸²² A. Olubajo, "Pervasive insurable interest: a reappraisal", (2004) *Construction Law Journal* 45, p48

⁸²³ [1993] 2 Lloyd's Rep 582; H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006)

⁸²⁴ [1999] 1 All ER [Comm] 69

⁸²⁵ *Deepak Fertilisers & Petrochemicals Ltd v Davy McKee [London] Ltd* [1999] 1 All ER [Comm] 69, p85-86; see also *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587, para. [116]-[117], p617-618 per Dyson LJ; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p207

policy, in order to protect themselves against the risk of loss.⁸²⁶ It means that the extension of application of the doctrine of pervasive insurable interest will end after completion of construction project, even though a sub-contractor has a potential liability for damage to or destruction of the insured property.

Later, the Court of Appeal changed their position again in the case of *Feasey v Sun Life Assurance Co of Canada*.⁸²⁷ It was held that where a sub-contractor has a potential liability, it is sufficient to constitute an insurable interest in the entirety of the contract works. It was asserted that there was no reason why potential liability for damage to, or loss of, the insured property should not establish an insurable interest in the property, provided that the sub-contractor has a contractual relation to the property and the subject of the insurance embraces the relevant liability.⁸²⁸

Moreover, as criticised by *Feasey*⁸²⁹, the *Deepak* made things more complicated regarding the application of the principle of insurable interest.⁸³⁰ The *Deepak* denied the ground founded on potential liability for granting a sub-contractor an insurable interest in the whole of the construction project, but failed to critically analyse the previous cases which based on the ground of potential liability to give sub-contractors an insurable interest.⁸³¹

It seems that the *Deepak* went beyond the legal right approach, as it confirmed insurable interest of the sub-contractor during the period of construction. However, it is unnecessary to acknowledge its limitation when narrowing down the recognition of the sub-contractor's insurable interest until the works were completed. Conversely, the sub-contractor should be able to be granted insurable interest even if the works completely finished since it might suffer the actual economic loss at any time after that.

It is submitted that the reasoning based on potential liability to grant a sub-contractor an insurable interest should no longer be adopted. This ground has its own historical value, but is no longer suited to modern economic activities. On the one hand, applying this ground to current economic and legal contexts makes things more unnecessarily complicated and

⁸²⁶ A. Olubajo, "Pervasive insurable interest: a reappraisal", (2004) *Construction Law Journal* 45, p52

⁸²⁷ [2003] 2 All.E.R. [Comm] 587; EWCA Civ 885

⁸²⁸ *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587, p614 para [97]; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p207

⁸²⁹ *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587, p613 para [95]

⁸³⁰ *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587, p613 para [95]

⁸³¹ *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587, p612 para [94]

causes inconsistency in explaining the existence of sub-contractor's insurable interest in the entirety of the construction projects. On the other hand, dismissing this ground would give way to a more transparent and easy-to-apply insurance law.

The third ground, which is not absolutely conclusive either, is loss of opportunity to do the work and to be remunerated for it.⁸³² This ground could be merely an additional justification for granting sub-contractors an insurable interest in the construction works. It gives a closer legal relation between the sub-contractor and the properties involved in the construction project. However, it is not a sufficient ground to explain why a sub-contractor has an insurable interest in the whole of the construction project.

This ground strengthens the legal relation between sub-contractors and the properties involved in the construction project because it points out that an actual economic loss, which they will suffer on the destruction of the insured properties, is the remuneration under their contract when the project is done. For example, sub-contractors who contract to paint a vessel for a certain sum will not receive that sum if the vessel is destroyed by fire. The legal relation between the sub-contractors and the vessel is the painting contract, and the economic loss is the sum that they would have got if the work has been done.

This ground was established in the English case of *Deepak Fertilisers & Petrochemicals Ltd v Davy McKee [London] Ltd*.⁸³³ In this case, it was held that sub-contractors who provided technological and processing know-how in the construction of a plant “undoubtedly had an insurable interest in the plant under construction and on which they were working because they might lose the opportunity to do the work and to be remunerated for it”⁸³⁴ if the plant was destroyed. The ground was also mentioned in the case of *Feasey v Sun Life Assurance Co of Canada*.⁸³⁵ However, there is no attempt to go further in explaining the reason why this ground will give sub-contractors an insurable interest in the construction project as the whole.

⁸³² *Deepak Fertilisers & Petrochemicals Ltd v Davy McKee [London] Ltd* [1999] 1 All ER [Comm] 69; 1 Lloyd's Rep 387, p399 para. 65: “they might lose the opportunity to do the work and be remunerated for it if the property were damaged or destroyed.”; *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587, p612 para [94] *per* Waller L.J, and at para [115] *per* Dyson L.J; A. Olubajo, “Pervasive insurable interest: a reappraisal”, (2004) *Construction Law Journal* 45, p49; C. Nicoll, “Insurable interest: as intended?” (2008) J.B.L 432, p444; UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p116; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p79; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p145; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p159

⁸³³ [1999] 1 All ER [Comm] 69

⁸³⁴ *Ibid*, at p85 para [65]

⁸³⁵ [2003] 2 All.E.R. [Comm] 587

On the basis of loss of opportunity to do the work and to be remunerated for it, sub-contractors only have a limited interest in the properties involved in the construction project. They only have an interest up to the value of the work that has been done by them, and materials that are provided or used, and equipments that are supplied or owned by them, and the expected profits if specifically insured.⁸³⁶ For example, the sub-contractors who contract to paint a vessel have an interest in a certain sum that they will receive when the construction of the vessel is completed, but they do not have an interest in the full value of the vessel. Therefore, this ground cannot clearly explain the reason why a sub-contractor has an interest in the entirety of the construction project, and is entitled to recover the full value.

In sum, this ground helps sub-contractor insureds to prove their actual economic loss, but is not sufficient to provide a satisfactory explanation of why a sub-contractor should be granted an insurable interest in the whole construction works. It actually creates uncertainty over application of the doctrine of pervasive interest.

The fourth ground concerns commercial convenience.⁸³⁷ Several courts have made an effort to escape from the strictness of the concept of insurable interest; however, the grounds for the court's finding were not quite compelling. Commercial convenience could be a reasonable ground for the doctrine of pervasive interest, but it is not a good ground in all circumstances.

The reason for the courts' finding that a sub-contractor under a construction policy has a pervasive insurable interest in the contract works was to prevent parties involved in a common goal from suing one another in the event of damage to the joint effort. This should be right because it is a commercial convenience for both insureds and insurers. The insurers' expense of lengthy litigation against the sub-contractor may cost them more than they can get from the subrogation proceedings. Joint insurance of a large construction project is clearly commercially convenient, and become a common practice; in some cases, it is even an industry requirement.⁸³⁸

It is believed that the rationale underlying the pervasive interest principle is to prevent parties involved in a common goal from suing each other in the event of loss or damage. In some

⁸³⁶ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p79

⁸³⁷ UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p116; D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p37

⁸³⁸ UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p116

cases, this rationale may not be highly relevant. A case in point is a sub-contractor who was a supplier of a tail shaft and was not an ongoing constructor in the building of the vessel. It was argued that, in a strict sense, only the constructor who had purchased the tail shaft to install into the vessel should be protected by the policy of commercial convenience.⁸³⁹ If a supplier supplies defective equipment which may cause damage to a property, he should be liable for the damage. Therefore, the policy of commercial convenience which underpins the doctrine of pervasive insurable interest should not have led to the conclusion that the supplier needed such protection under the marine insurance policy of the main shipbuilder.⁸⁴⁰

The fifth ground founded on construction of the insurance policy was set out in *Feasey*.⁸⁴¹ It is submitted that the main reason that the supplier was entitled to enjoy such protection is that the insurer had agreed to do so in the insurance contract. Where the supplier suffered an actual or economic loss which had been insured against, the insurer should not be allowed to break his promise under the insurance contract.

It is suggested that the question of whether a sub-contractor has an insurable interest in the whole of the insured property is truly one of construction of the policy. Where the parties to the insurance contract do not agree to extend the cover of the policy until after the completion of the project, the sub-contractor should not have an insurable interest in the entirety of the construction project. If they do agree to do so, the sub-contractor should have an interest. It is unfair to the insured if the insurer is allowed to withdraw his promise when the insured perils occurred. The narrow concept of insurable interest should not be a legal obstacle to doing insurance business. Moreover, the insured cannot get unfair benefit from his insurance contract. As the requirement of the principle of indemnity, he must prove that he has suffered an actual loss, and he cannot recover more than the actual loss under his policy.

Conclusion

⁸³⁹ *Petrofina (UK) Ltd v Magnaload Ltd* [1984] QB 127 and *Commonwealth Construction Co Ltd v Imperial Oil Ltd* [1977] 69 DLR (3d) 558

⁸⁴⁰ A. Olubajo, "Pervasive insurable interest: a reappraisal", (2004) *Construction Law Journal* 45, p48

⁸⁴¹ UK Law Commission, *Insurance Contract Law: Post Contract Duties and other Issues*, (Law Com Consultation Paper No 201, 2012), p116, see the footnote 59 for new cases; D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p37

Several courts have relied on the doctrine of “pervasive” interest to find for such interest. This doctrine is still open to debate.⁸⁴² It is argued that the finding of a pervasive insurable interest is inconsistent with the doctrine of insurable interest as this doctrine is generally understood to operate in the laws of insurance.⁸⁴³

The question arises of how a sub-contractor, who only has an insurable interest in respect of his loss or liability in relation to the project, may have an interest in the whole of the project works. In order to overcome the strictness of the narrow concept of insurable interest and to lean toward granting a sub-contractor an insurable interest in the whole of contract works, a number of grounds have been looked for. However, these grounds are not totally convincing and cause several problems. For example, the doctrine of insurable interest is founded on an analogy with the position of bailees; however, the accuracy of the analogy is doubtful. Beside, the reason for successive courts stating that a sub-contractor should be given an insurable interest in the entirety of the property involved in the project is commercial convenience. A very certain foundation was not provided.⁸⁴⁴

The factual expectation approach, with these uncertain grounds, makes the doctrine of insurable interest more difficult to understand and apply, even though granting a sub-contractor an insurable interest in the whole of contract works is a right thing to do. It is submitted that the doctrine of insurable interest is an unnecessary barrier to prevent an insured from getting unjust benefit from his insurance; it only creates a number of legal obstacles to the insurance business. Moreover, it is an unjust technical defence for insurers to break their promise of making payment when the insured perils occur.

5.3.2. Difficulties in measuring the actual losses suffered by insureds

Difficulties in valuating certain types of expectation interest: There are several difficulties in valuating certain types of expectation interest. This difficulty can be the basis of denying the existence of an insurable interest.⁸⁴⁵

⁸⁴² M. Templeman, “Insurable interest: a suitable case for treatment?” in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p206; A. Olubajo, “Pervasive insurable interest: a reappraisal”, (2004) *Construction Law Journal* 45, p45

⁸⁴³ A. Olubajo, “Pervasive insurable interest: a reappraisal”, (2004) *Construction Law Journal* 45, p45

⁸⁴⁴ M. Templeman, “Insurable interest: a suitable case for treatment?” in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p207

⁸⁴⁵ R. Pinzur, “Insurable interest: a search for consistency”, (1979) 46 *Ins.Counsel J.* 109, p116

First example: an ice-cream shop is built next to a cinema, hoping to profit by serving the moviegoers. There is a possibility that destruction of the cinema caused by fire may put the business of the owner of the ice-cream shop in difficulty. To avoid that risk of loss, the owner of the ice-cream shop wishes to take out an insurance policy for the cinema to the extent of covering his future profit. It is practically difficult to measure the expected profit due to many contingencies which can have impacts on the business of the ice-cream shop.

If profits arising from contracts can be recoverable under an insurance policy, to what extent are profits from a commercial enterprise insurable? For example, an ice cream parlour is built next to a cinema, hoping to profit by serving the cinema patrons. To guard against the risk of lost business resulting from the cinema being closed by a fire, the owner of the ice-cream parlour procures an insurance policy covering the cinema to the extent of his future profits. Certainly, the destruction of the cinema would cause some detriment to the parlour's business. Furthermore, the continued existence of the cinema is beneficial to the insured. It is argued that the owner of the ice-cream shop would probably lack an insurable interest. It is clear that the insured has no legally enforceable right in the cinema. Moreover, a measurable amount of the ice cream business is not morally certain to come from the cinema. In fact, even if all of the parlour's business came directly from the cinema, many variables, outside of the insured's control, will affect the number of film-goers, including, inter alia, quality and popularity of the films. It might be practically too difficult to measure the expected commercial profits. Therefore, the profits would be construed as a mere expectancy.⁸⁴⁶ However, it is submitted that an insurable interest in some mere factual expectation should be recognised if it becomes economically desirable to extend insurance protection to new types of interest.⁸⁴⁷ In absence of the factual expectation theory, some legitimate insurance need may be barred from development.⁸⁴⁸

Second example: Another example is that of a son who may inherit his father's property wishes to purchase insurance on his father's property. The question is to what extent of future expectation the son can insure. In future, the father may leave him nothing by donating all of the property to charity when he actually passes away. However, it is believed that there is nothing to stop the parties to an insurance contract from fixing a certain amount of recovery at the time of inception. Valued policy will help to overcome the difficulties of measurement.

⁸⁴⁶ Pinzur, "Insurable interest: a search for consistency", (1979) 46 Ins.Counsel J. 109, p123

⁸⁴⁷ Pinzur, "Insurable interest: a search for consistency", (1979) 46 Ins.Counsel J. 109, p123;

⁸⁴⁸ Pinzur, "Insurable interest: a search for consistency", (1979) 46 Ins.Counsel J. 109, p124

If there is no such amount, the insured must prove his actual loss in order to recover. If he cannot prove it, he will recover nothing. The principle of indemnity is still a legal barrier to prevent a recovery exceeding the actual loss.⁸⁴⁹

Third example: The proponents of the legally enforceable right approach recognize an insurable interest in anticipated profits arising from a contract. Assume that a painter is contracted to paint a house. If the house burned down prior to painting, the contract would be impossible to perform. The painter would lose his profit on the contract and therefore has an insurable interest. The legal interest supporters would claim that the contract gives rise to a legally enforceable property interest in the expected profit.⁸⁵⁰ However, no one can be sure that the contract would have been performed in the absence of the fire. In reality, the insured may be creating a wager. He may be betting that the house will have a fire prior to his performance. That is, if the painter is in an excess demand situation- he has more houses to paint- he has suffered no loss. If the house burns down, he could merely paint for another customer.⁸⁵¹ However, this argument is not very convincing because it is contrary to business efficacy.

Conclusion

Courts have been applying the factual expectation approach in an inconsistent way. On determining the existence of an insurable interest, they adopted the factual expectation even though an insurable interest could be found in accordance with the legal right approach. On the other hand, in denying an insurable interest, they based on the legal right approach.

Academic writers have tried to list all types of insurable interest, but they could not agree with each other. Lord Waller in *Feasey* listed three types,⁸⁵² Harnett and Thornton gave a list of four types,⁸⁵³ and Vance made a list of five.⁸⁵⁴ This shows the difficulties in making a

⁸⁴⁹ R. Pinzur, "Insurable interest: a search for consistency", (1979) 46 Ins.Counsel J. 109, p127

⁸⁵⁰ Pinzur, "Insurable interest: a search for consistency", (1979) 46 Ins.Counsel J. 109, p122

⁸⁵¹ Pinzur, "Insurable interest: a search for consistency", (1979) 46 Ins.Counsel J. 109, p123

⁸⁵² (i) where the subject matter insured is an item of property, the insured must have an legal or equitable interest in the property; (ii) where the subject matter is property, but the policy extends beyond the property and covers such interest as the insured might possess; and (iii) where the insured faces loss by reason of the destruction of the insured subject matter even though he has no close relationship with the subject matter; see *Feasey v Sun Life Assurance Co of Canada* [2003] 2 All.E.R. [Comm] 587

⁸⁵³ (i) property right; (ii) contract right; (iii) legal liability; and (iv) factual expectation of damage; see Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162

⁸⁵⁴ (i) where the insured possesses a legal title to the property insured, whether vested or contingent, defeasible or indefeasible. (ii) when he has an equitable title, of whatever character and in whatever manner acquired; (iii)

complete list of types of insurable interest, which also causes uncertainty of application of the factual expectation approach.

Another problem with the factual expectation approach is that there is no reasonable degree of certainty which is the basis for determining the existence of a factual expectation interest in some circumstances.⁸⁵⁵ It must be a moral certainty, but numerous borderline cases can arise.⁸⁵⁶

In the context of complex commercial transaction or big construction projects, where the rights, obligations and liabilities owned between the parties involved are not easily specified clearly, and are usually structured according to the insurance arrangement, it is really unfair to insureds if there is a risk that the insurance contract relating to complex and legitimate transactions may be void because the present legal requirements of insurable interest are not clear.⁸⁵⁷

6. IS THE REQUIREMENT OF INSURABLE INTEREST NECESSARY?

The two approaches to the concept of insurable interest have been critically analysed. Several problems have been found in respect of theoretical and practical issues. Both approaches have built strong housings, but neither has planted a firm and fixed hold over the world of insurable interest.⁸⁵⁸ This creates uncertainty about the enforceability of the insurance contract.

The question of whether the principle of insurable interest, with all its uncertainty and complexities, is necessary in respect of indemnity insurance will be critically analysed. In this section, the following issues are critically analysed (i) complication arising from application

when he possesses a qualified property or possessory right in the subject of the insurance; (iv) when he has mere possession or right of possession; and (v) when he has neither possession of the property, nor any other legal interest in it, but stands in such relation with respect to it that he may suffer, from its destruction, loss of a legal right dependent upon its continued existence, see R. Vance, *Law of Insurance*, (2nd edn, St Paul: West Publishing Co, 1930), p161; R. Pinzur, "Insurable interest: a search for consistency", (1979) 46 *Ins.Counsel J.* 109, p114

⁸⁵⁵ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p36

⁸⁵⁶ R. Pinzur, "Insurable interest: a search for consistency", (1979) 46 *Ins.Counsel J.* 109, p116; D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p36

⁸⁵⁷ M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p208

⁸⁵⁸ R. Pinzur, "Insurable interest: a search for consistency", (1979) 46 *Ins.Counsel J.* 109, p129

of the insurable interest doctrine, (ii) whether the requirement of insurable interest effectively implements the policies underlying the requirement, (iii) whether the insurers can exploit the uncertainty of the principle of insurable interest (iv) relation and difference between the principle of indemnity and the principle of insurable interest, and (v) whether the principle of indemnity could be a sufficient barrier.

6.1. Complication arising from application of the insurable interest doctrine⁸⁵⁹

6.1.1. Difficulties of determining existence of an insurable interest and complexities of the doctrine:⁸⁶⁰

The law on insurable interest is very complex. This makes it difficult for both the insureds and insurers to understand and for judges to apply the law. Firstly, the difficulties and complexities concern the insureds who have limited interest in the insured property. Secondly, the judges also have difficulties of identifying the circumstances in which an insurable interest exists.

6.1.1.1. Problems concerning limited interests:

Complex problems sometimes arise concerning the extent to which a person who possesses either a limited interest in property or no interest at all may take out a valid insurance on it for the benefit of someone else, and recover an indemnity to the full value of the property in the event of a loss.⁸⁶¹ These problems may arise in situations relating to the limited interests of bailee and bailor, landlord and tenant, mortgagee and mortgagor, head-contractor and sub-contractor, and unsecured creditor.⁸⁶²

(i) Bailee and bailor. An example of these situations was established in a hypothetical case which is put up for discussion by the Law Commission in the Issue Paper 4. A mother insures house contents in her name. However, one room in the house is filled with belongs owned by her son who leaves them there while he is at university. Can the mother recover the value of

⁸⁵⁹ See Harnett, p1169 for problems with the factual expectation approach, unsecured creditor.

⁸⁶⁰ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p ii; J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p483; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008)

⁸⁶¹ Lee Kiat Seng, "Insurable interest in Singapore", (1997) *Singapore Journal of Legal Studies* 499, p520

⁸⁶² See also D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p41

her son's property when the house and all of the contents are destroyed by fire?⁸⁶³ It is submitted that where the mother has disclosed all material facts to the insurers, and the insurers have agreed to include the value of the son's property within the total value of the policy, the mother should be allowed to recover the full value. This is not different from the situation that the mother takes out a policy covering her own property and the son purchases his own policy, or that the mother acts as an agent for her son. It just requires more paper work, and is against commercial convenience. If the mother has not disclosed all of the material facts, she has breached the principle of utmost good faith and the principle of indemnity will limit the recoverable amount to the value of her own property which is her actual loss.

(ii) Landlord and tenant. Another example relates to the interests of landlord and tenant. The insured property, including the premises and the house contents, may be insured by the landlord on his own behalf, or by the tenant on his own behalf, or by either party on behalf of himself and the other. If the landlord and the tenant take out two separate policies covering their own interests, no problem arises. If one of them purchases a single policy insuring against risk of loss of both the premises and the house contents, it may be argued that the insured has no insurable interest in the property of the other, and he cannot recover for the full value, and hold the amount in excess of his own interest on trust for the other.⁸⁶⁴ There are two situations which should be considered: the landlord purchases insurance, and the tenant purchases insurance.

If the landlord takes out the cover, the tenant normally pays a contribution to the premium which is included in the rent in accordance with the terms of the lease. Therefore, the tenant has a right to claim for his personal loss from the insurance proceeds. The landlord cannot get more than he lost.

The more serious problem relates to the situation where the tenant takes out the cover. It is argued that the tenant's interest cannot extend to the whole value of the building. For example, the tenant only rents one floor in the building, thus, he has no legal right in the whole building. However, where the insured tenant has disclosed all material circumstances

⁸⁶³ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p43

⁸⁶⁴ *Re King* [1963] Ch 459; *Mumford Hotels Ltd v Wheeler* [1964] Ch 117; *Beacon Carpets v Kirby* [1985] Q.B 755; *Mark Rowlands Ltd v Berni Inns Ltd* [1986] Q.B 211; *British Traders' Insurance Co. Ltd v Monson* [1964] 111 CLR 86; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p81; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p148

to the insurer, he should have right to claim for the full value, and hold any excess of his actual loss on trust for the landlord. The tenant may be liable for the loss of or damage to the building because it has been accidentally burned down by him. If the tenant has not disclosed all of the material facts, he has breached the principle of utmost good faith and a part of his contract is void.

Moreover, if insurers do not wish to take this type of risk, they may decline to issue a single policy covering the interest of the landlord. Where they have agreed to insure both the interests of the landlord and tenant in a single policy, they should not be allowed to refuse to pay on the ground that the tenant has no insurable interest in his landlord's property.

(iii) Co-contractors and sub-contractors. Problems relating to a limited interest of an insured also arise in the context of large construction projects. A number of co-contractors and sub-contractors may be involved in such a project. They may directly implement construction work in the site of the project, or may only supply equipment or service to the contractors and never do any work at the site. It is commercial convenience that a single policy is arranged to cover all co-contractors and sub-contractors in respect of the project works as a whole. The problem relating to the principle of insurable interest appears. The question of why a contractor or sub-contractor may have an interest in the whole of the project works has not been answered with convincing grounds.⁸⁶⁵

In commercial practices in Vietnam's insurance market, only the head contractor is entitled to take out a single policy covering the risk of loss of or legal liability arising from the construction project as a whole. Vietnamese insurers gradually realised the complicated problems of correctly identifying who is at fault and liable for the losses. It may relate to several sub-contractors. It takes time and considerable cost to find out. These costs may be greater than the amount of money that insurers may get by the subrogation proceedings against the party at fault. Therefore, a clause of waiver of subrogation right is incorporated into the insurance policy. However, a sub-contractor is not allowed to take out a policy to cover the construction project as a whole because it is against Vietnamese insurance laws- a sub-contractor has no insurable interest in the whole of the construction project.⁸⁶⁶

⁸⁶⁵ See section 5.3.1 of this Chapter

⁸⁶⁶ For an illustration of some of the problems that may arise where a single policy is not effected for the benefit of all involved, see: *Talbot Underwriting v Nausch Hogan & Murray (The Jascon 5)* [2006] 2 All E.R 751; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and*

6.1.1.2. Difficulties of identifying the circumstances in which an insurable interest exists:

There is practical difficulty of identifying the circumstances in which an insurable interest exists. In order to determine the existence of an insurable interest, judges have to distinguish between degrees of interest, rather than kinds of interest.⁸⁶⁷ Making these distinctions leads to ambiguity and uncertainty about application of the insurable interest doctrine.⁸⁶⁸

The degree of relationship between the insured and the insured property must be sufficient to ensure that the insured is exposed to a real risk of loss if there is damage to, or loss of, the insured property.⁸⁶⁹ The loss to which the insured is exposed may be a negative financial consequence⁸⁷⁰ or deprivation of a positive financial consequence.⁸⁷¹ However, the question of what constitutes a sufficient degree of relation is difficult to answer correctly in all circumstances.

Since the early nineteenth century, courts have debated whether the insurable interest must involve formal property right (the legal interest test), or whether the interest need only involve a factual expectation of economic gain (the factual expectation test).⁸⁷² Historically, the legal interest test was preferred, but recently the factual expectation test has been increasingly applied.⁸⁷³ The debate between legal interest test and factual expectation test remains one of the most ancient yet continuing controversies caused by the insurable interest doctrine.⁸⁷⁴

Commercial Insurance Law, (Informa, 2008), ft101 at p207; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p78

⁸⁶⁷ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p484; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p187

⁸⁶⁸ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p484; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p187

⁸⁶⁹ M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p187

⁸⁷⁰ For example: cost of replacement, cost of repair, legal liability to another, etc.

⁸⁷¹ For example: loss of expected profit, freight, hire, commission, etc.

⁸⁷² *Le Cras v. Hughes*, (1782) 99 Eng. Rep. 549 (K.B.), [1782] 3 Doug. 81 (applying factual expectation test), *Lucena v. Craufurd*, (1805) 127 Eng. Rep. 630 (H.L.), [1806] 2 Bas. & P.N.R. 269 (applying legal interest test). In the 1805 case of *Lucena v. Craufurd*, two English judges famously disputed the issue.

⁸⁷³ The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008), p36; J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p486; See *Delk v. Markel Am. Ins. Co.* [2003] 81 P.3d 629, 636 (Okla.) (adopting the "factual expectations" test, but observing that American jurisdictions "are divided" on which test to use)

⁸⁷⁴ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p486

The legal interest test is easier to apply because it only looks to objective legal rule to determine the existence of a property right. However, policyholders may have many economic interests in property they do not formally own. The legal right is insufficient to measure a person's actual interest in a piece of property.

On the other hand, the factual expectation test better reflects actual interests in property because it looks beyond formal property right to one's real-world expectation in a piece of property. However, the factual expectation test usually requires that the economic expectation be substantial. Determining what counts as a substantial factual expectation involves a necessarily subjective, fact-bound, case-by-case approach. A single fact can alter whether or not the insured has an insurable interest. Therefore, it remains hopelessly difficult to apply. Neither the under-inclusive legal test rule nor the vague factual expectation standard provides a measure of insurable interest that can be both accurate and predictable.⁸⁷⁵ The failure to resolve this issue over the past two hundred years suggests an inherent and irresolvable dilemma.⁸⁷⁶

Several inconsistent judgments, with quite similar facts, have been made.⁸⁷⁷ For example, *Macaura v Northern Assurance Co.*⁸⁷⁸ and *Wilson v Jones*⁸⁷⁹, *Constitution Insurance Co of Canada v Kosmopoulos*.⁸⁸⁰ *Macaura* and *Kosmopoulos* have exactly the same facts, but the two courts had different opinions, applying two different approaches, and contradictory judgments were reached. *Macaura* and *Wilson* were both about interests of a shareholder, but the interest in *Macaura* was the insured property itself, and the interest in *Wilson* was in the venture of laying the cable. The insured in *Macaura* was not allowed to recover, but the insured in *Wilson* was. This happened because the courts leaned toward finding an insurable interest and bringing justice to the insureds. Another example of the problems is the Australian case of *British Traders' Insurance Co. Ltd v Monson*.⁸⁸¹ Professor Birds agreed with the decision of the Australian High Court,⁸⁸² but the ALRC 20 disagreed. It was

⁸⁷⁵ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p486-487; R. Pinzur, "Insurable interest: a search for consistency", (1979) 46 Ins.Counsel J. 109, p129

⁸⁷⁶ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p486

⁸⁷⁷ M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p203

⁸⁷⁸ [1925] A.C. 619

⁸⁷⁹ [1867] L.R. 2 Ex 139

⁸⁸⁰ [1987] 34 D.L.R 208

⁸⁸¹ [1964] 111 CLR 86

⁸⁸² J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p82

criticised that the insurer was able to avoid his liability at the time of loss, in spite of the fact that he had accepted premiums based on the value of the property rather than on the insured's limited interest in that property and had made a clear promise to indemnify the insured for the full value at the time of contract.⁸⁸³

With the same facts, different courts can give different judgments, and different commentators can have different opinions. This complication and disagreement is caused by the principle of insurable interest. It is suggested that the construction of the insurance policy and the surrounding circumstance are the most importance factors which should be considered. The intention of the parties will give the final answer to question of whether or not the insured can recover for the full value of the property.

6.1.2. Difficulties of giving a comprehensive definition of insurable interest

An insurance contract's enforceability depends on how the courts choose to define "insurable interest". However, it is very difficult to give a comprehensive and precise definition of insurable interest which is easy to apply, bringing a fair result to both insurers and insureds. This task of definition has been highly equivocal. Indeed, confusion over the meaning of insurable interest began with the original invention of the doctrine, and such confusion has continued over centuries to the present.⁸⁸⁴ The "legal interest" concept clearly does not include all kinds of actual interest, and is out of touch with reality in many respects, bringing injustice to insureds. The "factual expectation" concept is wide, but vague, and it still brings uncertainty about application of the doctrine. Parties to insurance contracts may look to court's judgments for guidance, but unfortunately the courts have given either little guidance or a sharp conflict of authority as to when an insurable interest may exist.⁸⁸⁵

Moreover, a number of academic writers have pointed out this difficulty.⁸⁸⁶ Issue Paper 4 stated that the rules on insurable interest are complex and not always consistent.⁸⁸⁷ Professor

⁸⁸³ ALRC 20, p76

⁸⁸⁴ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p484

⁸⁸⁵ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p488; Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1163

⁸⁸⁶ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p32-39

⁸⁸⁷ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p2

Merkin said that the law on insurable interest is a confusing and illogical mess.⁸⁸⁸ Professor Birds said that the law relating to insurable interest is arguably in need of reform.⁸⁸⁹ In MacGillivray on Insurance Law, it is recognised that it is not easy to formulate a satisfactory definition applicable to all cases.⁸⁹⁰ Templeman said that the law is difficult to analyse.⁸⁹¹

Therefore, definition of insurable interest has always been ambiguous and inconsistent. Such difficulties produce uncertainty about the ultimate validity of a given insurance contract. Parties to insurance contracts have to bargain in the shadow of uncertainty.⁸⁹² This uncertainty has a negative bad impact on insurers. It may diminish the confidence of insurers, who wish to protect their reputation, in offering new products⁸⁹³ or, in the opposite way, it may increase the motivation of insurers, who stake their reputation or are in financial difficulty, for issuing more policies with uncertainty over their enforceability.⁸⁹⁴

6.2 Does the requirement of insurable interest effectively implement the policies underlying the requirement?

The policies underlying the requirement of insurable interest are: (i) the policy against wagering in the guise of insurance, and (ii) the policy for prevention of moral hazard. Does the principle of insurable interest effectively implement these policies? This question will be critically analysed.

⁸⁸⁸ R. Merkin, “Reforming insurance law: is there a case for reverse transportation?”, p78, available at http://www.lawcom.gov.uk/docs/merkin_report.pdf

⁸⁸⁹ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p64

⁸⁹⁰ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p27

⁸⁹¹ M. Templeman, “Insurable interest: a suitable case for treatment?” in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p209; see also J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p488, he summarised the opinions of American academic writers that: **“the definition of insurable interest remains vague and inconsistent... Indeed, it has always been so:** in 1891, one treatise writer called the insurable interest doctrine **“false, artificial and confusing”**; in 1918, another scholar lamented the **“great diversity of judicial opinion”**; in 1948, another observer noted the **“sharp conflict of authority”**; and by 1986, the definition of insurable interest was still **“contradictory and vague”**.

⁸⁹² J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p488

⁸⁹³ The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008), p iii

⁸⁹⁴ J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p477

6.2.1. Concerning wagering or gambling:⁸⁹⁵

Public policy against wagering has been followed by most countries. The courts have been reluctant to enforce insurance contracts which appear to embody wagering transactions because wagering is an evil. However, it is controversial on whether the dangers of gambling in the guise of insurance still exist and whether insurable interest is still necessary to prevent them arising.⁸⁹⁶

6.2.1.1. *It is difficult to make a clear distinction between insurance and gambling. Insurance contracts always contain some measure of gambling.*

It is difficult to make a clear distinction between the valid business of insurance and the morally suspect practice of wagering.⁸⁹⁷ Insurance law has often stated that insuring is a productive example of risk-averse behaviour and wagering is an unproductive dissipation of resource.⁸⁹⁸ However, a detailed examination shows that this statement is not entirely true. Distinction between insurance and gambling is the product of law and culture, and not axiomatic.⁸⁹⁹

⁸⁹⁵ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1179-1184

⁸⁹⁶ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p18

⁸⁹⁷ The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008), p5; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p140

⁸⁹⁸ **"While courts seldom have deigned to consider in detail the basic social values implicit in the policy against wagering, non-legal analysts have constructed a reasonable justification for the policy.** On the economic level the theory of diminishing marginal utility operates against the wager. Assume X, possessing a capital of \$5000, wagers \$1,000 against \$1,000 of Y's capital. Further assume ideally fair conditions so that X has a legitimate one to one chance of winning the wager. If X loses, his capital will be reduced to \$4,000, and if he wins it will be increased to \$6,000. However, in reality he will lose more if his capital is reduced to \$4,000 than he will gain if his capital is increase to \$6,000. This is so because the fifth thousand of his capital provides for more urgent needs than the sixth thousand- that is, the more capital a man possesses, the less relatively important the addition of further capital becomes... Assuming the validity of the policy against wagering, it is however, pertinent inquire as to the relationship between wagering and insurance, in order that evaluation may be made of the extent to which the policy against wagering should be carried over into insurance law. **While a perfectly fair wager is demonstrably unsound from purely economic view point, the insurance contract is not unsound, and in fact produces a net gain to society.** Assume that X procures a \$5,000 policy of fire insurance for a premium of \$50. Further assume ideally fair conditions such that the chance of the destruction by fire of the \$5,000 worth of property is one in one hundred. The bargain is then sound, because the \$5,000 X may lose by fire represents a greater loss in terms of sacrifice in marginal utilitarian terms than one hundred times he loss of the \$50 required to pay the premium." See Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1179-1181

⁸⁹⁹ J. Davey, "The reform of gambling and the future of insurance law", (2004) *Legal Stud.* 507, p507; R. Kreitner, "Speculations of contract, or how contract law stopped worrying and learned to love risk", (2000) 100 *Colum.L.Rev.* 1096, p1127

Contracts of insurance and wagers both specify that payment under them depend on an uncertain event or date. In a wager, neither of the parties has an interest in the contract or the event, other than the sum of money or the stake they win or lose. In an insurance contract, the policyholder suffers a loss if the subject matter of insurance is destroyed.⁹⁰⁰ The distinction between the two types of contract is based on the 'valuable' relationship between the prospective insured and the subject matter of insurance. However, that relationship has expanded greatly with the growth of economic activities. It has blurred the border between the two.

It has been argued that if the scope of wagering is clarified, it will help to determine the scope of insurable interest,⁹⁰¹ because valid insurance is defined as any insurance that does not promote wagering. The question turns out to be: what is wagering?

A wagering contract can be defined as "one by which two persons, professing to hold opposite views touching the issue of a future certain event, mutually agree that, dependent upon the determination of that event, one shall win from the other, and that other shall pay or hand over to him, a sum of money or other stake; neither of the contracting parties having any other interest in that contract than the sum or stake he will so win or lose, there being no other real consideration for the making of such contract by either of the parties."⁹⁰² Unfortunately, this definition is too wide for drawing a fine line between wagering and insurance. A wagering contract is defined by negative reference to an interest.⁹⁰³ It is a vicious circle. The question of where the line is to be drawn between them is not easy to answer.

If an insurable interest is required to enforce an insurance contract, an insurance contract can fall into three categories: contracts supported by an insurable interest, wager contracts, and contracts that are not wagers but that nevertheless lack an insurable interest.⁹⁰⁴ Whether the legal right approach or the factual expectation approach is followed, there are still some

⁹⁰⁰ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p5

⁹⁰¹ Lord Ellenborough, in *Robertson v Hamilton* [1811] 14 East 522, p533, stated: "the scope of the evil of wagering determined the scope of the insurable interest: light begins where darkness stops."; see also *The Moonacre* [1992] 2 Lloyd's Rep 501, p510; *O'Kane v Jones [The Martin P]* [2004] 1 Lloyd's Rep 389; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p139

⁹⁰² Per Hawkins J in *Carlill v Carbolic Smoke Ball* [1892] 2 QB 484, p490-491; see also Clarke; Lee Kiat Seng, "Insurable interest in Singapore", (1997) *Singapore Journal of Legal Studies* 499, p528 – see note 96 for critical analysis of other writers on the difference between wagering and insurance contract.

⁹⁰³ Lee Kiat Seng, "Insurable interest in Singapore", (1997) *Singapore Journal of Legal Studies* 499, p529

⁹⁰⁴ H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p78

contracts falling into the third category.⁹⁰⁵ The third category makes it difficult to clearly distinguish between an insurance contract and a wager.

If preventing an insured from obtaining a policy in the guise of an insurance contract is an important concern in the context of insurance contracts, the narrow definition of insurable interest has completely failed to solve the problems.⁹⁰⁶ Some actual pecuniary interests are excluded by the legal interest concept. It brings injustice to an insured who has actually suffered economic losses resulting from destruction of the insured property, and cannot recover the losses under his policy.⁹⁰⁷ Such an insured takes out an insurance policy to protect himself against a real possibility of economic loss, not to gain the possibility of an unjust enrichment.⁹⁰⁸ Indeed, it is only a requirement of paper work, if the policy was effected in the name of another person, the insured would be indemnified for his loss. It is suggested that “the policy against wagering is satisfied by any valuable relationship which equals the pecuniary value of the insurance, regardless of the legal nature of that relationship.”⁹⁰⁹

6.2.1.2. Insurers themselves can prevent gambling in the guise of insurance:

The insurers themselves have the ability to prevent gambling in the guise of insurance. They can do this job better than the courts would have done and better than if the principle of insurable interest had been operating as a legal barrier. It is the insurers who, in practice, decide what risks are to be taken.⁹¹⁰ In order to issue a policy, the insurers can ask the insureds about all material information or circumstances relating to the risk. They also can make an enquiry as to whether there is sufficient possibility of indemnity loss before a contract is made.⁹¹¹

⁹⁰⁵ *Macaura v Northern Assurance Co.* [1925] A.C. 619; factual case

⁹⁰⁶ *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208,

⁹⁰⁷ *Macaura v Northern Assurance Co.* [1925] A.C. 619

⁹⁰⁸ In a commentary on the case of *Aqua-Land Exploration Ltd. v. Guarantee Co. of North America* [1966] 54 D.L.R 299, it was asserted that: “A corporation that has advanced \$30,000 to designers of a marine drilling rig is not affronting any social anti-gambling norms by insuring the rig. If there is a “gamble” involved, it is in backing technological development- a highly regarded activity.” see C. Brown and J. Menezes, *Insurance Law in Canada*, (Carswells, Toronto, 1982), p71

⁹⁰⁹ Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 Col.I.R. 1162, p1181

⁹¹⁰ J. Davey, “The reform of gambling and the future of insurance law”, (2004) Legal Stud. 507, p513

⁹¹¹ The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008), p vi

Insurers are able to classify risks by collecting a large number of data and transferring them into the basis of probabilities.⁹¹² Insurance has become an exact science in which prediction can be made with all the certainty of mathematical calculations.⁹¹³ Moreover, professional institutions that collect statistics and group instances, transforming them into predictable and measurable risks will give insurers certain strong bases to do business on the insurance market.

It is suggested that if insurers, with all above-mentioned tools to assist them in making a decision on whether or not to issue a policy, still make a contract in deliberate terms which covers an insured property in a specific situation, they should be bound by their promises, and should not be allowed to put up the defence of lack of insurable interest, and to refuse to pay to their insured.⁹¹⁴

The legal consequences of application of the principle of insurable interest are really unfair to an insured. It punishes a policyholder who seems to have no insurable interest, and gives benefits to the insurer, irrespective of the relative fault of the parties.⁹¹⁵ An insurer who deliberately enters into an insurance contract is later able to plead his own negligence as a defence when the insured perils occur. He may or may not return the premiums, and is not required to indemnify the insured. Actually, he is put in the position of losing nothing, even though he is at fault.

6.2.1.3. There are many convenient devices for gamblers other than taking out an insurance policy to gain benefit. It takes a lot of time and several documents must be prepared to submit to insurance companies.

The risk of insurance contracts being used to make a gambling transaction could be overestimated.⁹¹⁶ Property insurance is not commonly contemplated as a wagering transaction because property insurance is a contract of indemnity in which recovery is limited by the amount of loss. Usually, an insured takes out insurance not for any wagering purpose but to assure him of financial protection in the event the subject matter of the insurance is

⁹¹² R. Kreitner, "Speculations of contract, or how contract law stopped worrying and learned to love risk", (2000) 100 Colum.L.Rev 1096, p1128 n146

⁹¹³ R. Kreitner, "Speculations of contract, or how contract law stopped worrying and learned to love risk", (2000) 100 Colum.L.Rev 1096, p1128

⁹¹⁴ Per Mance J. in *Cepheus Shipping Corp. V Guardian Royal Exchange Assurance (The Capricorn)* [1995] 1 Lloyd's Rep 622, p641

⁹¹⁵ R. Merkin, "Gambling By Insurance – A Study of the Life Assurance Act 1774" (1980) 9 Anglo-American L.R. 331, p339

⁹¹⁶ *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208

destroyed.⁹¹⁷ Moreover, it takes a lot of time to make a claim against insurers and several documents must be prepared to submit to them. Many more convenient devices, with far greater chance of fortuitous success, are available to serious gamblers, without them having to take out an insurance policy to gain benefits.⁹¹⁸

*6.2.1.4. It is no longer public policy to prevent gambling; instead public policy is to regulate it.*⁹¹⁹

Gambling is increasingly widely accepted, and it is no longer public policy to prevent gambling; instead, public policy is to regulate it.⁹²⁰ The question should not be whether or not a contract is gambling or insurance, it should be displaced into the question of how the contract should be regulated.⁹²¹ Regulations can limit the harmful social consequences of gambling.⁹²² Moreover, specialised committees can be established and given power to govern and distinguish wager and insurance.⁹²³ Gambling transactions have been regulated at a level that was unthinkable when the original legislation requiring insurable interest was passed.⁹²⁴ If gambling is effectively governed by laws, it can be a productive economic venture, at least as much as any of the rest of the entertainment industry.⁹²⁵

6.2.1.5. In indemnity insurance, the distinction between insurance contracts and gambling contracts for purposes other than enforcement can be drawn by the principle of indemnity.

⁹¹⁷ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1183

⁹¹⁸ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p140; Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 Col.I.R. 1162, p1181; see also *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208

⁹¹⁹ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p54

⁹²⁰ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p54; D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p44; for more details on this issue, see R. Kreitner, "Speculations of contract, or how contract law stopped worrying and learned to love risk", (2000) 100 Colum.L.Rev 1096; "it had become apparent that the anti-wagering laws served no useful purpose." See R. Merkin, "Reforming insurance law: is there a case for reverse transportation?", para 8.7 available at <http://www.lawcom.gov.uk/docs/merkin_report.pdf>

⁹²¹ R. Kreitner, "Speculations of contract, or how contract law stopped worrying and learned to love risk", (2000) 100 Colum.L.Rev 1096, p1137; The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p54

⁹²² R. Kreitner, "Speculations of contract, or how contract law stopped worrying and learned to love risk", (2000) 100 Colum.L.Rev 1096, p1127

⁹²³ Such as Gambling Commission and FSA in UK; see also: The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p54

⁹²⁴ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p54

⁹²⁵ R. Kreitner, "Speculations of contract, or how contract law stopped worrying and learned to love risk", (2000) 100 Colum.L.Rev 1096, p1137

In indemnity insurance, the distinction between insurance contracts and gambling contracts for purposes other than enforcement can be drawn by the principle of indemnity.⁹²⁶ If the policyholder cannot prove his loss when the insured perils occur, then the principle of indemnity prevents him from recovering.⁹²⁷ Put it in a different way, if an insured takes out a policy without any kind of interest in the insured property, he cannot recover under it.

Harnett and Thornton stated that the principle of indemnity “is not in any sense an independent policy, but merely another head of the hydra that is the policy against wagering. To the extent that a possible insurance recovery is in excess of the insured’s interest, it is a wager, and limiting indemnity to the extent of the interest is simply the way in which an insurance contract is removed from the wager category.”⁹²⁸

6.2.2. Concerning moral hazard:⁹²⁹

At first, the traditional logic behind the insurable interest doctrine, that of preventing moral hazard, appears quite compelling. However, a closer analysis will reveal that there is an imprecise link between the legal definition of insurable interest and the actual presence of moral hazard.⁹³⁰

6.2.2.1. Even if the requirement of insurable interest still exists, the insured who has an insurable interest still has an incentive to destroy his property

It is believed that where the insured has an insurable interest, he will be less tempted to destroy the insured property. However, it is doubtful whether the presence of an insurable interest has the effect claimed. A person who has an interest may also have a reason to destroy the property, for example, to convert an asset which is difficult to sell into cash, or a piece of property that the owner never liked in the first place may be at risk. In addition, insurance cover may make the insured careless.

⁹²⁶ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p39; J. Davey, “The reform of gambling and the future of insurance law”, (2004) Legal Stud. 507, p512

⁹²⁷ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p42

⁹²⁸ Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 Col.I.R. 1162, p1183

⁹²⁹ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p138; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p138; Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 Col.I.R. 1162, p1182

⁹³⁰ D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p17; J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p483

A person who has no interest might find it difficult to obtain a policy. If he obtained a policy but concealed his lack of interest, he would not be able to recover because of non-disclosure. Hence it is doubtful whether the moral hazard provides a sufficient justification for the legal requirement of insurable interest.⁹³¹

Even if the requirement of insurable interest has the objective of minimizing the insured's incentive to destroy the subject matter of insurance, it could be difficult to draw a fine line between a situation where an insured only has a moral certainty of loss or prejudice and a situation where an insured actually stands in some form of legal or equitable relation to the subject matter of insurance. There are many cases in the law reports where fraud is still practised on insurers despite the existence of such legal or equitable relation. It is not clear that temptation in one situation is necessarily greater than in the other.⁹³²

It has been said that if the insured has no interest at all in the insured property, he is likely to destroy the property in order to obtain the insurance monies. However, it is unlikely that he can actually destroy it.⁹³³ He is not usually in possession or control of the property. It is more difficult for him to commit the destructive act than for an insured with an insurable interest, who is in possession of his own property. The insured with an insurable interest has intimate access to it, and is able to systematically plan the fraud and carry it out. Moreover, if a policyholder does destroy an insured property, he will commit a criminal offence. The criminal laws will serve as a powerful deterrent against such conduct. Thus, it is questionable to assume that the requirement of insurable interest minimizes the insured's motivation to destroy the insured property. It may well in fact increase it.⁹³⁴

6.2.2.2. *Insurers themselves can prevent moral hazard:*

The issue of moral hazard should be left to the market. The insurers themselves are able to set the degree and kind of risk that they are willing to assume, and they should be responsible for

⁹³¹ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p138

⁹³² Lee Kiat Seng, "Insurable interest in Singapore", (1997) *Singapore Journal of Legal Studies* 499, p503; see also: R. Merkin, "Gambling By Insurance – A Study of the Life Assurance Act 1774" (1980) 9 *Anglo-American L.R.* 331, p333; *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 209, p224, per Wilson J

⁹³³ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 *Col.I.R.* 1162, p1183

⁹³⁴ Harnett and Thornton, "Insurable interest in property: a socio-economic re-evaluation of a legal concept" (1948) 48 *Col.I.R.* 1162, p1183; see also *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208

not issuing policies which encourage moral hazard.⁹³⁵ Market pressures give the insurers significant incentives to reduce unbearable moral hazard on their own, and they are better able to do so than the courts.

Insurers are able to classify risks by collecting a large number of data and transferring them into the basis of probabilities.⁹³⁶ Professional institutions can help the insurers to do this job. Insurance has become an exact science. The insurers have strong bases to decide whether or not to take certain types of risk.

In indemnity insurance, for example, an individual specific instance of demolition of a building by fire is unpredictable, but an institution can group a large number of instances, and it can treat the results as the basis of probabilities, or all insurers can group together the instances of demolition of buildings by fire. It is uncertain for the individual but highly certain for large groups on the basis of actuarial statistics.⁹³⁷

Similarly, in life insurance, which is considered as having greater potential for moral hazard, insurers are also able to do this job quite well. For example, life insurance does not usually cover suicide. However, insurers have found out that the chance of suicide is small after purchasing a life insurance for a year, and they can take that risk.⁹³⁸ A celebrity who can use her hands as a model in television advertisements is able to insure her hands for five million pounds,⁹³⁹ but an ordinary person cannot do so, because insurers normally refuse to cover.

It is submitted that the issue of reducing moral hazard primarily depends on the construction of the contract and the intention of the insurers.⁹⁴⁰ In the leading English case of *Beresford v Royal Ins Co Ltd*,⁹⁴¹ Lord Atkin stated that on “ordinary principles of insurance law, an assured cannot by his own deliberate act cause the event upon which the insurance money is payable. The insurers have not agreed to pay on that happening. The fire assured cannot

⁹³⁵ M. Clarke, “Insurance of wilful misconduct- the court as keeper of the public conscience” (1996) 7 I.L.J 173, p191

⁹³⁶ R. Kreitner, “Speculations of contract, or how contract law stopped worrying and learned to love risk”, (2000) 100 Colum.L.Rev 1096, p1128 n146

⁹³⁷ R. Kreitner, “Speculations of contract, or how contract law stopped worrying and learned to love risk”, (2000) 100 Colum.L.Rev 1096, p1128 n146; J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p505

⁹³⁸ M. Clarke, “Insurance of wilful misconduct- the court as keeper of the public conscience” (1996) 7 I.L.J 173, p176

⁹³⁹ BBC News

⁹⁴⁰ M. Clarke, “Insurance of wilful misconduct- the court as keeper of the public conscience” (1996) 7 I.L.J 173, p176

⁹⁴¹ [1938] AC 586

recover if he intentionally burns down his house, nor the marine assured if he scuttles his ship, nor the life assured if he deliberately ends his own life. This is not the result of public policy, but of the correct construction of the contract.”⁹⁴²

Last but not least, insurers always have a business mentality. They will do their best to prevent their own losses in doing business. They will take notice of a possibility of standing to lose by destruction of a particular property or of a continual state of sustaining losses in relation to certain types of risk. They themselves will not issue to a large number of insureds the policy which attaches to a great risk that the insured property is likely to be destroyed.⁹⁴³ When they suspect that there is potential of fraud, or criminal offence, they can notify the police to make an investigation.⁹⁴⁴ They themselves can do a good job of reducing moral hazard.

6.2.2.3. *The criminal laws will do the job*

Certainly, insurance policies should not give someone an incentive to destroy someone else’s life or property, and it is also commonly recognised that a policyholder should not receive insurance payments earned through crime or fraud. However, it is submitted that tort, fraud, and criminal law can reduce that incentive of policyholders, and will punish policyholders found to have committed wrongdoing.⁹⁴⁵ The apprehension of being punished for committing a criminal offence is a powerful force for preventing policyholders from committing misdeeds. Brown and Menezes stated that: “insurance concepts cannot on their own prevent deliberate causing of loss. The primary burden for discouraging anti-social activity lies with the criminal justice system. Insurance principles cannot eliminate arson or murder any more than banking legislation can eliminate armed robbery.”⁹⁴⁶

⁹⁴² *Ibid*, p604

⁹⁴³ Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 Col.I.R. 1162, p1183

⁹⁴⁴ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p138

⁹⁴⁵ J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p483

⁹⁴⁶ Brown and Menezes, p74; *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208, p27

*6.2.3. Creating unfairness and reducing the economic efficiency of the insurance market.*⁹⁴⁷

As discussed above, because it is difficult to give a precise definition of insurable interest,⁹⁴⁸ the requirement creates a gap between the insurance contracts which are strongly supported by an insurable interest and the insurance contracts which have an absolutely unbearable level of moral hazard. Some insurance contracts which lack an insurable interest as the law requires but do not create an unbearable amount of moral hazard fall into this gap.⁹⁴⁹

For those contracts which do not carry a high risk of moral hazard, and have no socially harmful effect, the insureds may desire to seek a financial protection and the insurers may be willing to provide it. However, the doctrine is a barrier to prevent the parties from entering into such contracts because it has been seen that the doctrine has invalidated a number of insurance contracts where no unbearable moral hazard actually exists.⁹⁵⁰ When both the insureds and insurers are prevented from engaging in the mutually beneficial insurance contracts, the requirement creates inefficiency in the insurance market.⁹⁵¹

The uncertainty of enforceability of those contracts also gives a subsidy to insurers who accept higher risk, and creates an incentive for the insurers to over-insure. This is so because the insurers are allowed to hold an option to breach the contract without paying damages. Uncertainty about the ultimate validity of a contract with questionable insurable interest permits insurers to enter into contracts that have a higher risk of moral hazard and appear valid to policyholders, but may nonetheless be deemed invalid by courts. The potential for invalidation decreases the value of the insurance contract to the insureds but increase the value to the insurers.⁹⁵² When a policy is issued, the insurers may act in good faith, and have no desire to take action to invalidate the contract for lack of an insurable interest, but the ability to take the action can become desirable if circumstances change at a later time.⁹⁵³ If the insured event never happens, the insurers have no need to exercise their option. If the event does happen, they can exercise it.

⁹⁴⁷ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p498-499

⁹⁴⁸ See section 6.1.2 of this Chapter

⁹⁴⁹ *Ibid*, p498

⁹⁵⁰ *Ibid*, p501

⁹⁵¹ *Ibid*, p498

⁹⁵² J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p478

⁹⁵³ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p495

6.3. Insurers abuse the uncertainty of the principle of insurable interest in practice

The unintended consequences of uncertainty about enforceability of insurance contracts may give insurers a chance to get unfair benefits. It puts them into of position of “all to gain, nothing to lose”.

6.3.1. Insurers issue more policies to get unfair benefits

The uncertainty about the insurable interest doctrine’s application actually creates an opportunity for insurers to exploit the policyholders.⁹⁵⁴ When an insurance policy is considered as invalid for lack of insurable interest, the insurers are under no obligation to pay out their promised compensation. The prospect that an insurance policy will be declared void gives insurers who are in financial troubles, or do not care so much about their business reputation, a motivation for issuing more policies with questionable insurable interest to policyholders. It is a kind of gambling for such insurers. If the contract in question is treated as valid by the courts, the insurers will indemnify their insureds in accordance with their promises under the contract, and they will bear the loss for which they are prepared and have comprehensive knowledge at the time of inception. If the contract is declared void, the insurers do not need to pay out, and they will not bear the loss. The insureds have to bear the loss even they had purchased insurance, and they have found out that unfortunately their insurance policy is worthless. The insurers will be in a better position if the contract is invalidated than if the contract is enforced. Therefore, the prospect that an insurance policy will be declared void reduces the expected cost of an insurance contract to the insurers.⁹⁵⁵

It was suggested that although insurers sometimes complained about the uncertainty of the doctrine’s application, and requested a precise definition of insurable interest,⁹⁵⁶ and put significant energy into distinguishing insurance from gambling,⁹⁵⁷ they were actually

⁹⁵⁴ J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p478

⁹⁵⁵ J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p491; for critical analysis in more details using economic tools, see *Ibid*, p491-494

⁹⁵⁶ ALRC Report 91, p? or The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008)?

⁹⁵⁷ In relation to claims for loss of goods prior shipment, “some insurers have distinguished so called ‘trade’ or ‘commercial’ risk from insurance risks and stated that under FOB terms where goods are clearly not shipped or there is loss prior to shipment the insured should be able to claim only against the seller as the matter is a trade dispute and `nothing to do with insurance. The Commission suggests that this is an artificial distinction, especially from the perspective of an insured business. While insurers may have good commercial reasons to choose not to insure certain risks of trade, this does not constitute a sufficient justification for legislatively

partially instrumental in keeping the uncertainty of the doctrine's application and the link between gambling and insurance alive in law by using the doctrine as a technical defence against payment on certain claims.⁹⁵⁸ Loshin pointed out the two steps which can be used by insurers to exploit inexperienced insureds: "first, sell your customer an insurance contract with as much wilful indifference to insurable interest requirements as doctrinal ambiguity will allow. Second, if the insured event comes to pass, claim that the contract had no insurable interest after all and escape obligation for payment."⁹⁵⁹

It is even worst for insureds because it is not clear whether they are able to get the premiums back.⁹⁶⁰ The courts have conflicting opinions about this issue.⁹⁶¹ In practice, the insurers only have to refund the premiums if they have been found guilty of fraud for inducing the insureds to make the contract.⁹⁶² If the insurers are not required to refund the premiums, only the insureds are penalised. They are not indemnified for their financial loss, and not able to recover the premiums, whereas the insurers retain the premiums and have assumed no risk at all.

6.3.2. It is difficult to prove that the insurers have not acted in good faith

It may be argued that the insurers who exploit inexperienced insureds have not acted in good faith, and that they should be punished by law and liable for their insureds' losses. Unfortunately, however, it is difficult to prove that the insurers have not acted in good faith.⁹⁶³ In order to prove it, the insureds must show evidence that the insurers had awareness of lack of insurable interest or that the insurers had intentionally and recklessly disregarded

hindering such insurance. There are many insurable risks during transit that involve commercial risks and commercial claims against third parties such as sellers and carriers." see ALRC Report 91, para 11.81

⁹⁵⁸ R. Kreitner, "Speculations of contract, or how contract law stopped worrying and learned to love risk", (2000) 100 Colum.L.Rev 1096, p1115-1116; J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p495

⁹⁵⁹ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p495

⁹⁶⁰ M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p216

⁹⁶¹ *American Mutual Life Insurance Co. v Mead* [1906] 79 N.E. 526; *Commonwealth Life Insurance Co v George* [1947] 28 So. 2d 910; J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p490

⁹⁶² *British Workman's and General Assurance Co v Cunliffe* [1902] 18 Time. L.R 425; *Harse v Pearl Assurance Co* [1904] 1 K.B 558; M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p216

⁹⁶³ R. Kreitner, "Speculations of contract, or how contract law stopped worrying and learned to love risk", (2000) 100 Colum.L.Rev 1096, p1126; J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p501-502

the actual existence of insurable interest.⁹⁶⁴ Yet, in the light of uncertainty surrounding the principle of insurable interest, it is difficult to obtain that evidence. Insurers are always able to use ambiguity in the principle to argue that they have been actually acting in good faith.⁹⁶⁵ It has come to be concluded that “determining whether a contract is entered into in good faith turns out to be as difficult, and as dependent on social consequences and cultural values as the distinction between wagers and insurance was in the first place.”⁹⁶⁶

It is submitted that the doctrine of insurable interest tends to undermine the underlying aims it purports to advance- against moral hazard and wagering. Indeed, the doctrine encourages unfairness and inefficiency in the insurance market, and it may do more harm than good. Serious consideration should be required in respect of abandoning the doctrine.⁹⁶⁷

6.4. The principle of indemnity and the principle of insurable interest⁹⁶⁸

The principle of insurable interest is derived from the principle of indemnity. In indemnity insurance, the principle of indemnity requires that the insured has suffered a loss in order to recover under the policy; therefore, the insured must have an insurable interest in the subject matter of the insurance or exposure to legal liability for the loss of another in order to have a valid claim.⁹⁶⁹ Although the two principles are different, in indemnity insurance, they serve the same purposes.⁹⁷⁰

6.4.1. Similar effects in respect of application of the two principles:

The principle of indemnity is a fundamental principle in insurance laws. It expresses several public concerns, such as the need to control the risk, the need to minimize moral hazard, the

⁹⁶⁴ J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p502

⁹⁶⁵ *Anderson v Continental Insurance Co.* [1978] 271 N.W.2d 368; *Bankers’ Reserve Life Co. v Matthews* [1930] 39 F.2d 528; *Prudential Insurance Co. of America v Williams* [1914] 168 S.W. 1114; *Warnock v Davis* [1881] 104 U.S 775; *Finnie v Walker* [1919] 257 F. 698; “...good faith is not only futilely ambiguous, but also positively misleading... The phrase ‘good faith’ is valueless as a universal test of insurable interest.” see R. Kreitner, “Speculations of contract, or how contract law stopped worrying and learned to love risk”, (2000) 100 Colum.L.Rev 1096, p1126

⁹⁶⁶ *Ibid*, p1126

⁹⁶⁷ J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p477

⁹⁶⁸ J. Long, “The concept of insurable interest and the Insurance Law Reform Act 1985”, (1992) 7 Auckland Univ L Rev 80, p83, ALRC 20, p70

⁹⁶⁹ J Lowry and P Rawlings, *Insurance Law: Cases and Materials*, (Hart Publishing, Oxford, 2004), p641

⁹⁷⁰ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p138; R. Kreitner, “Speculations of contract, or how contract law stopped worrying and learned to love risk”, (2000) 100 Colum.L.Rev 1096, p1116, n93

need to prevent gambling in the guise of insurance, and the need to allocate the risk fairly.⁹⁷¹ In order to implement those public policies, several subsidiary principles were established, one of which is the principle of insurable interest. The rationale behind the principle of insurable interest is to prevent moral hazard and gambling. The principle of indemnity addresses the question of whether or not the insured has suffered an actual economic loss. The principle of insurable interest addresses the question of whether or not the insured has an insurable interest in the subject matter of insurance. The principle of insurable interest can be considered a “second door”, working together with or being a statutory affirmation of the principle of indemnity, to prevent moral hazard and gambling in the guise of insurance.

6.4.2. Difference between insurable interest and indemnity:⁹⁷²

*The question of indemnity is of importance only where a loss has occurred, and in quantifying the loss. In contrast, the question of insurable interest is to ensure that an insured who has no prospect of suffering a loss is prevented from insuring in the first place.*⁹⁷³ At the time of inception, the insured is also required to disclose all material facts relating to his interests in the subject matter of insurance in accordance with the principle of utmost good faith. Those material facts will help the insurer to understand about the risk and to decide whether or not he will enter into the insurance contract. In this respect, the principle of utmost good faith can assist the insurer to prevent an insured who has no prospect of suffering a loss from insuring in the first place.

The principle of insurable interest takes a further step. It allows the insurer to deny a claim for lack of an insurable interest at the time of loss. It acts like a “second door”, giving the insurer extra protection. In addition, even if there was no statutory requirement of insurable interest, the insured is still required to prove his actual loss in compliance with the principle of indemnity. If the insured fails to show his loss, the insurer’s obligation to indemnify cannot arise.

*The principle of indemnity takes effect as an implied term in the agreement between the parties, whereas the rules of insurable interest are statutory.*⁹⁷⁴

⁹⁷¹ M. Baer, “Recent developments in Canadian law: Insurance law”, (1990) 22 Ottawa L Rev 387, p391

⁹⁷² R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p137

⁹⁷³ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p138

⁹⁷⁴ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p138

The principle of indemnity can be waived, while the principle of insurable interest cannot be waived. In accordance with the indemnity principle, if the parties to an insurance contract give a fixed amount of compensation at the time of inception, the insured is not required to demonstrate the amount of his loss when the insured perils occur. Where the parties may agree that the policy is a valued one, the insured is allowed to recover an amount in excess of his actual loss for his own benefit or for the benefit of other interested parties.⁹⁷⁵

However, it remains open to the insurer to refuse to make the payment on the ground that the insured has no insurable interest.⁹⁷⁶ If there was no requirement of insurable interest, the intention of the parties to contract will prevail. The freedom of contract will make the parties consider more carefully the terms of the contract.

6.5. The principle of indemnity could be a sufficient barrier to prevent the insureds from making a profit:⁹⁷⁷

Because the principle of indemnity already ensures that an insured recovers no more than the value of his loss, it may be questioned whether the requirement of insurable interest is needed at all in respect of indemnity insurance. The following section presents arguments supporting the view that, in indemnity insurance, the principle of insurable interest can be eliminated and the principle of indemnity could be a sufficient barrier.

6.5.1. The rules on insurable interest are complex, uncertain and unpredictable and need for reform.

This is a key driver for reform. The uncertainty over enforceability of an insurance contract causes confusion among the parties who get involved in complex commercial transactions, in particular in the context of offshore and construction projects, where the rights, obligations and liabilities of the parties are often structured according to the insurance arrangements that have been made by or for each of them.⁹⁷⁸

⁹⁷⁵ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p138

⁹⁷⁶ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p138

⁹⁷⁷ ALRC 20, p72

⁹⁷⁸ M. Templeman, "Insurable interest: a suitable case for treatment?" in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p208

The courts give judgments that are inconsistent and unpredictable, creating uncertainty about application of the principle of insurable interest.⁹⁷⁹ Therefore, the courts create uncertainty about application of the principle of insurable interest and enforceability of insurance contracts that are not clearly supported by an insurable interest. The insurers can exploit this uncertainty to get premiums and refuse to fulfil their obligation to indemnify the insureds when the insured events occur.

The rules are not satisfactory when a commercial lawyer has to advise a client in complex and legitimate transactions that there is a risk that the contract might be void because the present legal requirements are not clear, but it is unlikely that the point will be taken.⁹⁸⁰ And it is even more unsatisfactory for clients, having paid for such advice, to be required to order their affairs on the basis that a significant transaction may be fatally flawed, but that with any luck no one will complain. Clearly, the law is in need of reform.⁹⁸¹

6.5.2. No clear link between the legal standard of insurable interest and the actual presence of moral hazards and gambling in the guise of insurance

The underlying rationale behind the doctrine of insurable interest is to prevent moral hazard and gambling in the guise of insurance contract. However, there is no evidence of wagering in most of the cases which have been declared to have a lack of insurable interest, and there is no close link between the principle of insurable interest acting as a barrier, and the actual presence of moral hazard. Even when the legal right approach applies, there are several cases in which the insured who had a legal property right nonetheless attempted to destroy the property to get the insurance proceeds.

⁹⁷⁹ “Sometimes interest is held to exist and on other occasions not”, D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p30; see also: J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p508

⁹⁸⁰ M. Templeman, “Insurable interest: a suitable case for treatment?” in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p208

⁹⁸¹ M. Templeman, “Insurable interest: a suitable case for treatment?” in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p208. This statement expressed Templeman’s overall consideration that the requirement of insurable interest is unnecessary in indemnity insurance, and it is more important than his own opinion in the first part of his article, which was cited by UK Law Commission in Law Commission Consultation Paper No 201, “Insurance Contract Law: Post Contract Duties and other Issues”, (2012), p128, see also: M. Templeman, “Insurable interest: a suitable case for treatment?” in Baris Soyer (eds), *Reforming Marine and Commercial Insurance Law*, (Informa, 2008), p202, to argue that there is no significant benefits from abolishing the requirement of insurable interest: “Mark Templeman QC put this point in the following terms: Few would disagree with the proposition that the law on insurable interest in indemnity insurance is uncertain. And it may be that the law merits reform for that reason alone. But if lack of clarity is the driver for reform, it may be necessary to proceed with caution. For the most part, the law in relation to insurable interest does not produce injustice. That is not to say that it never does so: on occasion it has, and no doubt (if unreformed), it will continue, on occasion to so. But it is not a major source of injustice.”

The imperfect relationship between the legal standard of insurable interest and the actual presence of moral hazards and gambling in the guise of insurance suggests that the doctrine may end up invalidating unobjectionable and mutually beneficial insurance contracts, obstructing the goal of economic efficiency in the insurance market. Not all policies deemed to lack an insurable interest create an unbearable level of moral hazard and gambling in the guise of insurance. Hence, the doctrine of insurable interest is an imperfect barrier to prevent such moral hazard and gambling, and it may do more harm than good.⁹⁸² It is suggested that the best way to fix the age-old doctrine may be simply to eliminate it.

6.5.3. The indemnity principle can prevent moral hazard and gambling in the guise of insurance⁹⁸³

The role of the principle of insurable interest is to prevent moral hazard and gambling in the guise of insurance. In support of maintaining the principle, it is argued that the inefficiency and uncertainty of the principle of insurable interest is simply a cost that must inevitably be paid in order to prevent moral hazard and gambling in the guise of insurance since these are inherent in insurance contracts. It may not be perfectly efficient but it remains the most efficient option available.⁹⁸⁴

But this is not a good argument. First, in fact, the insurers can do a better job than the courts in detecting and evaluating moral hazard and gambling.⁹⁸⁵ The insurers do not get paid to follow the laws. They get paid to sell financial certainty to the insureds.⁹⁸⁶ They have professional skills at using probabilistic terms to assess the risk of moral hazard and gambling in the guise of insurance. They have become experts at doing exactly what the insurable interest requirement asks the courts to do- to identify and avoid unbearable levels of risk.⁹⁸⁷

⁹⁸² J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p478

⁹⁸³ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p56

⁹⁸⁴ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p499

⁹⁸⁵ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p504

⁹⁸⁶ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p508

⁹⁸⁷ J. Loshin, "Insurance law's hapless busybody: a case against insurable interest requirement", (2007-2008) 117 Yale L.J 474, p508

Second, the indemnity principle could itself prevent gambling in the guise of insurance and moral hazard.⁹⁸⁸ Harnett and Thornton stated that: “limiting indemnity to the extent of the interest is simply the way in which an insurance contract is removed from the wager category”.⁹⁸⁹ The principle of indemnity shall limit recovery to the extent of the actual economic loss of the insureds. They must lose something in order to get insurance benefit. If the insureds have not suffered a loss, the insurers’ obligation to indemnify cannot arise.

In indemnity insurance, the issue of moral hazard is not very important.⁹⁹⁰ An insured cannot claim for the destruction of his insured property when it is not lost, and he only suffers a loss if he has a connection to it.⁹⁹¹ Therefore, he is prevented insofar as possible from deliberately destroying the property without any interest in its destruction. As the indemnity principle already guards against moral hazard, it is submitted that insurable interest in indemnity contract, with all of its complexities and legal requirements, is unnecessary.⁹⁹²

6.5.4. A greater role of the freedom of contract principle

The removal of the insurable interest principle enables the freedom of contract principle to play a greater role in the interpretation of the terms of the insurance contract and in encouraging the parties to stipulate fully and clearly the risks and the scope and the subject matter which is covered against.

The indemnity principle enables parties to an insurance contract to define the risk and the extent of the policy in a more effective way than the statutory requirement of insurable interest.⁹⁹³ Freedom of contract of the parties will prevail, and it brings fairness to both of the parties.⁹⁹⁴ They will be bound by what they have agreed in their contract. The insurers cannot seek the “technical defence” to invalidate the contract for lack of insurable interest when the insured perils occur. This will make the parties to an insurance contract fully clarify their

⁹⁸⁸ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p56

⁹⁸⁹ Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 Col.I.R. 1162, p1183

⁹⁹⁰ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p iv; see also Pinzur, “Insurable interest: a search for consistency”, (1979) 46 Ins.Counsel J. 109, p127

⁹⁹¹ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p iv

⁹⁹² See also ALRC 20, p72

⁹⁹³ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p56

⁹⁹⁴ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p57

intention in express terms. Those express terms help the insureds to be fully aware of the terms of the contract. It is better than the current situation, where the insureds, due to the complexity and ambiguity of the rules on insurable interest, are uncertain about the enforceability of their contract and find it worthless when the insured perils occur.

The most important factor to be considered is what subject matter was insured against what risk.⁹⁹⁵ The insurers and insureds are free to negotiate on types of loss to be insured and the recoverable amount in the insurance contract. If a loss that is suffered by the policyholder falls within the definition of loss in the contract, then there would be certainty on both sides that the contract is valid and an indemnity will be paid. The freedom of contract will increase the insurers' motivation for clearly and carefully defining the insureds' interests.

6.5.5. Elimination of the principle of insurable interest benefits both insurers and insureds:

The current rules on insurable interest are unfair to the insureds because “the insurer solicited the insurance, charged and accepted a premium, investigated the property and the insured, and then seeks to avoid its part of the bargain by considering that the insured was not entitled to coverage, though it did not make such a discovery before the loss when the prospective insured's premium was dangling before it. The majority rule is that only the insurer can raise the objection of no insurable interest.”⁹⁹⁶

It is suggested that elimination of the requirement of insurable interest will give benefits to both the insureds and insurers.⁹⁹⁷ Insureds get security against the risk of loss, and insurers can make profit which could be invested for socially beneficial purposes.⁹⁹⁸ At the social level, there is no anti-social aspect to insurance, because it is not a matter of one losing and the other gaining, rather both gain. The insureds will not suffer unfairness from invalidity of their insurance contracts. They will get the commercial benefits of obtaining effective cover for their actual economic loss. Their risk margins would reduce, their profitability would increase. The insurers also get benefits. They would be given more opportunity to do business. If there is a commercial demand for cover against new types of risk, the insurers

⁹⁹⁵ D. Rhidian Thomas, “Insurable interest: accelerating the liberal spirit” in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p18-20

⁹⁹⁶ R. Pinzur, “Insurable interest: a search for consistency”, (1979) 46 *Ins.Counsel J.* 109, p128

⁹⁹⁷ M. Taylor, “Is the requirement of an insurable interest in the Marine Insurance Act still valid”, (2000) 11 *Ins. L.J* 1, p4

⁹⁹⁸ Harnett and Thornton, “Insurable interest in property: a socio-economic re-evaluation of a legal concept” (1948) 48 *Col.I.R.* 1162, p1181

may wish to provide this product. They can avoid the uncertainty of the application of the principle of insurable interest and have a chance to enter new markets.

Moreover, in practice, even if there is statutory requirement of insurable interest, the insureds and insurers may still enter into insurance contracts which appear to lack an insurable interest.⁹⁹⁹ When the insured perils occur, the insurers still indemnify the insureds in accordance with the terms in their contracts. It means that the insurers may not consider the issue of insurable interest as crucial as they say. It has no impact on the contract under which the parties to it are willing to enter into and perform their obligations. The courts cannot “blow the whistle” and force the parties to follow the laws.

Some academic writers have argued that if the principle of insurable interest is eliminated, insurers may take higher risk, leading to uncertainty of financial market.¹⁰⁰⁰ However, the insurers only issue more risky policies with higher premiums that compensate for the high risk of loss. These high premiums make the purchase of such high risk policies unattractive, reducing moral hazard and gambling in the guise of insurance. In addition, if the insurers consider that the risk in a particular proposal which the insured wishes them to undertake is too high, they can simply refuse to cover.¹⁰⁰¹

6.5.6. Extension of the concept of insurable interest

The traditional statutory concept of insurable interest has been stretched so far in recent years, and there is no longer much difference between it and the principle of indemnity.¹⁰⁰²

Since *Lucena v Craufurd* and MIA 1906, in order to determine a sufficient insurable interest, it was required that the insured must have legal or equitable relation to the insured property. Then the element that the insured has some legal liability arising from destruction of or damage to the insured property was added in *MacGillivray and Parkington on Insurance Law*, and then another element that the insured has suffered an economic loss on destruction of or damage to the insured property, or has an economic benefit from the its preservation

⁹⁹⁹ *NSW Leather Co Pty Ltd v Vanguard Insurance Co Ltd* [1991] 25 NSWLR 699; *Kosmopoulos v. Constitution Insurance Co.* [1987] 1 S.C.R. 2

¹⁰⁰⁰ Law Commission Consultation Paper No 201, “Insurance Contract Law: Post Contract Duties and other Issues”, (2012), para 12.15

¹⁰⁰¹ J. Loshin, “Insurance law’s hapless busybody: a case against insurable interest requirement”, (2007-2008) 117 Yale L.J 474, p507

¹⁰⁰² The Law Commission and Scottish Law Commission, *Insurance Contract Law: Insurable interest Issue Paper 4*, (Law Com Issue Paper 4, 2008), p57

was approved in *Feasey v Sun Life Assurance Co of Canada*. The concept of insurable interest is still expanding.¹⁰⁰³

In addition, even if the principle of insurable interest is eliminated, the principle of indemnity requires the insured to prove his actual economic loss at the time of loss in order to be able to claim under the policy.¹⁰⁰⁴ In practice, a person who suffers a pecuniary or economic loss would often have an insurable interest.¹⁰⁰⁵ If the principle of insurable interest is still retained, it only creates uncertainty and unnecessary complexity. It is submitted that there is no significant difference between the two principles.

6.5.7. Principle of double insurance can solve any dispute relating to overlapping insurance:

The elimination of the principle of insurable interest would cause too many insurance policies on the same subject-matter of insurance. For example, in marine insurance, insurers argue that eliminating the requirement of insurable interest creates overlapping insurance because both the sellers and FOB buyers may take out policies insuring against pre-shipment loss.¹⁰⁰⁶ The sellers are more likely to resist the buyers' claim made against them, even if the sellers are in breach of contract for sale of goods. The buyers are less likely to cooperate with the insurers in claims against the sellers. Therefore, premiums for the FOB buyers would have to increase because of the reduced prospects of recovery against the sellers.¹⁰⁰⁷ However, the risks which are insured against in the buyers' policy and in the sellers' policy may be different. The FOB buyer insured should not be deprived of his legal right to recover for his actual economic losses.

Elimination of the insurable interest requirement will leave it open for the parties to the insurance contract to agree to terms which make it clear, for example, in relation to the risk of loss prior shipment, the parties may agree that the buyers' cover is subsidiary to the sellers' insurance or being limited to meeting a shortfall in other inadequate insurance;¹⁰⁰⁸ therefore, where the pre-shipment loss is covered by the sellers' policy, the sellers' insurer should be under a duty to indemnify for the loss first.

¹⁰⁰³ Law Commission Consultation Paper No 201, "Insurance Contract Law: Post Contract Duties and other Issues", (2012), p99, 112

¹⁰⁰⁴ Lee Kiat Seng, "Insurable interest in Singapore", (1997) *Singapore Journal of Legal Studies* 499, p527

¹⁰⁰⁵ ALRC Discussion Paper 63, at 7.41

¹⁰⁰⁶ ALRC Discussion Paper 63, at 7.32

¹⁰⁰⁷ ALRC Discussion Paper 63, at 7.32

¹⁰⁰⁸ ALRC Report 91, at 11.71

Even if there is the problem of one or more of the parties obtaining insurance for the same risk, or there is concern that elimination of the principle of insurable interest will lead to too much insurance,¹⁰⁰⁹ principle of double insurance can solve any dispute of this nature.¹⁰¹⁰ Living with the potential problem of double insurance is better than dealing with the uncertainties that are caused by the principle of insurable interest.¹⁰¹¹

Furthermore, the insureds are still under a duty to disclose all material circumstances to the insurers. This information will help the insurers to assess the risk to be taken. If the risk is high, they can limit their liability or charge higher premiums. If they cannot estimate the likelihood of the loss occurring, they can simply refuse to cover.¹⁰¹²

6.5.8. The principle of insurable interest has been removed from Australian insurance law

Australian insurance laws dispensed with the requirement of insurable interest in indemnity insurance nearly thirty years ago,¹⁰¹³ and no serious problem has arisen¹⁰¹⁴. Section 17 of the Australian ICA 1984 provides that when the insured suffers pecuniary or economic loss because insured property has been damaged or destroyed, the absence of an interest at law or in equity in the property at the time of loss does not relieve the insurer from liability. There are only a few noticeable cases relating to the requirement of insurable interest. In *Pacific Dunlop Limited v Maxitherm Boilers PL* (1997) 9 ANZ Ins Cases 61-357, the Supreme Court of Victoria noted uncertainty as to whether s 17 could be relied upon by a non-party insured; *Howard v Australian Jet Charter Pty Ltd* (1991) 6 ANZ Ins Cases 61-054 in which Hill J in the Federal Court held that, by virtue of ICA s 16 and 17, a company that had contracted to maintain and crew an aircraft could not have an interest in a contract of insurance covering loss from damage to that aircraft; and *Advance (NSW) Insurance Agencies Pty Ltd v Matthews* (1988) 12 NSWLR 250 in which Samuels JA found that under ICA s 17 a husband had an economic, and therefore insurable, interest in his wife's clothing and other personal effects.¹⁰¹⁵

¹⁰⁰⁹ Lord Eldon in *Lucena v Craufurd* [1806] 2 Bos. & P.N.R. 269

¹⁰¹⁰ M. Taylor, "Is the requirement of an insurable interest in the Marine Insurance Act still valid", (2000) 11 Ins. L.J 1, p5; *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208, p17

¹⁰¹¹ ALRC Discussion Paper 63, at para. 7.35

¹⁰¹² *Constitution Insurance Co of Canada v Kosmopoulos* [1987] 34 D.L.R 208, p17

¹⁰¹³ D. Rhidian Thomas, "Insurable interest: accelerating the liberal spirit" in D. Rhidian Thomas (eds), *Marine Insurance: The Law in Transition*, (Informa, London, 2006), p42

¹⁰¹⁴ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p59-60

¹⁰¹⁵ ALRC Report 91, note 104

The UK Law Commission argued that “the Lloyd’s Market Association provided anecdotal evidence of the effect in Australia of the abolition of insurable interest. It had led to an increase in fraudulent claims and a higher level of out of court settlements in non-marine business; teething litigation still continued in some areas and more fraudulent/frivolous claims were being paid or settled due to the difficulty of proving fraud.”¹⁰¹⁶ However, it can be seen that no clear evidence or serious case is given. It means that problems arising out of the abolition of insurable interest are not serious. Perhaps, the level of out of court settlements is higher, yet if the insurers are confident about the possibility of winning the case or there is no fault or weakness on their side, they will be determined to take the case to courts. If there is actual presence of fraud, criminal laws will intervene. The insurers’ difficulties of proving fraud are not sufficient ground to retain the principle of insurable interest.

7. CONCLUSION

The insurable interest principle is derived from principle of indemnity, and its main purpose is to prevent wagering and moral hazard. Both current English law and Vietnamese law contain some specific provisions to recognize this principle. The courts are also based on this principle to determine the existence of an insurable interest, and determine the right of the insureds to make a valid claim against the insurers. The insurable interest principle has become one of the most important principles of insurance law in England, and in Vietnam as well as in many other countries.

However, application of this principle has caused many difficulties for the parties to an insurance contract as well as to the judges. The traditional approach to this principle is the legal right approach. This approach seems appropriate in the early stage of an insurance market, but has become inadequate now that the insurance market is more developed and constantly changing. An insured’s claim may be rejected by an insurer on the ground that the insured does not have a legal interest in the subject matter of insurance, without regard to the fact that the insured has suffered an actual loss. This approach is too harsh and is inconsistent with the nature of the principle of indemnity.

¹⁰¹⁶ Law Commission Consultation Paper No 201, “Insurance Contract Law: Post Contract Duties and other Issues”, (2012), p126 n.4

Therefore, the concept of insurable interest has been gradually expanded, with the introduction of a new approach- the factual expectation approach. The new approach enlarges the number of circumstances in which an insurable interest can be shown. Through the factual expectation approach, economic interests are sufficient to create insurable interests, it is not necessary that the insured should have a legal interest in the subject matter of insurance.

However, the above analyses show that both approaches can create difficulties and uncertainties in their application. For example, the legal right approach prevents the insureds who have suffered actual economic losses from recovering for the losses; while, the factual expectation approach makes it difficult for judges to establish firm grounds for determining the existence of an insurable interest and difficulties in measuring the actual losses suffered by the insureds. Consequently, it is difficult to have a unified understanding and application of the principle, and different judges make different judgments for similar cases. In some awkward circumstances, the insurers are not completely sure whether the insureds have an insurable interest in order to decide to enter into an insurance contract. Some insurers may take advantage of the ambiguity and uncertainty over the application of the principle of insurable interest to make an unfair profit. They may issue policies with questionable insurable interest in order to get the premiums, and then when the insured events occur, they may refuse to indemnify the insureds on the ground of lack of insurable interest. Therefore, the inexperienced insureds who do not have comprehensive knowledge and full information about insurance laws ultimately suffer the losses.

In this context, the approach under Australia's insurance laws is worthy of notice. Australian insurance laws have dispensed with the requirement of insurable interest in indemnity insurance for nearly thirty years, and no serious problem has arisen. With reference to the Australian approach, this thesis suggests that the insurable interest principle is no longer needed in property insurance, and can be eliminated. The elimination of this principle will remove the ambiguities and uncertainties over the application of the principle. This elimination also prevents the insurers from taking advantage of those ambiguities and uncertainties to make an unfair profit. If the principle is removed, a question of how to prevent gambling in the guise of insurance and moral hazard may arise. The answer is that the insurers themselves and the principle of indemnity can do this job.

In conclusion, it is submitted that the principle of indemnity already provides protection against moral hazard and against the risk of gambling in the guise of insurance, by limiting the insureds' recovery to their actual losses. Therefore, a statutory requirement for insurable interest in indemnity insurance is not necessary.¹⁰¹⁷ Objections to reform of the insurable interest requirement are largely answerable by reference to the principle of indemnity as potential recovery is limited to actual loss. The reform will have the effect of making parties to insurance contracts think more carefully about what they are agreeing to.¹⁰¹⁸

¹⁰¹⁷ The Law Commission and Scottish Law Commission, Insurance Contract Law: Insurable interest Issue Paper 4, (Law Com Issue Paper 4, 2008), p57

¹⁰¹⁸ ALRC Report 91, at 11.85

CHAPTER 5: SUBROGATION

1. INTRODUCTION

The rationale behind the rights of subrogation is the principle of indemnity. Brett LJ in *Castellain v Preston*¹⁰¹⁹ stated that subrogation is ‘a corollary of the great law of indemnity’¹⁰²⁰. The principle of indemnity is a nucleus principle of the law of insurance.¹⁰²¹ The underlying idea of the principle of indemnity is that the insured should receive a full indemnity for his loss, but should not receive more than a full indemnity.¹⁰²² The classic statement of the principle of indemnity is that:

“The very foundation of every rule which has been applied to insurance law is this, namely, that the contract of insurance contained in a marine or fire policy is a contract of indemnity, and of indemnity only, and that this contract means that the assured, in case of a loss against which the policy has been made, shall be fully indemnified, but shall never be more than fully indemnified”.¹⁰²³

The possibility that the insured may recover more than an indemnity results from the facts that the insured who has recovered his entire loss from his insurer still takes an action against the third party responsible for the loss to claim for compensation. The reason for the insured’s right to take an action is that, in English insurance law, there is nothing to prevent the insured from bringing proceedings against the third party wrongdoer for damages, even if the insured has received a full indemnity from the insurer.¹⁰²⁴ To prevent the insured from recovering a double indemnity, the doctrine of subrogation intervenes.¹⁰²⁵ It prevents the insured from

¹⁰¹⁹ (1883) 11 QBD 380

¹⁰²⁰ Brett LJ in *Castellain v Preston* (1883) 11 QBD 380, p401

¹⁰²¹ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1056

¹⁰²² Brett LJ in *Castellain v Preston* (1883) 11 QBD 380, p386; similarly, the insurer may not recover, through the exercise of subrogation rights, more than the sum paid out under the contract. The insurer cannot also make profit from the insured’s loss- case: *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330

¹⁰²³ Brett LJ in *Castellain v Preston* (1883) 11 QBD 380, at 386; A Green, “Strengthening the insurer’s subrogation rights”, (1995) 3(10) Int.I.L.R 348, p348

¹⁰²⁴ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p499; see also *Bradburn v Great Western Railway Co* (1874) I.R 10; *Bovis Construction Ltd v Eagle Star Insurance Co Ltd* (2002) Ll.L.Rep 321

¹⁰²⁵ Brett LJ in *Castellain v Preston* (1883) 11 QBD 380, at 387: “that doctrine (subrogation) does not arise upon any of the terms of contract of insurance...it is a doctrine in favour of the underwriters or insurers in order to prevent the assured from recovering more than a full indemnity; it has been adopted solely for that reason.” In *Driscoll v Driscoll* (1918) 1 I.R. 152, p159: it is said that: “A contract of insurance against fire is only a contract of indemnity, and I think that the foundation for the doctrine of subrogation is to be found in the principle that no man should be paid twice over in compensation for the same loss.” It is for the purpose of carrying out the indemnity principle that the principle of subrogation has been adopted. In other words, in the absence of the subrogation principle, an insured may recover more than full indemnity. To prevent such a result the courts have adopted the rule that the insured shall be entitled to only one full indemnity for the loss sustained.”

unjust enrichment through the aggregation of both insurance moneys and compensation from a third-party wrongdoer.¹⁰²⁶ In other words, the insured cannot profit from his loss at the expense of either the insurer or a third party wrongdoer.

As the subrogation principle is derived from the principle of indemnity, it is applicable only to indemnity insurance contracts (principally to contracts of property, fire, motor and liability insurance).¹⁰²⁷ This principle does not apply to non-indemnity insurance, such as life insurance. The reason for this is the impossibility of measuring the value of life;¹⁰²⁸ the insured can never recover a full indemnity for his losses under a life insurance policy. Therefore, life insurance will not be discussed in this chapter.

In England, the principle of subrogation has long been governed by the common law for general insurance and section 79 of the Marine Insurance Act 1906 (MIA 1906) for marine insurance. In Vietnam, Article 577 of Vietnam's Civil Code 2005 stipulates general principles relating to subrogation, Article 49 of Vietnam's Law on Insurance Business 2000 deals with the matter of subrogation in general insurance, and subrogation in marine insurance is codified in Article 247 and Article 248 of Vietnam's Maritime Code 2005. In Vietnam, contractual subrogation is commonly incorporated into insurance policies or stipulated by subrogation and receipt forms, vesting the insurer wider rights in subrogation. However, these documents are unfortunately silent on the issue of how to allocate any subrogation recovery between the insured and the insurer if the insured has suffered an uninsured loss.

In the triangular relationship: the insured, the insurer and the third party, where the insured is fully compensated for his total loss under the insurance policy or by the third party's payment, the problem of distribution of subrogation recovery between the insurer and the insured does not arise. However, the third party payment is often insufficient to cover all the claims from the insured and the insurer, and insurance proceeds frequently do not fully compensate for damages suffered by the insured as a result of a loss. When this occurs, the insurer has a right to subrogate against the third party wrongdoer responsible for the loss, and the insured is also entitled to seek full compensation for his total loss from the third party

¹⁰²⁶ *Castellain v. Preston* (1883) 11 QBD 380

¹⁰²⁷ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p321

¹⁰²⁸ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p492

wrongdoer. In such a case a fundamental issue arises as to the distribution of any subrogation recovery between the insured and the insurer.

In this chapter, approaches to the issue of distribution of subrogation recovery between the insured and the insurer will be critically analysed. There are several approaches,¹⁰²⁹ such as: priority to the insured, priority to the insurer, and pro rata allocation. The Vietnamese approach will be critically evaluated in comparison with the English approach, to reveal the problems under Vietnamese insurance laws, and to examine whether or not the Vietnamese approach is consistent with the principle of indemnity.

Vietnamese insurance laws give priority to the insurer in pursuing subrogation recovery from the third party. There are several obstacles to the insured achieving full compensation for his total loss.¹⁰³⁰ Under Vietnamese insurance laws, there is confusion between the principle of subrogation and the principle of assignment.¹⁰³¹ This confusion causes several problems in commercial practices and judicial practices. Critical examination of the English approach can give ideas for reforming Vietnamese insurance laws, bringing Vietnamese insurance laws into compliance with the principle of indemnity.

2. THE JUSTIFICATION OF THE SUBROGATION PRINCIPLE

The subrogation principle has been developed to prevent the insured from recovering from both the insurer and a third party, which could mean double recovery or overcompensation of the insured. Subrogation is also designed to ensure that a wrongdoer who is legally responsible for the insured's loss will not be released from liability merely because the insured has been indemnified by the insurance policy. Hence, the ultimate payment of the

¹⁰²⁹ See R. Keeton, *Basic text on insurance law*, (West Publishing Co., 1971), p160-162; There are five approaches. First, the insurer is the sole beneficial owner of the claim against the third party and is entitled to the full amount recovered, whether or not it exceeds the amount paid by the insurer to the insured. Second, the insurer is to be reimbursed first out of the recovery from the third party, and the insured is entitled to any remaining balance. Third, the recovery from the third party is to be prorated between the insurer and the insured in accordance with the percentage of the original loss for which the insurer paid the insured under the policy. Fourth, out of the recovery from the third party the insured is to be reimbursed first, for the loss not covered by insurance, and the insurer is entitled to any remaining balance, up to a sum sufficient to reimburse the insurer fully, the insured being entitled to anything beyond that. If there is any windfall, it goes to the insured. Fifth, the insurer is the sole owner of the claim against the third party and is entitled to the full amount recovered, whether or not the total thus received from the third party and the insurer exceeds his loss

¹⁰³⁰ See section 3.2 and 4.1 of this Chapter

¹⁰³¹ See section 5 of this Chapter

obligation is by the person who ought to pay it. In order to understand these purposes, the meaning of subrogation and the origin of subrogation will be examined.

2.1. Definition and the meaning of subrogation

It is commonly recognised in English law that where A has fully indemnified B for loss caused by C to B under some form of agreement between A and B, A is entitled to exercise B's rights against C.¹⁰³² That is a simple example of how subrogation may arise.

Subrogation can be defined literally as 'substitution'.¹⁰³³ In an insurance context, subrogation entitles the rights of the insurer to be substituted with, and replaced by, the rights of an insured. For example, an insurer who indemnifies his insured against the loss of the subject-matter insured is entitled to substitute for the insured to bring proceedings against the third party liable for the loss.

The definition of the principle of subrogation in insurance can be founded in precise terms in the leading case of *Burnard v Rodocanachi*¹⁰³⁴. Lord Blackburn stated that:

“The general rule of law (and it is obvious justice) is that where there is a contract of indemnity (it matters not whether it is a marine policy, or a policy against fire on land, or any other contracts of indemnity) and a loss happens, anything which reduces or diminishes that loss reduces or diminishes the amount which the indemnifier is bound to pay; and if the indemnifier has already paid it, then, if anything which diminishes the loss comes into the hands of the person to whom he has paid it, it becomes an equity that the person who has already paid the full indemnity is entitled to be recouped by having that amount back.”¹⁰³⁵

It means that the insurer is entitled to take over all the rights and remedies of the insured against the third party wrongdoer for his own benefit, after having fully indemnified the assured. The insurer acquires two distinct rights¹⁰³⁶ from the insured: (i) the right to any

¹⁰³² R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p488

¹⁰³³ Compact Edition of the *Oxford English Dictionary*, (OUP, 1987) vol II, p3126; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p689; Zhen Jing, “The Confusion between Subrogation and Assignment in the Insurance Law of the People's Republic of China 1995-A Critical Analysis on Article 44 of the Insurance Law”, (2002) J.B.L. 608, p609; the mechanism is simple, as follows: the subrogee, having indemnified the injured person for the whole or part of his loss, is substituted to the latter's (subrogor's) rights against the wrongdoer.

¹⁰³⁴ (1882) 7 App Cas 333, HL

¹⁰³⁵ *Burnard v Rodocanachi* (1882) 7 App Cas 333, HL, p339; S Hodges, *Cases and Materials on Marine Insurance Law*, (Cavendish Publishing Limited, London, 2003), p17

¹⁰³⁶ *England v Guardian Insurance Ltd* (1999) 2 All.E.R. 481, p487

benefits already in the hands of the insured which extinguish or diminish the loss, (for example, the recoveries from the third party wrongdoer- covered by the doctrine of subrogation- are regarded as diminishing the loss) and (ii) the right to any cause of action which the insured may have against a third party, in relation to the said loss. The transfer of both these rights from the insured to the insurer is known as subrogation in insurance law.¹⁰³⁷

2.2. The origins of the doctrine of subrogation

There has been a lengthy and controversial discussion on the origins of the rights of subrogation¹⁰³⁸ in English law. One view is that the doctrine is derived from common law principle which is implied in every contract of indemnity by the operation of law¹⁰³⁹; the other view is that subrogation is based on rules of equity¹⁰⁴⁰.

It seems that the argument is settled in the case of *Napier v Hunter*.¹⁰⁴¹ In this case, the House of Lords held that the right of subrogation is derived from equity.¹⁰⁴² In the words of Lord Templeman: “The principles which dictated the decisions of our ancestors and inspired their references to the equitable obligations of an insured person towards an insurer entitled to subrogation are discernible and immutable. They establish that such an insurer has an enforceable equitable interest in the damages payable by the wrongdoer. The insured person is guilty of unconscionable conduct if he does not provide for the insurer to be recouped out of the damages awarded against the wrongdoer. Equity will not allow the insured person to

¹⁰³⁷ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p489

¹⁰³⁸ The origin of the doctrine of subrogation can be traced back to Roman law. In *John Edwards & Co Ltd. v. Motor Union Insurance Co. Ltd* (1922) 2 K.B. 249, it is said that the doctrine of subrogation “was derived by our English courts from the system of Roman law. The doctrine has been widely applied in our English body of law, e.g. to sureties and to matters of *ultra vires* as well as to insurance. In connection with insurance it was recognized ere the beginning of the eighteenth century.”; see also SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p4

¹⁰³⁹ *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330; and in the case of *Hobbs v Marlowe* (1978) A.C. 16, H.L at 39 Lord Diplock said: “For my own part I prefer to regard the doctrine of subrogation in relation to contracts of insurance as having its origin at common law in the implied terms of the contract and calling for the aid of a court of equity only where its auxiliary jurisdiction was needed to compel the assured to lend his name to his insurer for the enforcement of rights and remedies to which his insurer was subrogated...”

¹⁰⁴⁰ In *Randal v Cochran* (1748) 1 Ves.Sen. 98, at 99 Lord Hardwicke said that the insurer “had the plainest equity that could be.”; *Mason v Sainsbury* (1782) 3 Doug. 61; *White v Dobinson* (1844) 14 Sim. 273; *Burnard v Rodocanachi* (1882) 7 App Cas 333, HL, at 339 it is said that “If the indemnifier has already paid it, then, if anything which diminishes the loss comes into the hands of the person to whom he has paid it, it becomes an equity that the person who has already paid the full indemnity is entitled to be recouped by having that amount back.”; *Morris v Ford Motor Co Ltd* (1973) QB 792, at 801 Lord Denning said: “subrogation was an equitable remedy and could be refused where it would be inequitable.”

¹⁰⁴¹ (1993) A.C. 713

¹⁰⁴² W Gummow, “Names and equitable lien”, (1993) L.Q.R 159, p161, A Green, “Strengthening the insurer’s subrogation rights”, (1995) 3(10) Int.I.L.R 348, p348 -349; Goff and Jones, *The Law of Restitution*, (5th ed., Sweet & Maxwell, 1998)

insist on his legal rights to all the damages awarded against the wrongdoer and will restrain the insured person from receiving or dealing with those damages so far as they are required to recoup the insurer under the doctrine of subrogation.”¹⁰⁴³

The doctrine of subrogation stemming from the operation of equity can give strong grounds for the following circumstances. Firstly, the insurer’s subrogation right is possibly denied by the court if the exercise of subrogation is inequitable.¹⁰⁴⁴ Secondly, the general equitable principle of the doctrine of subrogation should not be capable of being modified or excluded by an express term in a policy.¹⁰⁴⁵ Thirdly, the insurer who has paid to the insured under the insurance policy has an equitable lien or charge over the sum recovered from the third party liable for the loss if the third party may become insolvent.¹⁰⁴⁶ Fourthly, the insurer can rely upon equity to compel the insured to use the insured’s name in proceedings against the third party wrongdoer.¹⁰⁴⁷

Although it has prevailed that subrogation in insurance is an equitable doctrine, its application can be modified, excluded or extended by contract.¹⁰⁴⁸ This issue was critically

¹⁰⁴³ *Napier v Hunter* (1993) A.C. 713, p738

¹⁰⁴⁴ In *Morris v Ford Motor Co Ltd* (1973) QB 792, Lord Denning refuses the cleaners’ claim against Ford’s employee, on the reasoning that subrogation is an equitable remedy. However, in *England v Guardian Insurance Ltd* (1999) 2 All.E.R. 481, it was held that the insurer’s rights to subrogation and to equitable lien are unaffected despite his unconscionable conducts. Two reasons for this are: (a) the equitable lien was a proprietary interest which could not be undermined by the insurer’s conduct toward the insured in handling the insured’s claim such as: initially denying liability or refusing to participate in attempted settlement negotiation with the insured; and (b) in any event, if the insurer had prejudiced the interests of the insured, he had a right of action against the insurer for damages.

¹⁰⁴⁵ *Banque Financière de la Cité v Parc (Battersea) Ltd and others* (1998) 1 All.E.R 737; Goff and Jones, *The Law of Restitution*, (5th ed., Sweet & Maxwell, 1998), pp 589-608; SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), pp 114-151; R Hodgkin, “Subrogation in insurance law”, (1975) J.B.L 114; J Birds, “Contractual Subrogation in Insurance”, [1979] J.B.L. 124, p131

¹⁰⁴⁶ The existence of the equitable lien means that the insurer would have priority in an insolvent administration of the insured. He is able to take priority over the claims of other creditors. (See *Re Miller, Gibb & Co Ltd*. [1957] 1 W.L.R. 703) This view was approved by the House of Lords in *Napier v Hunter* (1993) A.C. 713, at p752 per Lord Browne-Wilkinson. Some authorities had described the rights of the insurer as arising under a trust. (SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), pp 25-26; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p699; see also *Randal v Cochran* (1748) 1 Ves.Sen. 98) However, Birds suggests that the imposition of a trust would impose too great a burden on the person actually holding the money (J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p 323)

¹⁰⁴⁷ *Commercial Union Assurance Co v Lister* (1874) L.R. 9 Ch.App. 483; *Caledonia North Sea Ltd v British Telecommunications Plc* (2002) All ER (D) 85; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p491; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p331

¹⁰⁴⁸ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p324

examined by the House of Lords in the case of *Banque Financière de la Cité v Parc (Battersea) Ltd and others*.¹⁰⁴⁹

3. FULL COMPENSATION OR FULL INDEMNITY?

It is generally acknowledged in insurance laws that the insured cannot make profit on his insurance contract at the expense of either the insurer or the third party wrongdoer.¹⁰⁵⁰ The rule is clearly illustrated by the leading case of *Castellain v. Preston*¹⁰⁵¹. The case was concerned with property insurance. A house was insured against fire by its owner. After he had contracted to sell it but before completion of the sale, it was damaged by fire. The seller not only recovered money from the insurer but also received the full amount of the purchase money from the buyer, despite the damage to the house. It was held that the insurer was entitled to recover from the insured seller a sum equal to the insurance money. Brett LJ, in this case, stated that the insured “shall be fully indemnified, but shall never be more than fully indemnified.”¹⁰⁵²

This classical statement arises out of an important concept of “full indemnity”. This concept has caused a controversial understanding of its meaning. It can be interpreted in two different ways. First, the insurer is entitled to exercise his subrogation right to recoup when he fully performs his obligations under the insurance policy, irrespective of the fact that the insured is not fully compensated for his total loss. Second, the insurer’s rights to recover only arise when the insured is fully compensated for his total loss. The English approach and the Vietnamese approach to the issue will be critically analysed to clarify the weaknesses in Vietnamese insurance laws. A fairer approach will be recommended to overcome the weaknesses in Vietnamese insurance laws.

¹⁰⁴⁹ (1998) 1 All.E.R 737, at 744, Lord Hoffmann said that: “although in *Lord Napier and Ettrick v Hunter*, *Lord Napier and Ettrick v R F Kershaw Ltd* [1993] 1 All ER 385, [1993] AC 713 your Lordships rejected the exclusivity of this claim for the common law and assigned a larger role to equitable principles, there was no dispute that the doctrine of subrogation in insurance rests upon the common intention of the parties and gives effect to the principle of indemnity embodied in the contract.”

¹⁰⁵⁰ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p325-326

¹⁰⁵¹ (1883) 11 QBD 380,

¹⁰⁵² *Castellain v. Preston* (1883) 11 QBD 380, p386

3.1. English approach

In English insurance law, it is not quite clear whether “full indemnity” means that the insured are merely fully indemnified within the terms of the policy¹⁰⁵³ or that the insured must be fully compensated for his total loss.¹⁰⁵⁴ The answer to the question¹⁰⁵⁵ has been the subject of a number of cases, articles and textbooks. There are several authorities supporting the argument that the insurer is only required to meet in full his obligations in the insurance contract.¹⁰⁵⁶

3.1.1. Marine insurance

In marine insurance, the insurer is entitled to subrogate where he has paid the whole amount due on the policy.¹⁰⁵⁷ The insurer’s rights to subrogate come into effect regardless of whether the insured has been fully compensated or not, the insured himself must bear the uninsured loss.¹⁰⁵⁸

In the case of a valued policy, the agreed value of the subject matter insured is conclusive as between the insured and the insurer as to the value of that property.¹⁰⁵⁹ Thus, the insured cannot dispute that the amount paid to him in accordance with the valuation has indemnified him fully for his loss, even if the actual value of the subject-matter exceeds its agreed value or the insured’s actual loss is greater than the indemnity paid by the insurer. This principle is illustrated by the case of *North of England Insurance Association v Armstrong*¹⁰⁶⁰. In this case, a valued policy of insurance for £6,000 on one of defendants’ vessels was underwritten by plaintiffs, the real value of the vessel being £9,000, and no other insurance had been effected on it. The vessel had been run down and sunk by another vessel. The insurers paid to

¹⁰⁵³ In other words, the insurer is only required to meet in full his obligations under the insurance contract

¹⁰⁵⁴ In *Page v Scottish Insurance Corp.* (1929) 33 Ll.L.Rep 134, p138, Scrutton LJ left open the question whether the insurer ‘is not subrogated though he has paid the whole amount due on his policy if the insured has a further loss.’; see also A Brown, “An insurer’s rights in litigation or contractual subrogation: an oxymoron?”, (1996) 8 Ins.L.J. 60, p60; A Green, “Strengthening the insurer’s subrogation rights”, (1995) 3(10) Int.I.L.R 348; p349;

¹⁰⁵⁵ This question cannot arise if the subject matter is fully insured. The insured shall be fully compensated for his actual total loss. The problem will arise in the three situations: under insurance, loss under an excess or deductible clause and valued policy.

¹⁰⁵⁶ *Napier v Hunter* (1993) A.C. 713; *England v Guardian Insurance Ltd* (1999) 2 All.E.R. 481

¹⁰⁵⁷ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1029

¹⁰⁵⁸ The insured cannot apply any recovery from a third party first to his own uninsured loss.

¹⁰⁵⁹ S 68(1) & s27(3) of MIA 1906

¹⁰⁶⁰ (1870) LR 5 QB 244; In the case of *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330, at p 336, Lord Diplock confirmed *The Armstrong* by stating: ‘In that case it was held that the insurers were entitled to the whole of the sum recovered from the third party wrongdoer, although the agreed value was only two-thirds of the actual value. It is submitted that s79 of MIA is based on that decision and gives statutory effect to the law as there stated.

defendants the £6,000, and afterwards recovered by proceedings instituted in the insured's name against the owners of the ship which caused the damage the sum of £5,683. It was held that the underwriters were entitled to the whole of the amount recovered from the third party, and the insured was not entitled to any part of it on the ground that the vessel insured was of greater value than that named in the policy.¹⁰⁶¹

Similarly, in the event of a partial loss, the agreed valuation is conclusive evidence of the insurable value of the subject-matter insured. It was held in *Goole & Hull Steam Towing Co Ltd v Ocean Marine Ins Co Ltd*¹⁰⁶² that the insurer was only liable for the difference between the amount valued in the policy and the amount recovered by the insured from the third party. Consequently, the insurer was entitled to claim the whole amount recovered from the third party wrongdoer and the insured was under-compensated where the agreed value was lower than the current market value. Although the insured's actual loss was greater than the policy valuation, he was not compensated for that loss.

Under statutory law, section 81 of MIA 1906, dealing with the case of under insurance, provides that the insured 'is deemed to be his own insurer in respect of any uninsured balance'. The insurer is only liable to part of the insured's loss which the sum insured bears to the actual value of the subject matter insured. Average principle is implied into marine policies by virtue of section 81 of MIA 1906. Therefore, allocation of the subrogation recovery between the insured and the insurer is based on pro rata apportionment in accordance with their respective liabilities.¹⁰⁶³ Consequently, the insured is not fully compensated for his entire loss. This rule was clearly illustrated in *The Commonwealth*¹⁰⁶⁴. The Welsh Girl was run down by the steamship The Commonwealth, and was totally lost. The Welsh Girl was valued at £1,350, but was only insured for £1,000. After the insurer had paid the owners of The Welsh Girl the £1,000 indemnity, the insurer pursued the third party wrongdoer (owners of The Commonwealth) by way of subrogation, recovered £1,000, and contended that the insurer was entitled to the whole sum. The Court of Appeal held that, as the value of Welsh Girl was £1,350 and the insurer was only liable for £1,000, the owners of The Welsh Girl were self-insured for the remaining £350. Thus, the apportionment of the sum

¹⁰⁶¹ The reason for this judgment is that the valued policy is conclusive evidence of insurable value of the subject matter insured.

¹⁰⁶² (1928) 1 KB 589

¹⁰⁶³ According to the principle of average, the subrogation recovery from a third party is divided between the insurer and the insured in proportion to their respective interests.

¹⁰⁶⁴ (1907) P 216 CA

recovered from the third party between the insurer and the insureds was 1000:350 respectively.

3.1.2. Non-marine insurance

Unlike marine insurance, in the case of non-marine insurance, the insured might be fully compensated for his total loss¹⁰⁶⁵ because there is no presumption that the insured is to be his own insurer for the amount which is uninsured.¹⁰⁶⁶ The insured only bears the uninsured loss under the under-insured policy if there is an average clause in the policy.¹⁰⁶⁷ However, average clause is generally incorporated into commercial policies, which brings the marine insurance principle into play.¹⁰⁶⁸

The House of Lords in the case of *Napier v Hunter*¹⁰⁶⁹ supported the view that the insurer is entitled to claim to the subrogation recoveries once the insured is fully indemnified under the insurance policy. The effect of an excess clause on subrogation recovery was critically analysed in this case.

Lord Templeman gave a hypothetical example and divided the insured's losses into three successive layers of loss: the top layer is the loss in excess of the policy limit, the bottom layer is the loss under the excess clause, and the middle layer is the loss falling between the policy limit and the excess clause. The "recover down" principle applied. It was held that the insured should bear the loss under the excess clause and was under-compensated. The reason, in Lord Templeman's view,¹⁰⁷⁰ was that the insured had agreed to bear the loss in excess of the policy limit (top layer) and the loss falling below the excess clause (bottom layer), he should occupy the same position as would have been occupied by insurers of the top and bottom layers if a separate policy had been issued for each of the three layers.

Lord Jauncey agreed with Lord Templeman's reasons and stated that: "... in the context of recoveries subrogation is concerned only with the loss against which the assured is insured rather than any general loss. If an assured has suffered an insured loss and an uninsured loss

¹⁰⁶⁵ *Kuwait Airways Corp v Kuwait Insurance SAK (No1)* (1996) Lloyd's Rep 664

¹⁰⁶⁶ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p721

¹⁰⁶⁷ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p721

¹⁰⁶⁸ *Ibid*; see also: J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p311

¹⁰⁶⁹ (1993) A.C. 713

¹⁰⁷⁰ *Napier v Hunter* (1993) A.C. 713, p730

full indemnification of the former subrogates the insurers irrespective of the fact that the assured has not yet recovered the uninsured loss.”¹⁰⁷¹

Following *Napier v Hunter*, it seems that the notion that an insurer can exercise his subrogation rights when he has fulfilled his contractual obligations even though the insured has not been fully compensated for his entire loss represents current English law. This approach has been followed in later cases.¹⁰⁷²

3.2. Vietnamese approach

As in English insurance law, the principle of subrogation is recognised under Vietnamese insurance laws.¹⁰⁷³ The insured cannot be unjustly enriched at the expense of either the insurer or the third party. First, the insured is not allowed to receive double payment: the indemnity payment from the insurer and the compensation for damage from the third party wrongdoer. Where the insured has been paid for losses by a third party, the insurer is only liable for the difference between the amount payable under the insurance policy and the payment from the third party. Second, after making payment to the insured under the insurance policy, the insurer is entitled to exercise his subrogation rights to recoup from the third party responsible for the loss.

3.2.1. When do insurers’ rights of subrogation arise?

Under Vietnamese insurance law, insurers’ rights of subrogation arise when they fulfil their obligations under the insurance contract, regardless of whether the insureds are fully compensated for their total loss.

Regarding the first limb of the principle of subrogation, it is not clearly stipulated, but it is implied in Vietnamese insurance laws. Article 557(2) of Vietnam’s Civil Code 2005 provides that where the insured, before making a claim against the insurer, has received compensation for damage from the third party which is less than the amount payable by the insurer, the insurer is only required to pay the difference between the insurance benefits and the amount

¹⁰⁷¹ *Napier v Hunter* (1993) A.C. 713, p747

¹⁰⁷² *England v Guardian Insurance Ltd* (1999) 2 All.E.R. 481; *Kuwait Airways Corp v Kuwait Insurance SAK (No1)* (1996) Lloyd’s Rep 664

¹⁰⁷³ Article 577 of Vietnam’s Civil Code 2005, article 49 of Vietnam’s Law on Insurance Business 2000, and article 247 and 248 of Vietnam’s Maritime Code 2005

paid by the third party.¹⁰⁷⁴ The insured cannot make a profit from an insured event under Vietnam's insurance laws because the insurer has a right to deduct the sum that the insured recovered from the third party from his payment to the insured.¹⁰⁷⁵

In addition, it is implied in Vietnamese insurance laws that the insurer is not required to pay the insured anything if the amount the insured recovered from the third party is greater than the amount payable under the insurance policy, even though the payment from the third party is not fully compensated for the insured's total loss. The insured's shortfall may be caused by the ceiling liability of the third party or the third party's insufficient financial resource or the insured's contributory negligence. It is unfair to the insured as the insurer is not liable for any unrecoverable loss from the third party. In fact, the insured is deprived of his insurance benefits. Meanwhile, the insurer can still retain the premium but has no legal liability to make payment on the occurrence of the event insured against where the insurance is under-insurance.

Concerning the second limb of the subrogation principle, the insurer is allowed to sue the third party responsible for the insured's loss once the insurer has fully indemnified the insured in accordance with the insurance policy under Vietnamese insurance laws.¹⁰⁷⁶ After

¹⁰⁷⁴ Article 577(2) of Vietnam's Civil Code 2005 stipulates: "Where an insured has received monetary compensation for damage from a third party which is less than the amount payable by the insurer, the insurer is only required to pay the difference between the [total] insurance benefits [otherwise payable] and the amount paid by the third party, unless otherwise agreed. If the insured has received insurance benefits but the insurance benefits are less than the damage caused by the third party, the insured has the right to demand the third party indemnify [the insured] for the difference between the insurance benefits and the monetary compensation for the damage."

In marine insurance, article 248(3) of Vietnam's Maritime Code 2005 states: "if the assured has received the indemnity for losses from the third party, the insurer shall be obliged to pay only the difference between the indemnity amount according to the contract of insurance and the amount of money the assured received from the third party."

Article 49(2) of Vietnam's Law on Insurance Business 2000 provides: "If the insured refuses to pass such right to the insurer or does not reserve or abandons the right to make a claim against the third party, then the insurer shall have the right to deduct an amount of indemnity depending on the level of fault of the insured."

¹⁰⁷⁵ Article 577(2) of Vietnam's Civil Code 2005; article 248(3) of Vietnam's Maritime Code 2005; article 49(2) of Vietnam's Law on Insurance Business 2000

¹⁰⁷⁶ Article 577(1) of Vietnam's Civil Code 2005: "*Transfers of claims for indemnity*: (1) Where a third party is at fault for causing damage to the insured, and the insurer has paid insurance benefits to the insured, the insurer has the right to demand the third party indemnify the insurer for the insurance benefits already paid. The insured must provide the insurer with all necessary information, documentation and evidence of which the insured has knowledge in order to enable the insurer to exercise its right to demand the third party [to indemnify]."

Article 247 of Maritime Code 2005: "*Transfer of the right to recourse*: After having indemnified the insured, the insurer shall have the right to recourse against the person who is responsible for such loss (hereinafter referred to as the third party) within the amount paid. The insurer shall exercise this right in accordance with the provisions applicable to the insured."

Article 49(1) of Vietnam's Law on Insurance Business 2000: "*Right of subrogation*: Where the wrongful act or omission of a third party causes damage to an insured and the insurer has already indemnified the insured, the insured must pass to the insurer the right to claim recovery of such sum of indemnity from the third party."

being indemnified by the insurer, the insured must transfer to the insurer the right to bring a claim against the third party wrongdoer for his own benefit.¹⁰⁷⁷ Thus, the insurer is allowed to exercise his subrogation rights regardless of whether the insured has been fully compensated or not. The insured himself must bear the uninsured loss.

However, under Vietnamese insurance laws, the insurer is entitled to make a claim against the third party wrongdoer in his own name, unlike under English law.¹⁰⁷⁸ It is not required by Vietnamese laws that the insurer must step into the insured's shoes and use the insured's name to make a claim against the third party wrongdoer.¹⁰⁷⁹ Where the insured is fully insured and has been indemnified by the insurer, the insured is not permitted to bring a claim against the third party wrongdoer because he must transfer to the insurer the right of suit against the third party wrongdoer.¹⁰⁸⁰ In this case, only the insurer has the right to take action against the third party. The insured is under a duty to assist the insurer in the proceedings against the third party.

In the case of under-insurance, where the amount paid to the insured under the insurance policy is less than the insured's total loss, the insured has a right to bring a claim against the third party for the uninsured loss, and at the same time the insurer has a right to sue the third party wrongdoer for his own benefit within his payment under the policy.¹⁰⁸¹

A simple example can illustrate the application of subrogation principle under Vietnamese insurance laws. A motorcycle insured for £150, but worth £200, was written off due to negligence of a third party. After paying £150 to the insured, the insurer subsequently recovered £100 from the third party wrongdoer through subrogation. The insured brought another claim against the third party but obtained nothing because of the third party's

¹⁰⁷⁷ Article 577(1) of Vietnam's Civil Code 2005; article 247 of Vietnam's Maritime Code 2005; Article 49 (1) of Vietnam's Law on Insurance Business 2000

¹⁰⁷⁸ In English insurance laws, the insurer must step into the shoes of the insured to make a claim against the third party wrongdoer; *Mason v Sainsbury* (1782) 3 Doug. K.B. 61; see also *Lister v Romford Ice and Cold Storage Co Ltd* (1957) 1 All.E.R. 125

¹⁰⁷⁹ In contrast, section 79 of MIA 1906 states that the insurer is "...**subrogated to** all the rights and remedies of the assured in and in respect of that subject-matter..." There is confusion between the doctrine of subrogation and the doctrine of assignment under Vietnamese law. For critical analysis of this problem, see section 5 of this Chapter.

¹⁰⁸⁰ Article 577(1) of Vietnam's Civil Code 2005, article 49(1) Vietnam's Laws on Insurance Business 2000, and article 247 of Vietnam's Maritime Code 2005

¹⁰⁸¹ Article 577(2) of Vietnam's Civil Code 2005 stipulates: "...If the insured has received insurance benefits but the insurance benefits are less than the damage caused by the third party, the insured has the right to demand the third party indemnify [the insured] for the difference between the insurance benefits and the monetary compensation for the damage.

An insurer has the right to demand the third party indemnify fully [the insurer] for the amount it has paid to the insured"

financial problem. The insured had to bear £50 of the uninsured loss. The insured could not argue that he could share with the insurer the subrogation recovery from the third party as he was not fully compensated for his loss.

In another way, where the insured has been paid by the third party wrongdoer before making a claim against his insurer, it comes to the same result. The insured recovered £100 from third party, and then made a claim against his insurer. The insurer is under an obligation to pay only £50, the difference between the insurance benefit and the amount recovered from the third party wrongdoer.

3.2.2. An excess clause in an insurance policy:

In case of an excess clause, the insured must bear the loss falling below an excess under Vietnamese insurance laws. In fact, there is no expressed provision concerning excess clause in Vietnamese insurance laws. In this circumstance, laws of contract apply to deal with any problem arising out of an excess clause under an insurance policy.¹⁰⁸² The reason is that insurance contracts are a type of contract which is governed by laws of contract.¹⁰⁸³ Moreover, the freedom of contract of the parties is recognised by Vietnamese laws of contract.¹⁰⁸⁴

The excess clause is a part of the parties' agreement which is binding on both the parties, and the insurers commonly incorporate an excess clause in their insurance contracts. A standardized term of an excess clause provides that the loss under the excess clause is borne by the insured in every circumstance.¹⁰⁸⁵ Therefore, where the insured is insured for his full loss, subject to an excess clause, the insurer has a right to make a claim against the third party wrongdoer from the moment when the amount equal to the difference between the insured's loss and the loss under the excess clause is paid by the insurer. Consequently, the insured is not fully compensated for his total loss.

¹⁰⁸² For more details about rules on applying legal documents under Vietnam's legal system, see section 3.1.1 of Chapter 2

¹⁰⁸³ See section 3.1.1 of Chapter 2

¹⁰⁸⁴ Article 4 of Vietnam's Civil Code 2005: "*Principle of free and voluntary undertaking and agreement*: The law guarantees the freedom to undertake and agree on the establishment of civil rights and obligations if such undertakings and agreements do not breach matters prohibited by law and are not contrary to social ethics. In civil relations, parties shall be entirely voluntary and no party may force upon, prohibit, coerce, intimidate or hinder any other party. All lawful undertakings and agreements shall bind the parties and must be respected by individuals, legal entities and other subjects."

¹⁰⁸⁵ PVI property insurance policy

3.2.3. *Under-insurance*

In case of under-insurance, the insured is deemed to be his own insurer for the uninsured balance under Vietnamese insurance laws. Article 43 of Law on Insurance Business 2000 and article 233 of Maritime Code 2005 provide that where the insured sum as specified in the contract is lower than the insurable value, the insurer is only liable for losses in such proportion as the insured amount bears to the insurable value. Once the insurer fully performs his obligation under the insurance policy, he is entitled to exercise his subrogation right to recoup up to the extent of his payment. This is different from the English approach, based on pro rata apportionment, whereby any subrogation recovery shall be divided between the insurer and the insured in proportion to their respective interests.¹⁰⁸⁶ Under Vietnamese insurance laws, the insured cannot share with the insurer any amount the insurer recovered from the third party wrongdoer. The insured must bring an action in his own name against the third party for his uninsured balance. If the insured cannot recover anything from the proceedings against the third party, the insured himself must bear the uninsured loss.

3.2.4. *Judicial practices*

The case of *Bao Viet Insurance Co v Tran Son Co Ltd*¹⁰⁸⁷ illustrates how the Vietnamese courts apply the principle of subrogation. The insured (Amoro Co Ltd) took out a policy with the insurer (Bao Viet) to insure for its store. Due to negligence of the employees of the defendant, there was electrical leakage which resulted in damage of the insured's store by serious fire. The insurer paid to the insured for VND 1 billion of the sum insured, while the value of subject matter insured was about VND 6 billion. A subrogation and receipt form was signed by the insured. The insurer brought an action against the defendant in his own name for the sum paid to the insured. The Vietnamese people's court held that the defendant had to compensate the sum for the insurer.¹⁰⁸⁸

The court did not take into account the total loss or uninsured loss of the insured resulting from the third party's negligence, simply because this is a dispute between the insurer and the third party wrongdoer. The dispute between the insured and the third party wrongdoer over the uninsured loss could be settled in other litigation. Under Vietnamese insurance laws, the

¹⁰⁸⁶ *The Commonwealth* (1907) P 216 CA

¹⁰⁸⁷ Hanoi People's Court 2006

¹⁰⁸⁸ The insurer is entitled to bring an action against the third party wrongdoer in his own name. The insured can take an action for his uninsured loss in other litigation.

insurer and the insured have separate rights to take action against the third party for their own respective benefit if the insured's loss contains insured loss and uninsured loss.¹⁰⁸⁹

In commercial practice, signing a subrogation and receipt form is a condition for the insureds to receive insurance proceeds. The insurer is entitled to subrogate to the insured's rights immediately after the subrogation and receipt form is signed by the insured. This form is evidence that the insured has transferred his right to sue the third party wrongdoer to the insurer in respect of the insured's insured loss. It transfers to the insurer not only rights in action against the third party wrongdoer¹⁰⁹⁰ but also all the rights the insured may have against the third party.¹⁰⁹¹ The insurer is allowed to exercise his subrogated rights regardless of whether the insured is fully compensated for his total loss or not. Under Vietnam's insurance laws, the one fundamental prerequisite for exercise of subrogation right is that the insurer has met in full his obligations under the policy.

There is another way of proceeding against the third party wrongdoer: the insurer and insured could jointly bring an action against the third party wrongdoer. Under Vietnamese laws, the insurer is entitled to sue the third party wrongdoer for the insured's total loss if there is written consent by the insured. The insurer and the insured are free to contract for their rights and obligations relating to the proceedings against the third party wrongdoer.

However, in practice, the insurer rarely agrees to sue the third party for the insured's total loss. The insurer is only interested in his rights to recoup the payment paid to the insured. These rights have been transferred to him since the insured had signed the subrogation and receipt form. If he agrees to sue the third party wrongdoer for the insured's total loss, he may bear the greater cost of the proceedings and must clarify by a written agreement with the insured on allocation of the subrogation recovery. The insurer is anxious to avoid these problems. Therefore, where the insurer agrees to join with the insured in the proceedings against the third party wrongdoer, the insured has to consent to some terms and conditions in the litigation agreement, which may not be in his favour.

¹⁰⁸⁹ Article 577(2) Vietnam's Civil Code 2005; for critical analysis of this problem, see below in this Chapter.

¹⁰⁹⁰ It is in contrast to English law, the right in action belongs to the insured.

¹⁰⁹¹ The standard term in the subrogation and receipt form: "In consideration of having received this payment, we hereby agree to assign, transfer and subrogate to you, to the extent of your interest, all our rights and remedies in respect of the subject matter insured, and to grant you full power and give you any assistance you may reasonably require of us in the exercise of such rights and remedies in our or your name and at your own expenses."

3.2.5. *Opinions of Vietnamese academics*

Vietnamese academic writers have contended that the current regulation on subrogation is fair to both parties, for two reasons.¹⁰⁹² First, when the insured is fully indemnified in accordance with the policy, he must pass to the insurer his rights to make a claim against the third party wrongdoer, even though he is not fully compensated for his total loss. When the insurer fully performs his obligations under the contract, he should be entitled to exercise his subrogation rights. The insurer who has met in full his obligations under the policy should be protected by the law in respect of his payment to the insured.¹⁰⁹³ Under Vietnam's law of contract, where a party fulfils his obligations under a contract, he is entitled to get all benefit in accordance with the contract which should be performed by the other party.¹⁰⁹⁴ If the insured wishes to be fully compensated for his loss, he must take out a policy under which the subject matter is fully insured.

Second, the insured can still recover his uninsured loss if he brings an action against the third party wrongdoer. The insured and the insurer have separate rights to bring a claim against the third party wrongdoer for their respective losses. The insurer has the right to recoup within his payment, and the insured has the right to recover for his uninsured balance.

However, it seems that those Vietnamese academics and the drafters of Vietnam's insurance laws never properly addressed themselves to the problems of an insufficient recovery from the third party wrongdoer, and to the problems of competition between the insured and the

¹⁰⁹² Nguyen Thi Thuy, "Chuyen giao quyên doi boi thuong trong bao hiem tai san" (2008) *Tap chi Khoa hoc phap ly* 5 [Trans: Nguyen Thi Thuy, "Transfer of right to make a claim in property insurance", (2008) *Journal of Legal Science* 5], p9; Hiep hoi bao hiem Viet Nam, *Cam nang bao hiem phi nhan tho*, (NXB Tai chinh, 2007) [Trans: Association of Vietnamese Insurance, *Guideline on non-life insurance*, (Finance Publishing House, 2007), p154; Nguyen Van Dinh, *Giao trinh Bao hiem*, (NXB Dai hoc Kinh te quoc dan, 2006) [Trans: Nguyen Van Dinh, *Textbook on Insurance*, (Publisher of National Economics University, 2006)], p326; Phan Thi Cuc, *Giao trinh Bao hiem*, (NXB Thong ke, 2008) [Trans: Pham Thi Cuc, *Textbook on Insurance*, (Statistical Publishing House, 2008)], p215

¹⁰⁹³ A example of this protection is that where there is a third party responsible for the loss, the insurer has the right to refuse to indemnify the insured if the insured fails to provide all necessary documentation, information which enables the insurer to take an action against the third party wrongdoer; see also Article 248(1) & (2) of Vietnam's Marine Code 2005: "(1) The assured shall be obliged to provide the insurer with all information, documentation as well as proof and to take necessary measures to enable the insurer to exercise the right to recourse against the third party. (2) Where the assured fails to perform the obligations specified in Clause 1 of this Article or he/she is at fault that makes the insurer's right to recourse unexercisable, the insurer shall be exempt from the payment of the whole indemnity or enjoy a reasonable reduction of the payable indemnity..."

¹⁰⁹⁴ Pham Duy Nghia, *Chuyen khao luat kinh te*, (NXB Dai hoc Quoc gia, 2004) [Trans: Pham Duy Nghia, *Vietnamese Business Laws: Textbook for Postgraduate Program*, (Publisher of National University, 2004)], p301

insurer in their claims to subrogation recovery.¹⁰⁹⁵ The insured who has given valuable consideration under the insurance contract should be first protected by law. It should be emphasized that the insured should not benefit from his loss but should be fully compensated for his total loss. If the insured is not completely compensated for his loss, the insurer should not be allowed to avoid, at the expense of the insured, the risk of loss for which he has been paid.

Moreover, the heavy burden of responsibility on the third party wrongdoer should also be taken into account. He must get involved in two litigations with the same cause of action. It costs considerable time and money. It may create conflicting judgments due to different opinions and grounds being given by two different tribunals.

The question as to when the insurer may exercise his rights to recoup from a third party (when he has fully performed his obligations under the insurance policy or when the insured is fully compensated for his total loss) has long been discussed in English insurance laws. However, this question is not dealt with in Vietnamese insurance laws. It is suggested that the full compensation approach should be applied in Vietnamese insurance laws. This suggestion could be supported by the following reasons.

3.3. The insured should be fully compensated for his total loss before the insurer is entitled to exercise his rights to recoup from a third party

A number of strong arguments¹⁰⁹⁶ support the view that the insured must be fully compensated for his total loss. It is submitted that this approach is fair and consistent with the principle of indemnity. The insured must not receive more than a full compensation, but he also must not receive less from both the insurer and the third party.

MacGillivray points out that the general rule that an insured, who is paid out on his policy and then proceeds to recover from a third party, is entitled to retain the recovery until he is

¹⁰⁹⁵ J Fleming, "Insurance- Subrogation- Priority between insurer and insured", (1974) 52 Can.Bar.Rev. 103, p106

¹⁰⁹⁶ J Birds, "Insurance: subrogation in the House of Lords", (1993) J.B.L 294; M Hemsworth, "Subrogation: the problem of competing claims to recovery monies", (1998) J.B.L 111; A Tar, "Subrogation and the Ash Wednesday bushfire disaster", (1987-1988) 11 Adel. L. Rev. 232; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1029-1030; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p721; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p326; Goff and Jones, *The Law of Restitution*, 3rd ed., p540-542, G Veal, "Subrogation: The duties and obligations of the insured and rights of the insurer revisited", (1992) 28 Tort & Ins.L.J 69, p74; W Gummow, "Names and equitable lien", (1993) L.Q.R 159, p161

fully compensated for his total loss and needs only hand over any excess to the insurer is no doubt correct.¹⁰⁹⁷ A simple example has been given to illustrate this general rule. An insured who suffers a loss of £5,000 has taken out an insurance policy with cover up to £3,000. He subsequently recovers £3,500 from a third party wrongdoer. The insured can claim £3,000 under the policy, retain £2,000 out of his recovery, and hand over only £1,500 to the insurer.¹⁰⁹⁸

Birds also supports the general rule that an insured has to be fully compensated for his loss before the insurer obtains rights of subrogation, and he has doubts concerning the result of the decision in *Napier v Hunter*. In his opinion, the logic of the reasoning in this case is difficult to fault, but it seems hard to assume that the insured agrees to bear the loss under an excess clause and to stand behind the insurer when the subrogation recovery is distributed.¹⁰⁹⁹ Although some insureds do not in reality agree in many classes of insurance, they have no choice as to whether or not there is an excess in their insurance policies.¹¹⁰⁰ Furthermore, he criticises the decision in *Napier v Hunter* for worsening the position of the insured: the doctrine of subrogation which was developed in order to prevent an insured from being overcompensated is now operating in effect to deprive him of an indemnity against his loss.¹¹⁰¹

Clarke criticises the approach taken by the House of Lords in *Napier v Hunter* in respect of assumption of risk.¹¹⁰² The judgment of *Napier* seems rather hard on the insured. The excess clause does not merely render a portion of his loss irrecoverable from his insurer, but also disables him from recovering from the third party wrongdoer in respect of the loss falling below the excess clause until after the insurer has recouped himself.

The real intention of the insured and the insurer to the risk under an excess clause should be considered. It is hard to say that this risk is assumed by the insured, because the excess clause is stipulated not by the insured but by the insurer, in order to reduce transaction costs and to encourage the insured to be risk averse.¹¹⁰³ Although the insured does agree to bear that layer of risk when making a claim against the insurer for the insured loss, it is arguable that he

¹⁰⁹⁷ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p721

¹⁰⁹⁸ *Ibid*

¹⁰⁹⁹ J Birds, "Insurance: subrogation in the House of Lords", (1993) J.B.L 294, p298

¹¹⁰⁰ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p328-329

¹¹⁰¹ J Birds, "Insurance: subrogation in the House of Lords", (1993) J.B.L 294, p298

¹¹⁰² M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), 1029

¹¹⁰³ *Ibid*

actually intends the subrogation sum recovered from the wrongdoer to go to the insurer first, leaving himself under-compensated.

It is submitted that an excess clause merely presents the agreement between the insured and the insurer on a portion of the insured's loss irrecoverable from the insurer. Where there is a responsible third party involved, it does not presume that the insured totally agrees to be deprived of his right to recover from third party in respect of the excess. If the insurer has a prior right to recoup the amount under the excess clause from the subrogation recoveries, resulting in the insured being under-compensated, it is not clear why the insured should stand in a worse position than the insurer. This seems to penalise the under-compensated insured. Not only he may not recover under the policy but also he must stand behind the insurer when the recovery sum is distributed: the first result was part of the contract, but there is no clear reason for the second.¹¹⁰⁴

3.3.1. Pursuing the aims of the principle of indemnity

The notion that full compensation for the insured's actual loss is a prerequisite for an enforceable right of subrogation is justifiable for five reasons, as follows. First, the principle of subrogation has its root at the principle of indemnity. The principle of indemnity states that the insured should be fully compensated for his actual loss, while the principle of subrogation ensures that the insured does not receive double payment.¹¹⁰⁵ It should be emphasised that the primary purpose of subrogation is to ensure that the insured is not over compensated for his actual losses. This should be the main core for all the other rules derived from the doctrine of subrogation, and the rules which prevent the insured from full compensation for his entire loss would then be wrong. Brett L.J in his classic judgment in *Castellain v. Preston* said that: "if ever a proposition is brought forward which ... will prevent the assured from obtaining a full indemnity ... that proposition must certainly be wrong."¹¹⁰⁶ It would be more logical to assume that where the insured is not fully compensated for his entire loss by a combination of the payment from the insurer and the recovery sum from the third party, the insured is not over compensated or unjustly enriched.

Second, the insured must be fully compensated before the insurer may recover anything from the third party wrongdoer because the insurer assumed the risk of loss by accepting the

¹¹⁰⁴ M Hemsworth, "Subrogation: the problem of competing claims to recovery monies", (1998) J.B.L 111, p114

¹¹⁰⁵ A Tar, "Subrogation and the Ash Wednesday bushfire disaster", (1987-1988) 11 Adel. L. Rev. 232, p233

¹¹⁰⁶ *Castellain v. Preston* (1883) 11 QBD 380, p386

insured's premiums.¹¹⁰⁷ It is submitted that this rationale should be a foundation for the insured's full compensation.

The insurer is under a contractual obligation to indemnify the insured on the occurrence of the insured event. This obligation does not depend on the possibility of recoupment from a third party. After accepting the premium for the policy provided, the insurer is obliged to pay the insured's claims regardless of the fact that a proximate cause might be the insured's negligence or a third party's fault, provided that it is the risk which has been insured. In fact, if there is no third party involved or the third party is not responsible for the loss, the insurer still has to bear the loss up to the full amount of the insurance policy.

Moreover, an insurance contract contains a basic promise to pay in the event of the insured loss occurring, which should be subordinated to the insured's right to full compensation.¹¹⁰⁸

When the insured takes out an insurance policy, the main core of the bargain is that if there is a loss he should be fully compensated for the loss insured. The insurer has received valuable consideration in return for his agreement to accept the possibility of that risk of loss. There is no clear reason for giving the insurer rights to subrogation before the insured has not been fully compensated. Only if the insured has been fully compensated, the insurer is then entitled to exercise his subrogation right to recoup from third party's payment, in order to prevent the insured from obtaining unjust enrichment. Therefore, when the total amount of the recovery by the insured from the third party wrongdoer and proceeds of the policy is less than the insured's total loss, and the question of whether the insured or the insurer must to some extent go unpaid arises. It is suggested that the loss should be borne by the insurer. The reason for this argument is that the insured has paid the insurer to assume the risk of loss. It seems unfair if the burden of going uncompensated rests with the inadequately compensated insured.

Third, although it may be argued that the risk of uninsured loss is the risk that the insured has agreed to assume in exchange for the payment of lower insurance premiums,¹¹⁰⁹ this argument is debateable. The insurer only accepts the lower premiums for lower liability or policy limits. And, in order to determine the insurance premiums, the insurer does not take

¹¹⁰⁷ E Rinaldi, "Apportionment of recovery between insured and insurer in a subrogation case", (1993-1994) 29 *Tort & Ins. L. J.* 803, p808

¹¹⁰⁸ J Parker, "The made whole doctrine: Unraveling the enigma wrapped in the mystery of insurance subrogation", (2005) 70 *Mo.L.Rev* 723, p758

¹¹⁰⁹ E Rinaldi, "Apportionment of recovery between insured and insurer in a subrogation case", (1993-1994) 29 *Tort & Ins. L. J.* 803, p809

into account of the possibility of successful subrogation recovery from a third party.¹¹¹⁰ It means that subrogation has not led to lower premiums costs for the insured.

Even if the insured takes out a policy with lower premiums, resulting in a portion of his property being uninsured, there is no clear reason why this should lead to the assumption that the insured should be deprived of being fully compensated for his entire loss when a third party is responsible for the loss. The recovery money from the third party wrongdoer should go first to the uninsured loss of the insured.¹¹¹¹ If there is any surplus above the insured's actual total loss (where the sum combined of the recovery from the third party wrongdoer and payment by the insurer exceeds the insured's total loss), the surplus is recouped by the insurer.¹¹¹² Only the surplus, not the total amount of recovery money, reduces or diminishes the insured loss. When the insured is not fully compensated, the insured is not unjustly enriched through the aggregation of both the insurer's payment and compensation from the third party wrongdoer.

Fourth, where the insured has not been fully compensated, it is the insurer who is unjustly enriched and gains a windfall if allowed both subrogation rights to recover from a third party and retention of the premiums paid by the insured. The insurer is unjustly enriched at the expense of the insured.

Premium is a sufficient valuable consideration which is paid to the insurer for his promise of making payment in the event of loss. Where there is no third party involved, or the subrogation rights are not available to the insurer,¹¹¹³ premium is the only benefit the insurer can obtain. The mere fact that a third party is responsible for the loss may give the insurer the benefit of reducing the amount of payment he actually made under the policy, even if the insured is fully compensated before the insurer may recover anything from the third party wrongdoer. It is submitted that only the amount in excess of the insured's total loss should be recouped by the insurer. It seems unfair to the inadequately compensated insured if the insurer is allowed to recoup in a greater amount despite of the fact that the insured is not fully compensated.

¹¹¹⁰ for critical analyse on this issue, see R Hasson, "Subrogation in insurance law- a critical evaluation", (1985) 5 O.J.L.S 416

¹¹¹¹ It was held in *Law Fire Assurance Co v Oakley* (1888) 4 T.L.R. 309 that if the insured's loss includes damage which is not covered by the policy, the insurer is not entitled to be subrogated to any payment or liability in respect of the uninsured loss.

¹¹¹² *Castellain v. Preston* (1883) 11 QBD 380

¹¹¹³ Where the third party wrongdoer is insolvency or incapable of compensating the insured, the insurer must also bear the loss.

In marine insurance, the insured is deemed to be his own insurer in respect of the uninsured balance.¹¹¹⁴ The insurer may have a strong argument that payment under the policy, combined with the insured's own responsibilities as a self-insurer, constitutes a full compensation.¹¹¹⁵ However, this argument is debatable and the assumption should be changed. In non-marine policy, there is no such assumption; the insured has a right to claim up to the full amount of his total loss.¹¹¹⁶

In the case of a valued policy, where the coverage under a valued policy is taken out for an amount less than the valuation, payment of the sum insured prima facie will not constitute a full compensation for the insured's total loss. The insured should not be prevented from recovering the balance from other sources, such as from a third party, if the loss is caused by the third party. The insured should be entitled to retain the difference between the agreed value under the policy and the sum insured in order to make up the full compensation, because it is expressed in the agreement between the parties that the insured is underinsured.¹¹¹⁷

Any recovery from the third party wrongdoer is to be apportioned between the insurer and the insured in the proportion in which they share the risk only if there is an expressed average clause in the policy. Where there is no expressed average clause in the insurance policy, the principle of average should not apply.

In the case of an unvalued policy, when the maximum amount recoverable is less than the insured's actual loss, it would be open to the insured to argue that the amount paid to him has not fully compensated for his total loss. In this situation, the upper limit may not bear any relation to the true value of the insured property, and it may not be intended to provide a full compensation in the event of a total loss. Moreover, unlike valued policy, no estoppel from disputing the value of the thing insured as stated in the policy would arise under an unvalued policy.¹¹¹⁸ Therefore, the insured should be reimbursed first out of the recovery from the third party.

¹¹¹⁴ s81 of MIA 1906

¹¹¹⁵ *The Commonwealth* (1907) P 216 CA

¹¹¹⁶ Derham, *Subrogation in Insurance Law*, (Law Book Company, 1985), p52; an exception is that there is an average clause in the non marine insurance policy.

¹¹¹⁷ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p505; where there is an expressed average clause in the policy, the subrogation recovery should be allocated in proportion to the parties' respective interests.

¹¹¹⁸ Derham, *Subrogation in Insurance Law*, (Law Book Company, 1985), p51

Fifth, complication may arise in the situation where the insured has contributory negligence to the loss. Because of this, the third party wrongdoer is liable for less than the whole of the damage. A question arises as to how to allocate the subrogation recovery between the insured and the insurer. A simple example will illustrate available solutions to the issue. The insured has suffered a loss of £1,000 and his claim against the third party wrongdoer is worth £500 (due to the insured's contributory negligence) and he receives £600 from the insurer. Three solutions are available: (i) the insured must pass to the insurer in full, with a result that he is himself £400 out of pocket; (ii) the insured satisfies his own loss in full, passing only the remains to the insurer, so that the insured can keep £400, leaving only £100 for the insurer; (iii) the available compensation from the third party wrongdoer shall be divided between the insurer and the insured in accordance with their respective losses. It would entitle the insured to £200 and the insurer to £300.

In supporting the first solution, it can be strongly argued that a negligent insured is fully compensated in term of equity when he receives payment for that percentage of his damages for which he is not at fault. The insured should suffer reduction in the same proportion as his contributory negligence to the loss. He would be unjustly enriched if allowed to keep damages payment for his contributory negligence and the payment from his insurer as well.¹¹¹⁹ However, it submitted that the second solution is fairer as it conforms to the underlying rationale of subrogation. The primary purpose of subrogation is derived from the principle of indemnity that allows the insured to be fully compensated.¹¹²⁰ The principle of subrogation should not deprive the insured of full compensation for his total loss. Moreover, there is not much to be said for passing the loss to the insurer, who considers risks as his business, rather than to the insured who has paid the premium as valuable consideration in order to buy financial stability from the insurer.¹¹²¹ Therefore, if the wrongdoer cannot compensate the insured in full, the insured should be given priority to subrogation recovery. It is suggested that the third solution is applied where there is an expressed agreement between the parties.

¹¹¹⁹ *Sorge v National Car Rental System Inc* (1991) 470 N.W.2d 5, p7

¹¹²⁰ A Tar, "Subrogation and the Ash Wednesday bushfire disaster", (1987-1988) 11 Adel. L. Rev. 232, p233

¹¹²¹ JG Fleming, "The collateral source rule and loss allocation in tort", (1966) 54 Cal.L.Rev 1478, p1525-1526

3.3.2. Support from case law

3.3.2.1. English cases

The notion that the insured should be fully compensated before the insurer may recover anything from the third party wrongdoer finds support in English case law. The leading case is *Commercial Union Assurance Co v Lister*¹¹²². In this case, a mill of the insured was burnt down by an explosion of gas. The explosion was caused by the negligence of the servants of the third party. The mill was insured against fire for sums amounting to £33,000 but not for the full value. The insured's total loss (£56,000) exceeded the sum insured. The insured had successfully brought an action against the third party for the amount of his damage, and the insurers alleged that they were entitled to the benefit of any right of action vested in the insured. It was held that the insured was entitled to bring an action against the third party wrongdoer for the injury to himself and he had to do so for the whole loss, including that part of the loss against which he is indemnified by the insurance companies; thus, the insured was entitled to retain the amount in excess of the indemnity paid by the insurers.

In *Driscoll v. Driscoll*¹¹²³, the insured was a tenant of premises that were damaged by fire. The indemnity paid by the insurer was insufficient for reinstating the premises. The insured sued a sub-tenant for breach of the latter's repair obligations. The insurer claimed to be entitled to the proceeds of this claim in priority over full indemnification to the insured. The insurer's claim was rejected by the court. O'Connor M.R, the judge in this case, stated that: "I now come to the claim of the Insurance Company. That is based on the right of subrogation, and the contention of the Company is that whatever sum is recovered by the insured must go to recoup the Company the amount paid on foot of the policy, irrespective of the consideration of whether the insured has been fully indemnified against the loss sustained. This is met by the insured's contention that until he is fully indemnified he is not bound to contribute anything to the Company. I have no doubt that this latter view is correct. A contract of insurance against fire is only a contract of indemnity, and I think that the foundation of the doctrine of subrogation is to be found in the principle that no man should be paid twice over in compensation for the same loss. The corollary to this is that a contract of

¹¹²² (1874) L.R. 9 Ch.App. 483

¹¹²³ [1918] 1 Ir. R. 152.

indemnity against loss should not have the effect of preventing the insured from being paid once in full. I do not think that this can be disputed.”¹¹²⁴

It is clear from the above cases that until the insured receives full compensation for his actual loss, he is not unjustly enriched by being paid twice for the same loss.¹¹²⁵ It would be unfair to deny the insured all his rights and remedies respecting the loss when he had not been fully compensated for his total loss.¹¹²⁶ The insured should not be unjustly enriched by an overpayment but he is entitled to full compensation before the insurer is paid anything. Only if the insured had recovered more than his total loss the insurer would have being entitled to the surplus.¹¹²⁷

Similarly, there are a number of authorities in other jurisdictions which support the view that, until the insured has been fully compensated, the insurer is not entitled to any subrogation recovery.

3.3.2.2. *Canadian cases*

In Canada, the leading case in this line is *National Fire Insurance Company v. McLaren*.¹¹²⁸ It was held that the fact that a damages award received in an action against a third party is greater than a certain valuation of the property did not estop the insured as against the insurer from proving that in reality the property was worth more. The insured has a first claim to the damages recovered and he is entitled to an indemnity up to this real value.¹¹²⁹ Put differently, the insured is entitled to a full compensation for his actual loss. In this case, Chancellor Boyd stated that: “The doctrine of subrogation is a creature of equity not founded on contract, but arising out of the relations of the parties. In cases of insurance where a third party is liable to make good the loss, the right of subrogation depends upon and is regulated by the broad underlying principle of securing full indemnity to the insured, on the one hand, and on the other of holding him accountable as trustee for any advantage he may obtain over and above compensation for his loss... **The primary consideration is to see that the insured get full compensation for the property destroyed and the expenses incurred in making good his loss. The next thing is to see that he holds any surplus for the benefit of the insurance**

¹¹²⁴ *Ibid*, at 159

¹¹²⁵ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1029

¹¹²⁶ *Confederation Life Ins Co v Causton* (1989) 60 D.L.R. 372

¹¹²⁷ J Birds, “Contractual Subrogation in Insurance”, [1979] J.B.L. 124, p128

¹¹²⁸ (1886) 12 O.R. 682

¹¹²⁹ SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p134

company.¹¹³⁰ It is submitted that Boyd's statement is clear and broad enough to give solution to problems arising from competing interests between the insured and the insurer. This statement is in accordance with the primary purpose of the doctrine of subrogation, a corollary of the principle of indemnity. The insured should be granted priority to recover from the third party's payment until full compensation for his total loss is achieved, and any surplus (if any) is recouped by the insurer.

In *Globe & Rutgers Fire Insurance Co v Truedell*,¹¹³¹ the Appellate Division of the Ontario Supreme Court emphasizes that the doctrine of subrogation only gives the insurer the right to seek reimbursement from the insured if the total amount received from the third party and the insurer exceeds the extent of the total loss, and only for that amount in excess of the insured's actual total loss.¹¹³²

In another case of *Ledingham v. Ontario Hospital Services Commission*,¹¹³³ the Supreme Court of Canada took a further step to protect the insured's right to receive full compensation for damages. On the basis of equity, the court dismissed the statute-based subrogation right of the insurer which gave him the right to share with the insured in any amount recovered from a third party. In this case, the plaintiffs were injured in a vehicle accident. The defendant had provided certain services to the plaintiffs. Actions for damages against Motor Vehicle Accident Claims Fund were brought. The dispute between the parties involved competing claims against the inadequate sum paid by the Fund to an insured motorist, which was less than the plaintiffs' total loss. The Commission contended that it was entitled to exercise its right of subrogation to recover the cost of insured services from a third party. The argument for the Commission was that its statute-based subrogation right¹¹³⁴ allowed it to participate in *pro rata* with the injury victims in any third party recovery. The court held that no special meaning could be given to subrogation as none was expressed in the statute and that the Commission had no claim until the insureds had recovered complete indemnity from the third party. This is so because the subrogation had the ordinary meaning assigned to it by equity

¹¹³⁰ (1886) 12 O.R. 682 at p. 687; W Gummow, "Names and equitable lien", (1993) L.Q.R 159, p161

¹¹³¹ (1927) 2 D.L.R 659

¹¹³² *Ibid*, per Hodgins JA at p661-662, and per Ferguson JA at p668-669

¹¹³³ (1974) 46 D.L.R. (3d) 699

¹¹³⁴ In Canada's Hospital Services Commission Act 1970, section 55(2) and 55(4) provide that: "...the Commission is subrogated to any right of an insured person to recover all or part of the cost of insured services from any other person, including future insured services, and the Commission may bring action in the name of the insured person to enforce such rights. ...

An insured person, who commences an action to recover for loss or damages arising out of the negligence or other wrongful act of a third party to which the injury or disability in respect of which insured services have been provided is related, shall include a claim on behalf of the Commission for the cost of the insured services."

and where the insureds are not fully compensated there is no unjust enrichment or other equity capable of supporting a claim by the Commission to share *pro rata* with them.¹¹³⁵ The court also cited with approval the description of subrogation advance in *National Fire Insurance Company v. McLaren*.

This case illustrates how the court preserves the principle of indemnity when dealing with a competition between insurer and insured in their claims to subrogation recovery. In the situation where legislation only gives the rights of subrogation to the insurer without clearly specifying priority to the insurer, the court interprets the legislation in favour of the insured. The insurer is entitled to exercise his subrogation rights, but he can exercise those rights only if the insured is fully compensated for his loss. Equitable principle is a strong ground to support the insured's full compensation. The insured is not unjustly enriched where he is not fully compensated. Equity recognises the right of the insurer to seek subrogation where the insured may receive a double recovery. It is submitted that the ratio of this case is applicable to the situation where there is no clear or specific express provision which allows the insurer to share with the insured, in *pro rata*, any amount recovered from the third party wrongdoer. The argument that the insured is deemed to be his own insurer of uninsured loss should be dismissed.

3.3.2.3. *New Zealand cases*

In New Zealand, the leading case of *Arthur Barnett Ltd v National Insurance Co of New Zealand*¹¹³⁶ has been critically discussed by several English academics.¹¹³⁷ This case concerned under-insurance. The insured suffered a fire loss of £652,774, in respect of which only £469,472 was indemnified by the insurer. The insured alleged that the third party was liable to it in damages for negligence and brought proceedings against the latter. The insurer, however, refused to support this action, waiving his subrogation rights. The insured successfully brought an action against the third party. It was held that the insurer was entitled to recoup from the subrogation recovery only if the insured recovered more than its actual total loss. The primary purpose of subrogation was emphasised in this case, McCarthy J said: “the principle that an insurer who has met **the total of the insured's loss** is then entitled to all

¹¹³⁵ (1974) 46 D.L.R. (3d) 699, at p701.

¹¹³⁶ [1965] NZLR 874

¹¹³⁷ A Brown, “An insurer's rights in litigation or contractual subrogation: an oxymoron?”, (1996) 8 Ins.L.J. 60, p2; J Birds, “Contractual Subrogation in Insurance”, (1979) J.B.L. 124; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p717

the rights which the insured has against third parties which may extinguish or diminish the loss is fundamental in insurance law.”¹¹³⁸

3.3.2.4. Australian cases

In Australia, in the case of *AFG Insurances Ltd v City of Brighton*,¹¹³⁹ the High Court of Australia held that the doctrine of subrogation must not be allowed to infringe the principle of indemnity and the insurer cannot exercise its right of subrogation if it would result in the insured being less than fully compensated for his loss. The insurer is not subrogated to those rights of the insured when the continued enjoyment of those rights by the insured is not inconsistent with the principle of indemnity.¹¹⁴⁰

3.3.2.5. American cases

Strong support for the full compensation approach can be also seen from decisions of the courts in the United States. Most American courts require that the insured be fully compensated before the insurer is entitled to any subrogation recovery.¹¹⁴¹ The United States Supreme Court adopts this approach through its decision in *American Society Co v Westinghouse Electric Manufacturing Co*.¹¹⁴² The court held that: “a surety liable only for a part of the debt does not become subrogated to collateral or to remedies available to the creditor unless he pays the whole debt or it is otherwise satisfied.”¹¹⁴³

In *Garrity v Rural Mutual Insurance Co*,¹¹⁴⁴ the insured’s loss exceeded the amount recoverable under a fire insurance policy. The Supreme Court of Wisconsin held that the insured is entitled to be fully compensated before the insurer may recoup anything from the third party wrongdoer. The court emphasised that it is the insured who has priority to the amount recoverable from the third party wrongdoer, notwithstanding that the insurer has fully

¹¹³⁸ [1965] NZLR 874, p885

¹¹³⁹ (1972) 126 C.L.R 655

¹¹⁴⁰ A Tarr, “Subrogation and the Ash Wednesday bushfire disaster”, (1987) 11 Adel.L.Rev. 232, p235

¹¹⁴¹ G Veal, “Subrogation: The duties and obligations of the insured and rights of the insurer revisited”, (1992) 28 Tort & Ins.L.J 69, p72; see also: E Rinaldi, “Apportionment of recovery between insured and insurer in a subrogation case”, (1993-1994) 29 Tort& Ins.L.J 803, p807; J Berry and J McNally, “Allocation of insurance coverage: prevailing theories and practical applications”, (2006-2007) 42 Tort Trial & Ins. Prac. L.J. 999, p1000; J Parker, “The made whole doctrine: unravelling the enigma wrapped in the mystery of insurance subrogation”, (2005) 70 Mo.L.Rev. 723;

¹¹⁴² (1935) 296 U.S. 133

¹¹⁴³ (1935) 296 U.S. 133, p137

¹¹⁴⁴ (1977) 253 N.W. 512; see also *Rimes v State Farm Mut. Auto. Ins. Co.* (1982) 316 N.W.2d. 348; *Oss v United States Automobile Assurance* (1987) 807 F.2d. 457; *Ray v Donohew* (1986) 352 S.E.2d. 729; *Fleetwood v Med Center Bank* (1990) 786 S.W.2d. 550; *Powell v Blue Cross and Blue Shield of Alabama* (1990) 581 So.2d. 722;

indemnified the insured in terms of the policy. Where the recovery sum from the third party wrongdoer is not sufficient for the insured's full compensation, the principle of equity does not permit the insurer to recover anything from the third party wrongdoer.

In *Blue Cross and Blue Shield United v Fireman's Fund Insurance Co*,¹¹⁴⁵ the court had dismissed the insurer's subrogation claim against a third party wrongdoer's liability insurer because the insurer had failed to prove that the insured had recovered in full.

In conclusion, the purpose of insurance is to pay back or indemnify policyholders for what they have lost, or in other words, to restore the insured as far as practical to his pre-loss condition. The subrogation principles should be interpreted in ways that give effect to the greatest possible recovery for the insured until full compensation is achieved, but preventing the insured from receiving double payment.

4. THE DISTRIBUTION OF SUMS RECEIVED OR RECOVERED FROM THIRD PARTIES

How to distribute the subrogation recoveries from the third party is a very important aspect of the principle of subrogation. Every country's law contains some rules on this point, but the approaches are different.¹¹⁴⁶ Some approaches are completely in favour of the insurers, some approaches are consistent with the principle of indemnity, and others are to some extent in between. The purpose of this part of the thesis is to find out whether or not the Vietnamese rules and laws are consistent with the principle of indemnity.

The question of distribution of subrogation recovery from a third party relates directly to the issue of whether the full compensation approach or the full indemnity approach applies where the third party's payment is available. The relative rights of the insured and the insurer to any

¹¹⁴⁵ (1987) 411 N.W.2d. 133

¹¹⁴⁶ There are five approaches. First, the insurer is the sole beneficial owner of the claim against the third party and is entitled to the full amount recovered, whether or not it exceeds the amount paid by the insurer to the insured. Second, the insurer is to be reimbursed first out of the recovery from the third party, and the insured is entitled to any remaining balance. Third, the recovery from the third party is to be prorated between the insurer and the insured in accordance with the percentage of the original loss for which the insurer paid the insured under the policy. Fourth, out of the recovery from the third party the insured is to be reimbursed first, for the loss not covered by insurance, and the insurer is entitled to any remaining balance, up to a sum sufficient to reimburse the insurer fully, the insured being entitled to anything beyond that. If there is any windfall, it goes to the insured. Fifth, the insurer is the sole owner of the claim against the third party and is entitled to the full amount recovered, whether or not the total thus received from the third party and the insurer exceeds his loss; see R. Keeton, *Basic text on insurance law*, (West Publishing Co., 1971), p160-162

payment from a third party will be critically evaluated. The question of whether the underinsured insured is given priority in pursuing the third party's payment to achieve a full compensation for his total loss or whether the insurer has a first claim to the third party's payment within the amount of his payment will be analysed in details.

This question might not arise if the subject matter is fully insured or if the third party's payment is sufficient to cover the insured's total loss. The insured will be fully compensated for his actual total loss. The problem commonly arises from the three situations: under-insurance, loss under an excess or deductible clause, and valued policy.

In English law, the rules governing allocation of subrogation recovery are quite comprehensive, complicated and detailed. The issue of distribution of subrogation recovery has been strongly disputed in England for a long time. However, in Vietnamese insurance laws, there are few rules concerning competition between the insured and the insurer in their claims to subrogation recovery from the third party. The Vietnamese approach and English approach will be critically analysed to examine whether or not these approaches are consistent with the principle of indemnity. Finally, recommendation for the reforms of Vietnamese insurance laws will be proposed.

4.1. Vietnamese approach:

In Vietnam, the question of the distribution of subrogation sum recovered from a third party rarely arises, possibly, because the insurer and the insured have separate rights to take action against the third party for their own respective benefit if the insured's loss contains insured loss and uninsured loss. The insurer has a right to bring an action against the third party wrongdoer for his payment to the insured, and the insured has a right to take an action against the third party for the insured's uninsured balance.¹¹⁴⁷ This is contrary to English law: a cause of action may not be litigated twice. It creates a heavy burden on the third party wrongdoer under Vietnamese insurance laws.

In fact, both parties having separate right to claim against the third party does not preserve the principle of indemnity. It seems that Vietnamese insurance laws are in favour of the insurers, giving the insured little chance of achieving full compensation. Commonly, the insurer is given priority to the third party's payment. There are several obstacles to the

¹¹⁴⁷ Article 577(2) of Vietnam's Civil Code 2005

insured achieving full compensation for his total loss. Furthermore, several problems in respect of legal procedure may arise.

For example, once the insurer has paid the insured under the policy, the insurer is immediately subrogated to the insured's right of claim against the third party within the sum he paid, regardless of whether or not the insured has received any portion of compensation for the loss which is not covered by the policy.¹¹⁴⁸ The insured cannot join the proceedings against the third party wrongdoer which is already conducted by the insurer to claim for the uninsured loss. In commercial practice, after the insured has signed the subrogation and receipt form, the insurer often takes an action against the third party wrongdoer as soon as possible. The insured is under a duty to assist the insurer in proceedings against the third party.¹¹⁴⁹ The insured must assign all the rights against the third party wrongdoer.¹¹⁵⁰

Where the insured is fully insured, it is implied that, after being indemnified by the insurer, the insured has no further interest or involvement in proceedings against the third party wrongdoer. The insurer can take or abandon an action against the third party wrongdoer. The insurer may profit from the remains of the subject matter insured. Ownership of the remains has been passed to the insurer from the moment that the insured has been fully compensated by the insurer.¹¹⁵¹ This is not consistent with the principle of indemnity.

Where the payment under the insurance policy does not fully compensate for the insured's total loss, the insured has a right to claim against the third party wrongdoer for the uninsured balance. However, if the insurer cannot recoup in full for his payment, it is quite difficult for the insured to exercise his right. The reason is that, after being indemnified by the insurer, the insured must pass all his rights to claim against the third party wrongdoer, and the insured is

¹¹⁴⁸ Article 49 (1) of Vietnam's Law on Insurance Business 2000; article 577(1) of Vietnam's Civil Code 2005; article 247 of Vietnam's Maritime Code 2005

¹¹⁴⁹ Article 577(1) of Vietnam's Civil Code 2005: "*Transfers of claims for indemnity*: (1) Where a third party is at fault for causing damage to the insured, and the insurer has paid insurance benefits to the insured, the insurer has the right to demand the third party indemnify the insurer for the insurance benefits already paid. The insured must provide the insurer with all necessary information, documentation and evidence of which the insured has knowledge in order to enable the insurer to exercise its right to demand the third party [to indemnify]."; Article 248 (1) of Vietnam's Marine Code 2005: "(1) The assured shall be obliged to provide the insurer with all information, documentation as well as proof and to take necessary measures to enable the insurer to exercise the right to recourse against the third party."

¹¹⁵⁰ Article 49(1) of Vietnam's Law on Insurance Business 2000: "*Right of subrogation*: (1) Where the wrongful act or omission of a third party causes damage to an insured and the insurer has already indemnified the insured, the insured must pass to the insurer the right to claim recovery of such sum of indemnity from the third party."

¹¹⁵¹ Article 47 of Vietnam's Law on Insurance Business 2000

under a duty to assist the insurer in proceedings against the third party.¹¹⁵² Where the insurer cannot recoup in full for his payment, the insurer can argue that the insured does not properly perform his duty to assist the insurer in the proceedings against the third party.

It could be said that, due to lack of knowledge of insurance laws, Vietnamese law drafters only addressed themselves to the situation where the subject matter insured was fully insured, but did not take into account situations where: (i) the insured is not fully insured or (ii) there is a ceiling liability of the third party wrongdoer or (iii) the third party's financial resources are insufficient to cover the insured's total loss.

Vietnamese insurance laws are silent on those situations. There is no precise rule on allocation of the subrogation recovery under Vietnamese insurance laws. Only general rules are given, leaving tribunals to interpret the laws and make decisions based on the facts of cases. Therefore, similar facts of a subrogation dispute could be differently settled from court to court. The inconsistency between Vietnamese rules on distribution of subrogation recovery and the principle of indemnity will be critically analysed.

4.1.1. General rules on competition between the insurer and the insured in their claims to subrogation recovery

Under Vietnamese insurance laws, there are four guiding rules governing the competition between the insurer and the insured in their claims to the third party's payment.

(i) The insurer and the insured have separate rights to take action against the third party for their own respective benefit if the loss contains insured loss and uninsured loss.¹¹⁵³

(ii) Where the insured has received from the third party wrongdoer payment as damages that is less than the amount payable under the insurance policy, the insurer is only liable for a sum equal to the difference between the policy limit and the payment by the third party.¹¹⁵⁴

¹¹⁵² Article 49 of Vietnam's Law on Insurance Business 2000; article 577 of Vietnam's Civil Code 2005; article 248 of Vietnam's Maritime Code 2005

¹¹⁵³ Article 577(2) of Vietnam's Civil Code 2005 stipulates: "Where an insured has received monetary compensation for damage from a third party which is less than the amount payable by the insurer, the insurer is only required to pay the difference between the [total] insurance benefits [otherwise payable] and the amount paid by the third party, unless otherwise agreed. If the insured has received insurance benefits but the insurance benefits are less than the damage caused by the third party, the insured has the right to demand the third party indemnify [the insured] for the difference between the insurance benefits and the monetary compensation for the damage.

An insurer has the right to demand the third party indemnify fully [the insurer] for the amount it has paid to the insured"

(iii) Once the insurer pays the insured under the policy, the insurer is subrogated to all of the rights of the insured against the third party to the extent of the payment by the insurer to the insured.¹¹⁵⁵

(iv) Where the insured has been paid for his total loss by his insurer, the contractual relationship between the insurer and the insured comes to an end and the insurer has an exclusive right to control or abandon the proceedings against the third party wrongdoer.¹¹⁵⁶

According to these rules, there are four situations which could occur in respect of making claims to a third party's payment: (i) the insured has received payment from the third party before making a claim against the insurer, (ii) after indemnifying the insured, the insurer acts before the insured to claim against the third party, (iii) the insured takes an action before the insurer, and (iv) the insured and the insurer jointly bring an action against the third party.

4.1.1.1. The insured has received payment from the third party before making a claim against the insurer:

If the insured has received payment from the third party before making a claim against the insurer, the insurer is only liable for the sum equal to the difference between the third party's payment and the amount payable under the insurance policy.¹¹⁵⁷ There is no problem if the insured is fully insured. However, where the insured is under-insured or there is an excess clause in the insurance policy, Vietnamese laws clearly favour the insurer, giving the insurer first priority over any money that the insured has collected from a third party. For example, the subject matter insured is insured for £1,000 and there is an excess clause of £100. The insured received £700 from a third party. The insurer is only liable for £200. This result is not consistent with the principle of indemnity. The insured is not fully compensated for his total loss. The insured must stand behind the insurer when the recovery sum is distributed.

A number of problems relating to judicial procedure may arise where the insured, who does not wish to make a claim against the insurer first, instead takes an action against the third

¹¹⁵⁴ Article 577(2) Vietnam's Civil Code 2005

¹¹⁵⁵ Article 577(2) Vietnam's Civil Code 2005

¹¹⁵⁶ Article 47 of Vietnam's Law on Insurance Business 2000

¹¹⁵⁷ Article 557 (2) of Vietnam's Civil Code 2005: "(2) Where an insured has received monetary compensation for damage from a third party which is less than the amount payable by the insurer, the insurer is only required to pay the difference between the [total] insurance benefits [otherwise payable] and the amount paid by the third party..."; article 248(3) of Vietnam's Maritime Code 2005: "(3) If the assured has received the indemnity for losses from the third party, the insurer shall be obliged to pay only the difference between the indemnity amount according to the contract of insurance and the amount of money the assured received from the third party."

party wrongdoer for his entire loss. There are two different approaches to this issue. First, some courts allow the insured to claim for his entire loss. However, the legal consequences of this approach are that: (i) if the recovery sum is less than the indemnity under the insurance policy limit, the insurer is only liable for the difference between the insurance benefit and the amount paid by the third party;¹¹⁵⁸ (ii) if the recovery sum exceeds the amount payable under the insurance policy, the insurer is no longer under a duty to indemnify the insured for insured loss. The insured is not entitled to claim from the insurer for the loss which is unrecoverable from the third party wrongdoer, and the insured himself must bear the uninsured loss.¹¹⁵⁹ It is clear that Vietnamese insurance laws give the insurer priority to the third party's payment, leaving the insured not fully compensated for his total loss.

Second, some courts do not allow the insured to claim for his entire loss. The courts argue that the insured is only entitled to claim against the third party wrongdoer for the loss which is not covered by the insurance policy on the ground that the insured loss is to be recovered from the insurer. This approach is inconsistent with the general rule of subrogation that either the insured or the insurer must sue the third party wrongdoer for the insured's total loss. This approach also contrasts with the fundamental rule of insurance law by which the third party wrongdoer cannot benefit from the fact that all or part of the insured's loss has been met by the insurer. The third party wrongdoer, for instance, can get benefit in the situations where the insurer waives his rights of subrogation. Moreover, this approach is contrasted with English law; a cause of action may not be litigated twice.

In sum, Vietnamese insurance laws give the insurer first priority over any money that the insured collects from a third party, leaving the burden of going uncompensated on the insured. This is inconsistent with the principle of indemnity. Furthermore, there is confusion between the doctrine of subrogation and the doctrine of assignment under Vietnamese insurance laws.¹¹⁶⁰ This confusion causes several problems for the parties involved in a subrogation dispute. It also creates unnecessary legal proceedings against the third party wrongdoer.

¹¹⁵⁸ Article 49 of Law on Insurance Business 2000. In this situation, there is no clear rule on insurer's right of subrogation. It seems that the insurer has no right to claim against the third party wrongdoer. It is quite absurd, if the insurer brings an action against the third party wrongdoer. The third party wrongdoer can argue that the dispute between him and the insured has been settled by the court, and he has been released from responsibility.

¹¹⁵⁹ It is implied from Article 49 of Law on Insurance Business 2000

¹¹⁶⁰ This confusion will be critically analysed below at section 5 of this Chapter

4.1.1.2. *The insurer acts before the insured to claim against the third party:*

If the insurer, after having indemnified the insureds, makes a claim against the third party for the amount he paid to the insureds before the insureds do so, a question arises as to whether the insurer is entitled to recoup an amount up to the amount he has paid. For example, a property was insured for £10,000, where the agreed value and the actual value of the property was £15,000. When the property was totally destroyed because of the third party's fault, the insurer paid to the insured £10,000 under the policy, and then obtained a subrogation and receipt form from the insured. The insurer subsequently brought action against the third party for £10,000 of his policy liability and obtained that amount. The insured later made a claim against the third party for £5,000 but recovered nothing. Is there any possibility for the insured to share with the insurer the sum recovered from the third party wrongdoer under Vietnam's insurance laws? Vietnamese laws of insurance give a negative answer to this question.¹¹⁶¹ The insured must bear the loss of £5,000. This is so because the insurer and the insureds have separate rights to take an action against the third party, and the judgments of the two cases are relatively independent of each other.

This is unfair to the insureds. The insureds have not been fully compensated for their total loss and they themselves must bear the loss. The insurer is given priority to the subrogation recoveries from the third party wrongdoer. In this situation, taking out or not taking out an insurance policy has the same consequence on the insured.

Once again, there is confusion between the doctrine of subrogation and the doctrine of assignment under Vietnamese insurance laws. In this scenario, the provisions concerning the subrogation rights of the insurer under Vietnamese insurance laws likely refer to the doctrine of assignment. The insurer is allowed to obtain any subrogation recovery from the third party

¹¹⁶¹ Article 577 (1) of Vietnam's Civil Code 2005: "*Transfers of claims for indemnity*: (1) Where a third party is at fault for causing damage to the insured, and the insurer has paid insurance benefits to the insured, the insurer has the right to demand the third party indemnify the insurer for the insurance benefits already paid. The insured must provide the insurer with all necessary information, documentation and evidence of which the insured has knowledge in order to enable the insurer to exercise its right to demand the third party [to indemnify]."; Article 247 of Maritime Code 2005: "*Transfer of the right to recourse*: After having indemnified the insured, the insurer shall have the right to recourse against the person who is responsible for such loss (hereinafter referred to as the third party) within the amount paid. The insurer shall exercise this right in accordance with the provisions applicable to the insured."; Article 49(1) of Vietnam's Law on Insurance Business 2000: "*Right of subrogation*: (1) Where the wrongful act or omission of a third party causes damage to an insured and the insurer has already indemnified the insured, the insured must pass to the insurer the right to claim recovery of such sum of indemnity from the third party." If English law applies, the insured can share with the insurer in proportion to their respective interests because the average principle is applicable to this circumstance.

wrongdoer up to what he has paid to the insured under the policy, regardless of the interests of the insureds.

4.1.1.3. The insured takes an action against the third party wrongdoer before the insurer:

If the insured takes an action before the insurer to claim for the uninsured loss against the third party, can he keep all the recoveries without regard to the insurer's interest?

Take the above example: after having been indemnified by the insurer, the insured claimed against the third party for £5,000 of the uninsured loss and his claim was satisfied. The insurer also claimed later for £10,000 against the third party, but he was only able to pay the insurer £5,000 because of financial problems. Can the insured keep all the £5,000 even if the insurer only gets the £5,000? It seems that the answer is yes. However, in this situation, the insurer can argue that the insured did not properly fulfil his duties to assist the insurer in making claim against the third party wrongdoer. If the insurer can prove that this is the case, he will bring an action against the insured to recover part of the payment which had been paid to the insured.¹¹⁶²

According to Vietnamese insurance laws, where the insured breaches of his duty to provide necessary documentation and information¹¹⁶³ that enables the insurer to exercise subrogation rights against the third party wrongdoer, the insurer is entitled to deduct a reasonable amount from the payable indemnity or to refuse to pay the insured's claim. However, in practice, it is not very easy for the insurer to exercise those rights. It costs time and money to reclaim from the sum which has already come into the hands of the insured. Therefore, some Vietnamese academic writers have argued that the insurer should be allowed not to pay promptly to the insured.¹¹⁶⁴ Instead, the insurer can make a promise to pay a specified amount in writing and subsequently takes an action against the third party with the assistance from the insured.

¹¹⁶² Article 49(2) of Vietnam's Law on Insurance Business 2000: "If the insured refuses to pass such right to the insurer or does not reserve or abandons the right to make a claim against the third party, then the insurer shall have the right to deduct an amount of indemnity depending on the level of fault of the insured."

Article 248(1) & (2) of Vietnam's Marine Code 2005: "(1) The assured shall be obliged to provide the insurer with all information, documentation as well as proof and to take necessary measures to enable the insurer to exercise the right to recourse against the third party. (2) Where the assured fails to perform the obligations specified in Clause 1 of this Article or he/she is at fault that makes the insurer's right to recourse unexercisable, the insurer shall be exempt from the payment of the whole indemnity or enjoy a reasonable reduction of the payable indemnity..."

¹¹⁶³ This duty is different from the duty of good faith imposed on the insured. Where the insured breaches his duty of good faith, the insurer has a right to avoid the insurance contract under Vietnamese laws of insurance.

¹¹⁶⁴ Nguyen Thi Thuy, "Chuyen giao quyen doi boi thuong trong bao hiem tai san" (Transfer of right to make a claim in property insurance), (2008) *Legal Science Journals*, no.11 (November), p9

Where the insured fails to perform his duty properly, the insurer can exercise effectively his right to deduct a reasonable amount from his payment or to refuse to make payment to the insured.

This argument should be wrong because it undermines the insured's right to receive money promptly, which is in accordance with the terms and conditions under the policy, and it allows the insurer to delay payment, infringing a fundamental obligation under the insurance contract. This argument actually protects the insurer's interests, conversely reducing the interests of the insured. Indeed, the insurer has been protected by the law. In some circumstances at least, the insurer may rely on the insured's act as a breach of insurance contract, entitling him to damages against his insured if a relevant loss occurs.

The insured's overall financial position in accordance with this rule should be considered. As a general rule, the insured's overall financial position should not depend on whether the insured first recovers from the insurance policy or whether instead he proceeds directly against the party at fault.¹¹⁶⁵ The amount recoverable by the insured should be the same.

However, under Vietnamese laws of insurance, this amount can be different. If the insured recovers first from the third party wrongdoer and subsequently from the insurer, the insurer is only liable for the difference between the sum recovered from the third party and the policy limit.¹¹⁶⁶ It means that the maximum amount recoverable by the insured is the policy limit under the insurance policy.

The different financial position of the insured can be seen if the insured adopts another way. If he first claims from the insurer an indemnity to the extent of the policy limit, he is still entitled to bring proceedings against the third party wrongdoer for his uninsured loss which is not covered by the policy.¹¹⁶⁷ It means that he might be fully compensated for his total loss.

¹¹⁶⁵ SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p137

¹¹⁶⁶ Article 557 (2) of Vietnam's Civil Code 2005: "(2) Where an insured has received monetary compensation for damage from a third party which is less than the amount payable by the insurer, the insurer is only required to pay the difference between the [total] insurance benefits [otherwise payable] and the amount paid by the third party..."; article 248(3) of Vietnam's Maritime Code 2005: "(3) If the assured has received the indemnity for losses from the third party, the insurer shall be obliged to pay only the difference between the indemnity amount according to the contract of insurance and the amount of money the assured received from the third party."

¹¹⁶⁷ Article 557 (2) of Vietnam's Civil Code 2005: "...If the insured has received insurance benefits but the insurance benefits are less than the damage caused by the third party, the insured has the right to demand the third party indemnify [the insured] for the difference between the insurance benefits and the monetary compensation for the damage..."

This difference in the insured's financial overall position is an example of the Vietnamese law drafters' lack of knowledge of insurance laws. It could be said that the Vietnamese law drafters never addressed themselves to the problem of insufficient recovery from the wrongdoer or any resulting problem of priority between the insurer and the insured. They only addressed themselves to the situation where the subject matter insured is fully insured. It results in no difference in the overall financial position of the insured. Yet, it could be different if the insured is under-insured. It is submitted that this difference should be removed from Vietnamese insurance laws.

4.1.1.4. The insured and insurer claim against the third party together:

If the insured and insurer claim against the third party together, how to divide the insufficient sum recoverable from the third party wrongdoer? Vietnamese insurance laws do not give precise rules on this issue. It initially depends on the litigation agreement between the insurer and the insured prior to commencing any action against the third party wrongdoer.¹¹⁶⁸ This agreement could be made before the parties jointly bring an action against the third party wrongdoer.

The litigation agreement between the insured and the insurer may not be in favour of the insured

The insured must commonly accept some terms and conditions which are not in his favour. The reason for this is that the insured is normally in a weaker position by comparison with the insurer in respect of negotiating the terms and conditions in the agreement relating to the subrogation proceedings. Vietnamese insurance laws give the insurer a separate right to claim against the third party wrongdoer for his payment to the insured.¹¹⁶⁹ The insurer does not need to step into the insured's shoes in making a claim against the third party wrongdoer.¹¹⁷⁰ The insurer can use his own name to take an action against the third party wrongdoer¹¹⁷¹ and

¹¹⁶⁸ The analysis on litigation agreements between insureds and insurers before commencing proceedings against the third party wrongdoer in this section is based on open talks to some judges in Hanoi People's Courts and some senior legal staffs of insurance companies, such as Bao Viet, PVI and MIC.

¹¹⁶⁹ Article 577 of Vietnam's Civil Code 2005; article 49 of Vietnam's Law on Insurance Business 2000; article 248 of Vietnam's Maritime Code 2005

¹¹⁷⁰ It is in contrast with English approach; see *Mason v Sainsbury* (1782) 3 Doug. K.B. 61

¹¹⁷¹ Article 577(1) of Vietnam's Civil Code 2005: "*Transfers of claims for indemnity*: (1) Where a third party is at fault for causing damage to the insured, and the insurer has paid insurance benefits to the insured, the insurer has the right to demand the third party indemnify the insurer for the insurance benefits already paid..."; Article 49(1) of Vietnam's Law on Insurance Business 2000: "*Right of subrogation*: (1) Where the wrongful act or omission of a third party causes damage to an insured and the insurer has already indemnified the insured, the insured must pass to the insurer the right to claim recovery of such sum of indemnity from the third party.

he does not need to pay attention to the insured's proceedings against the third party. The outcome of the insured's proceedings against the third party wrongdoer cannot affect the insurer's right of subrogation.

Because the insurer himself has a right to sue the third party wrongdoer to recover his payment to the insured, jointly bringing an action against the third party wrongdoer means that the insurer offers the insured assistance in claiming against the third party wrongdoer. Moreover, the insurer has much more professional experience and legal knowledge in dealing with insurance disputes as well as in legal proceedings; moreover, asking for legal advice from solicitors is still unusual to some Vietnamese individuals and businessmen, and also some insureds. Getting involved in litigation is normally as a last resort to settle a dispute, amicable settlement and mediation being the common methods of resolution. Therefore, in order to avoid legal problems of his own proceedings against the third party, and leave the burden of dealing with the courts to the insurer, the insured may agree to some terms and conditions in the litigation agreement, which are not in his favour.

The parties may agree that any recovery is to be apportioned between them in accordance with their respective interests or to be divided in a proportion which they actually stipulate in their agreement. In this agreement, as the insured is inexperienced in dealing with problems of litigation, the insured commonly agrees that the insurer is given authority to act on the behalf of the insured. The insured will accept the outcome of the proceedings even if this outcome is not in his favour.

In practice, the insurer is not really interested in joining with the insured in the proceedings against the third party wrongdoer because it may result in extra work and preparation for the proceedings and increase the cost of the proceedings, or cause a dispute over allocation of recovery money. The insurer commonly wishes to avoid these problems.

How to distribute the subrogation recovery from a third party if it is stipulated in the litigation agreement between the insured and the insurer

Complication may arise in the situation where the apportionment that the insured and the insurer expressly stipulate in their agreement gives the insurer an amount of recoupment greater than his payment under the policy. A question arises as to whether the insurer is entitled to keep that amount or whether he is only entitled to recover within his payment.

The insured may argue that the insurer cannot recover more than what he paid under the policy. The sum in excess of the insurer's payment should be recovered by the insured. However, the insurer can contend that the parties have made a clear agreement on the allocation of recovery sum resulting from the proceedings against the third party wrongdoer. Freedom of contract is expressly recognised under Vietnamese laws of contract.¹¹⁷² The litigation agreement is the final settlement on the issue and is binding to both the insurer and the insured.

Conversely, if the amount of recoupment by the insurer in compliance with the agreement is less than his payment under the policy, the insurer is only entitled to recoup that amount. According to this assumption, the insurer cannot dispute that he has a first priority to recover up to the extent of his payment under Vietnam's insurance laws. Therefore, the proportion stipulated in the agreement between the parties is binding on both parties.

There is no clear guideline for Vietnamese judges and arbitrators. Different judgments can be seen from different courts or tribunals. The court has a great discretionary power to interpret legislation or to find out the intention of the parties according to written evidence submitted by the parties. Different judgments reflecting the two different views above can also be given by Vietnamese courts.

The two following cases may illustrate the problem. The first case of *Bao Minh v Giang Vo*¹¹⁷³ was about fire insurance. In this case, Thang Long had hired Giang Vo Electrical Co. to install a new electrical system in its store. The new system caused fire due to Giang Vo's negligent work. Thang Long had previously purchased fire insurance from Bao Minh Insurance Company. The policy limit under the insurance policy was VND 500 million and the excess clause was VND 10 million. The damage to the insured's store was about VND 1,000 million. Thang Long obtained VND 490 million from the insurer. Both parties entered into an agreement to bring an action against Giang Vo, in which it was stipulated that: "Any recoveries from Giang Vo Co. Ltd are to be apportioned between Bao Minh Insurance Co. and Thang Long Co. Ltd in the ratio 60 to 40." An amount of VND 950 million was

¹¹⁷² Article 4 of Vietnamese Civil Code 2005: "*Principle of free and voluntary undertaking and agreement* The law guarantees the freedom to undertake and agree on the establishment of civil rights and obligations if such undertakings and agreements do not breach matters prohibited by law and are not contrary to social ethics. In civil relations, parties shall be entirely voluntary and no party may force upon, prohibit, coerce, intimidate or hinder any other party. All lawful undertakings and agreements shall bind the parties and must be respected by individuals, legal entities and other subjects."

¹¹⁷³ Hanoi People's Court 2007

recovered from the third party wrongdoer. The court granted VND 570 million to the insurer, leaving VND 380 million for the insured, on the grounds that the provision above was absolutely binding on the both parties and the insured could not dispute otherwise.

Several problems emerged from this case. First, the insurer was able to profit from the loss of the insured,¹¹⁷⁴ which is not consistent with the principle of indemnity. The insurer may not recover, through exercise of subrogation right, more than the sum paid out under the insurance policy. Second, the insured had to bear a loss of about VND130 million. This is absurd since the insured was not fully compensated for his total loss, whereas the insurer made money from the insured's loss.

The second case of *BIDV v Gold Star*¹¹⁷⁵ was concerned with marine insurance. The facts, in brief, were that the dried raw cashew nuts of the insured were partly insured and sustained damage due to the carrier's fault. Donafood had taken out an insurance policy with BIDV Insurance Co. The sum insured was USD 200,000, but the agreed value and the actual value of the goods were worth about USD 250,000. The insured suffered the loss of about USD 100,000. The insurer paid USD 80,000 to the insured. After the insurance settlement, the insurer and the insured together commenced an action against the carrier. The insurer and the insured obtained a joint judgement of USD 93,000.

The parties disputed over the allocation of subrogation recovery. The insured argued that the sum should be divided between him and the insurer in accordance with their respective interests (on the basis of the 1:4 proportions). The insurer contended that he had priority to the amount recovered from the third party wrongdoer, in accordance with article 247 and 248 of Vietnam's Maritime Code 2005.¹¹⁷⁶ Moreover, the subrogation receipt signed by the insured provided: "We, Donafood received from BIDV Insurance Co the compensation

¹¹⁷⁴ It contrasts with English law; see *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330

¹¹⁷⁵ Hochiminh People's Court 2008

¹¹⁷⁶ Article 247 of Maritime Code 2005: "*Transfer of the right to recourse*: After having indemnified the insured, the insurer shall have the right to recourse against the person who is responsible for such loss (hereinafter referred to as the third party) within the amount paid. The insurer shall exercise this right in accordance with the provisions applicable to the insured."; Article 248 of Vietnam's Marine Code 2005: "(1) The assured shall be obliged to provide the insurer with all information, documentation as well as proof and to take necessary measures to enable the insurer to exercise the right to recourse against the third party. (2) Where the assured fails to perform the obligations specified in Clause 1 of this Article or he/she is at fault that makes the insurer's right to recourse unexercisable, the insurer shall be exempt from the payment of the whole indemnity or enjoy a reasonable reduction of the payable indemnity. (3) If the assured has received the indemnity for losses from the third party, the insurer shall be obliged to pay only the difference between the indemnity amount according to the contract of insurance and the amount of money the assured received from the third party."

amount of USD 80,000 in full and final settlement in respect of the above-mentioned matter... In consideration of having received this payment, we hereby agree to transfer and assign to you, to the extent of your interest, all of the rights and remedies in respect of the subject matter insured, and to grant you full power and give you any assistance you may reasonably require of us in the exercise of such rights and remedies in your name and at your own expenses.” Relying upon this provision and Vietnam’s insurance laws,¹¹⁷⁷ the court found that the insured has assigned his entire right of recovery, to the extent of payment, to the insurer, and awarded the insurer priority up to USD 80,000.

It can be seen that this judgement contrasts with the English approach, according to which, where the agreed value of the subject matter insured is greater than the sum insured, the insured is deemed to be his own insurer for the uninsured balance.¹¹⁷⁸ In marine insurance, the principle of average is implied in the policy. Therefore, any subrogation recovery from the third party wrongdoer shall be divided between the insurer and the insured in accordance with the sums insured and uninsured.¹¹⁷⁹

Under Vietnamese insurance laws, the insured is also deemed to be his own insurer for the uninsured balance, where the insured is insured for an amount less than the policy valuation.¹¹⁸⁰ The insurer is only liable for losses in such proportions as the insured amount bears to the policy valuation. Therefore, BIDV Insurance Co was required to pay the insured only USD 80,000 for the insured’s partial loss of USD 100,000. However, the principle of average does not play any role in allocation of recovery sum from a third party wrongdoer under Vietnamese laws. The allocation is first based on the litigation agreement between the insured and the insurer. The insured is not entitled to share the subrogation recovery with the insurer. Vietnamese insurance laws are harsher to the insured than English insurance laws. The insurer has a first claim to the subrogation recovery from the third party under Vietnamese insurance laws.

¹¹⁷⁷ Article 247 and 248 of Vietnam’s Maritime Code 2005, article 577 of Vietnam’s Civil Code 2005

¹¹⁷⁸ Section 81 of MIA 1906

¹¹⁷⁹ *The Commonwealth* (1907) P 216 CA. In this case, a vessel was insured under a valued policy for £1,000, but the actual and agreed value of it was £1,350. The sum of £1,000 was recovered from the third party wrongdoer. It was held that this sum was to be divided between the insurer and the insured in the proportions to their respective interests (1,000: 350)

¹¹⁸⁰ Article 233 of Maritime Code 2005: “*The insured sum*: (1). Upon concluding a contract of marine insurance, the insured must declare the sum for which the subject of insurance is insured (hereinafter referred to as the insured sum). (2). Where the insured sum as specified in the contract is lower than the insurable value, the insurer shall be liable for losses in such proportions as the insured amount bears to the insurable value, including other expenses under the insurance...”

This is an example of unnecessarily legal protection for the insurers under Vietnamese insurance laws. In fact, this is inconsistent with the principle of indemnity. The principle of subrogation is designed to prevent the insured from unjust enrichment, not to give priority to the insurer as to recoupment from subrogation recovery. There is no question of the insured making profit in the case above. The result of allocation of subrogation recovery from the third party wrongdoer under Vietnamese laws is wrong in principle. It deprives the insured from not only the right to be fully compensated for his total loss but also the right to share with the insurer, in proportion, any amount recovered from the third party.

This is also an example of misinterpretation of a provision copied from other laws. In this aspect of under-insurance, Vietnamese legislation is the same as English provision. However, it is interpreted in a different way, establishing different rules to protect the insurers. The reason for this protection for insurers under Vietnamese insurance laws may be that almost all major insurance companies are state-owned enterprises. Benefits of state-owned enterprises are commonly protected by Vietnamese laws.¹¹⁸¹

How to distribute the subrogation recovery from a third party if it is not stipulated in the litigation agreement between the insured and the insurer

Where the insured and the insurer jointly bring proceedings against the third party wrongdoer, but there is no agreement between the parties on allocation of the recovery money, the court will settle the dispute according to its view. The judgments can be different from court to court. First, the insurer is often given priority to the recovery sum up to the extent of his payment. The reason is that the insurer has a right to recover up to his payment to the insured and the insured is deemed to be his own insurer for the uninsured balance.¹¹⁸²

Second, in some cases, the insured could share with the insurer any sum recovered from the third party wrongdoer, in proportion and in accordance with their respective interests. The proportionate sharing approach may be used if the insured and the insurer, during the process of the proceedings against the third party wrongdoer, reach a mutual agreement on allocation of recovery sum from the third party wrongdoer. In this situation, the insured is normally an important and long-time customer of the insurer, and the insurer wishes to keep doing business with him. The mutual agreement is considered as successful conciliation which is

¹¹⁸¹ Ngo Thi Ngoc Thu, ‘Viet Nam’s legal environment of foreign investment in comparison with other regional countries’, (2005) *Economic Development Review*, p5

¹¹⁸² See article 43 and 49 of Vietnam’s Law on Insurance Business 2000

recognized by the court.¹¹⁸³ Consequently, the mutual agreement is final settlement on the dispute over allocation of subrogation recovered from the third party and binding on the both parties.

It is submitted that, in the situation where there is no litigation agreement between the insured and the insurer when jointly commencing the proceedings against the third party wrongdoer, the ways that Vietnamese courts deal with the competition between the insurer and the insured in their claims to the third party wrongdoer are inconsistent with the principle of indemnity. The insured is not fully compensated for his total loss; meanwhile, the insurer is given priority up to the amount he has paid out. The courts depend on their own views, and have discretionary power to give judgements, and commonly support the view that the insurer is to be reimbursed first out of the recovery from the third party irrespective of whether or not the insured is fully compensated for his total loss.

To sum up, where the insurer and the insured jointly bring an action against the third party wrongdoer, Vietnam's insurance laws do not establish any clear rule on allocation of subrogation recovery from a third party wrongdoer. The insured and the insurer are free to negotiate their litigation agreement in respect of the proceedings against the third party wrongdoer. This results in several problems as discussed above. The insured is put in weaker position in the competition with the insurer in respect of their claims to the subrogation recovery from the third party wrongdoer. Moreover, the courts have discretionary power to interpret the rules, and different judgments are given by different courts, which creates inconsistency and difficulty for parties getting involved in insurance disputes over subrogation recovery.

4.1.2. Who can obtain the fruit of action against the third party wrongdoer where the third party's payment is greater than the insured's total loss?

In practice, it rarely occurs that the third party's payment is greater than the insured's total loss. However, the case of *Yorkshire Insurance Co v Nisbet Shipping Co*¹¹⁸⁴ gives an example of the situation where the payment recovered from the third party was more than sufficient to

¹¹⁸³ Do Van Dai, *Luat hop dong Viet Nam: ban an va binh luan an*, (NXB Chinh tri quoc gia, 2008) [Trans: Do Van Dai, *Vietnamese contract laws: judgments and commentaries*, (National Politics Publishing House, 2008)], p215-216

¹¹⁸⁴ (1962) 2 Q.B. 330

fully reimburse both the insured and the insurer. Supposing that there was a similar case under Vietnamese insurance laws, the question arises as to who would be entitled to the fruit.

According to Vietnam's insurance laws, where the insured is fully compensated for his loss by the insurance policy, it is assumed that the insured has no further interest or involvement in the proceedings against the third party wrongdoer. The insured is not entitled to receive any sum recoverable from the third party wrongdoer.¹¹⁸⁵ The insured must pass all his rights or remedies against the third party wrongdoer to the insurer.¹¹⁸⁶ In practice, the insured is required to sign a subrogation and receipt form which assigns to the insurer all rights or remedies against a third party.¹¹⁸⁷ The insurer has an exclusive right to bring an action in his own name against the third party wrongdoer. Since the insurer uses his own name to sue the third party wrongdoer, the judgment is given to him. The insurer is entitled to receive the entire amount of the subrogation recovery from the third party.

Moreover, the fruit of the proceedings against the third party wrongdoer may depend on fluctuating exchange rates.¹¹⁸⁸ The insurer may recover an amount less than his payment if the exchange rate increases. It means that gains may occur in some case, but losses may be suffered in other cases. Therefore, it is argued that it is fair when the insurer may get the fruit of action against the third party wrongdoer.

It can be said that Vietnamese insurance laws are inconsistent with the principle of indemnity. They conflict the general principle that the insurer cannot recover more than he has paid to the insured by exercising his rights of subrogation. The amount that the insurer may recoup limits to the amount of his payment. Under the principle of indemnity, the insurer is to prevent from making profit out of subrogation.

In addition, as Derham points out, instead of making a claim against the insurer, the insured can bring an action against the third party wrongdoer for his entire loss, recovering more than the full amount of his loss. The insurer will not be entitled to any damages recovered from the third party wrongdoer. The financial position of the insured should not be changed if he first

¹¹⁸⁵ Article 47 of Vietnam's Law on Insurance Business 2000

¹¹⁸⁶ Article 49 of Vietnam's Law on Insurance Business 2000

¹¹⁸⁷ "...In consideration of having received this payment, we hereby agree to transfer and assign to you, to the extent of your interest, all of the rights and remedies in respect of the subject matter insured, and to grant you full power and give you any assistance you may reasonably require of us in the exercise of such rights and remedies in your name and at your own expenses."

¹¹⁸⁸ Nguyen Van Minh, "Nguyen tac the quyen trong bao hiem hang hai" (2006) *Tap chi Bao hiem* 30 [Trans: Nguyen Van Minh, "The principle of subrogation in insurance law", (2006) *Insurance Review* 30], p32

recovers from the insurer.¹¹⁸⁹ The cause of action should be vested in the insured. It is the insured who recovers judgment against the third party wrongdoer, and the judgment can be satisfied only by payment to him.¹¹⁹⁰

There is confusion between the doctrine of subrogation and the doctrine of assignment in the Vietnamese insurance laws. Vietnamese insurance laws allow the insurer to use his own name to bring an action against the third party wrongdoer, and the legal chose in action vests in the insurer. Therefore, the fruit of action against the third party is given to the insurer. It is submitted that this confusion should be removed from Vietnamese insurance laws.¹¹⁹¹

4.1.3. Who must bear the loss under an excess clause?

Under Vietnamese laws of insurance, there is no precise rule governing the allocation of subrogation recovery in respect of an excess clause. In principle, where specific law is silent on a particular issue, general law shall apply to solve disputes arising from the particular issue.¹¹⁹² Therefore, in this circumstance, the laws of contract will be applied to find the answer to any problems arising from an excess clause in an insurance contract. However, Vietnam's laws of contract are also silent on the allocation of subrogation recovery in respect of an excess clause. Agreements in the contract between the involved parties will be applied to solve the dispute. The reason is that freedom of contract is recognised by Vietnam's laws of contract, and all lawful agreements shall be binding on the involved parties.¹¹⁹³

How terms and conditions of an excess clause apply to allocation of subrogation recovery from the third party

Excess clause is frequently incorporated into insurance policies. In some types of insurance it is compulsory because the excess clause encourages the insured to take care of the subject matter insured, reducing the possibility of the occurrence of the insured peril. It also reduces

¹¹⁸⁹ SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p137

¹¹⁹⁰ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p499

¹¹⁹¹ The confusion between principle of subrogation and principle of assignment will be critically analysed at section 5 of this Chapter

¹¹⁹² See 3.1.1 of Chapter 2

¹¹⁹³ Article 4 of Vietnamese Civil Code 2005: "*Principle of free and voluntary undertaking and agreement*

The law guarantees the freedom to undertake and agree on the establishment of civil rights and obligations if such undertakings and agreements do not breach matters prohibited by law and are not contrary to social ethics. In civil relations, parties shall be entirely voluntary and no party may force upon, prohibit, coerce, intimidate or hinder any other party.

All lawful undertakings and agreements shall bind the parties and must be respected by individuals, legal entities and other subjects."

the number of small claims to insurance companies. An excess clause is imposed in insurance policies by insurers. It is commonly defined as the amount to be deducted from any payment to be made by the insurer to the insured, and the loss falling below the policy excess shall be borne by the insured in any occurrence.¹¹⁹⁴ It is furthermore stipulated that the insurer shall not be liable for the loss falling below the policy excess in any case of loss or losses after applying all other terms and conditions in this policy, including any condition of average principle.¹¹⁹⁵ The insured, during the currency of this policy, commits not to purchase any insurance policy to cover for the loss under the policy excess.¹¹⁹⁶

The case *PVI v Vietfracht*¹¹⁹⁷ illustrates how an agreement relating to an excess clause is applied to settle the dispute over allocation of the subrogation recovery from a third party. The case was concerned with partial loss. The insured's vessel, which was insured for USD 2,000,000, incurred collision damage that cost USD 50,000 to repair. There was an excess of USD 20,000 under the insurance policy. The insurer paid the insured USD 30,000 in respect of the loss. The insurer and the insured jointly brought an action against the third party wrongdoer. The sum recovered from the third party responsible for the loss was USD 32,000. The insured and the insurer disputed over distribution of the recovery money. It was held that the insurer was entitled to recoup USD 30,000 of the sum recovered from the third party, leaving only USD 2,000 for the insured on the ground that Vietnamese insurance laws allow the insurer a right to recoup his payment to the insured from the third party wrongdoer¹¹⁹⁸ and the insured agreed to bear the loss under the excess clause in accordance with the agreement in the insurance policy. The court also presumed that if an amount recovered from the third party wrongdoer was USD 20,000, the insurer would be entitled to claim the sum in full. The insured himself had to bear the loss of USD 20,000 under the excess clause.

As in English law, any sum recovered from the third party goes to the insurer up to the extent of the insurer's payment to the insured, the insured's excess being discharged only after the insurer has been reimbursed. However, the reasoning for this rule is different from that of

¹¹⁹⁴ PVI insurance policy

¹¹⁹⁵ This Insurance Policy does not cover the amount of the Excess stated in the Insurance Certificate in respect of each and every loss as ascertained after the application of all other terms and conditions of the Insurance Policy, including any condition of Average principle. The Insured warrants that the amounts of the Excess stated in the Insurance Certificate shall not be covered by any other insurance policies.

¹¹⁹⁶ PVI property insurance policy

¹¹⁹⁷ Hanoi People Court 2007

¹¹⁹⁸ Article 17(1)(e) of Vietnam's Law on Insurance Business 2000: "An insurer shall have the rights: ...to require a third party to reimburse the insured sum which the insurer has paid to indemnify the insured person as a result of a wrongful act or omission by the third party in the cases of property and civil liability insurance..."

English law. Under Vietnamese insurance laws, the insurer has a priority to any sum that may be recoverable from a third party wrongdoer. Supposing the Napier case had been resolved under Vietnamese insurance laws; the insurer would not be required to pay anything to the insured, because the third party's payment was greater than the sum insured. The insured himself would have had to bear the uninsured loss. It means that the insured has no chance to recover from the third party's payment for the loss above the policy limit. Vietnamese insurance laws are harsher to the insured than English insurance laws.

It is submitted that Vietnamese laws are inconsistent with the principle of indemnity, by which, the insurer is clearly given priority to the third party's payment, irrespective of whether or not the insured is fully compensated for his total loss. It should be emphasized that the principle of indemnity does not prevent the insured from attaining full compensation for his total loss. It merely prevents the insured from retaining any further profit. However, under Vietnamese insurance laws, where the insurer has met in full his obligations under the insurance policy, any sum recovered from the third party wrongdoer must go first to the insurer, even if the insured cannot achieve full compensation for his total loss.¹¹⁹⁹ It is illogical because there is no double recovery or no unjust enrichment to be prevented, where the insured is not fully compensated. It seems that Vietnamese insurance laws penalize the insured who is not fully compensated for his loss, giving especially favourable protection for the insurer.

Assumption of risk between the insured and the insurer

Assumption of risk between the insured and the insurer should be critically examined here. Under the insurance policy, the insured does agree to bear the loss falling below the excess when making a claim against the insurer. However, the insured does not agree to stand behind the insurer when the sum recovered from the third party wrongdoer is distributed. There is nothing in the agreement between the parties which mentions that the insurer is given priority over the third party's payment. Therefore, there is no clear justification for granting priority to the insurer.

Furthermore, when the insurer enters into the insurance contract, he accepts a risk of loss in return for the insurance premium. The insurance premium is a valuable consideration which is paid to the insurer by the insured. The insurer knowingly takes the risk of having to pay out

¹¹⁹⁹ See section 3.2 of this Chapter

on the insured's claim even there may be no cause of action at all against a third party to reduce the insurer's actual payment, or the cause of action may be worthless because the third party is insolvent or otherwise not worth suing. The insurer may not recover anything if there is no third party involved. Put differently, by accepting the insurance premium, the insurer is obliged to take the risk of loss and to indemnify the insured in the event of loss. Therefore, there is no clear reason why the insurer should be put in a better position than the insured in respect of recovering from the third party's payment, when a third party at fault is involved. The existence of an excess clause in the policy should not strengthen the insurer's position.

In a comparison between the insured who is not fully compensated for his total loss and the insurer who has received insurance premium to bear the risk of loss, it is submitted that the insurer should stand behind the insured when the subrogation recovery is distributed. Giving the insurer right to take priority over the insured, who is not compensated for the loss under the excess clause, is unfair to the insured, because the insurer can minimise any sum which should be paid to the insured.

An excess clause is drafted by insurers, not by insureds

Another reason for the view that the insurer should bear the risk under the excess clause is that the excess clause is stipulated by the insurer. It is submitted that when the language of the excess clause does not clearly express a preference for the insurer, it should be interpreted narrowly and against the insurer. The primary purpose of an excess clause is to reduce transaction costs (such as a reduction in the number of small claims, which is a benefit to insurers) and to encourage the insured to be diligent in taking care of his property or duty.¹²⁰⁰ It is not designed to divide between the insured and the insurer the subrogation recovery from the third party wrongdoer. In the absence of an expressed provision on the insured's assent to standing behind the insurer, the mere existence of an excess clause cannot result in the insurer's better right to claim over the insured's loss under the excess clause when distributing the sum recovered from the third party wrongdoer.

Moreover, the Vietnamese approach to this issue is not in accordance with the fairer approach in other jurisdictions, such as America, Australia, Canada, and New Zealand. Boyd J in the case of *National Fire Insurance v McLaren*¹²⁰¹ states that: "... The primary purpose is to see

¹²⁰⁰ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1029

¹²⁰¹ [1886] 12 O.R. 682

that the insured gets full compensation for the destroyed property and the expenses incurred in making good his loss. The next thing is to see that he holds any surplus for the benefit of the insurance company.”¹²⁰² This statement is consistent with the principle of indemnity. The insured should be given priority to the third party’s payment until full compensation is achieved. The insurer is only entitled to recoup the sum in excess of the insured’s full compensation.

Although, the statement is not specifically concerned with under-insurance resulting through the use of an excess clause, it is suggested that its reasoning is broad enough to cover the situation. It is not unjust and not inconsistent with the principle of indemnity if the insured is fully compensated for his total loss, and the insurer is entitled only for the amount in excess of the insured’s total loss.

Whether the insureds can recover the loss under an excess from the third party

Under Vietnamese insurance laws, another situation where the insurer and the insured separately bring proceedings against the third party wrongdoer can occur. The insurer takes an action for his payment, and the insured makes a claim for the loss under the excess clause. However, it rarely happens in practice. The reason is that the loss under the excess clause is relatively small in comparison with the insured loss. The insured usually does not make a claim against the third party for the loss under the excess clause because it costs him considerable time and money to bring an action against the third party wrongdoer for that relatively small amount. If the insured does bring an action against the third party, it also creates a burden on the third party wrongdoer because the same cause of action can be litigated twice. It submitted that this situation is not compatible with the principle of indemnity because it is difficult for the insured to be fully compensated for his total loss.

4.1.4. Who bears the loss under an unvalued policy?

Under Vietnamese insurance laws, an unvalued policy is a policy that does not specify the value of the subject matter insured, but specifies the sum insured at the time of commencement of the insurance policy.¹²⁰³ Regarding the measure of indemnity, the value of the subject matter at the time of loss is recoverable. This value may or may not correspond to the insured sum that is specified in the policy at the time of entering into the insurance

¹²⁰² *Ibid*, p687

¹²⁰³ Article 43(1) of Law on Insurance Business 2000; article 228(2) of Maritime Code 2005

contract. There are two possible cases: (i) if the value of the subject matter insured is greater than the sum insured, it is presumed that the insured is underinsured;¹²⁰⁴ (ii) in contrast, if the former is less than the latter, the sum equal to the difference between the former and the latter is not accepted by the laws.¹²⁰⁵ The insurer is only liable up to the value of the subject matter at the time of loss, part of the premium shall be returned to the insured, and the insured is fully insured.

Concerning the second case, the problem of competition between the insurer and the insured in their claims to subrogation recovery does not arise, because the insured is fully insured under the insurance policy. The insurer who has already paid the full indemnity is entitled to be recouped by having that amount back.

Regarding the first case, the insured is considered as his own insurer for the difference between the value of the subject matter insured at the time of loss and the sum insured. It means that the insurer is only liable for losses in such proportion as the sum insured bears to the value of the subject matter insured. Several problems of competition between the insurer and the insured in their claims to subrogation recovery may arise.

If the insured has received payment from the third party, the insurer is only liable for the sum equal to the difference between the sum insured and the third party's payment. Where the third party's payment is greater than the sum insured, the insurer is not obliged to pay the insured anything, irrespective of the fact that the insured has not recovered some unrecoverable costs from the third party, as when, for example, the third party's ceiling liability is less than the insured's total loss. The insured himself must bear the uninsured loss. Put differently, the insurer is given priority to the third party's payment, regardless of the fact that the insured is not fully compensated for his total loss.¹²⁰⁶

Where the insured has made a claim against the insurer before bringing an action against the third party wrongdoer, it leads to the two following possibilities. The insured and the insurer have separate rights to claim against the third party, or the both parties jointly bring an action

¹²⁰⁴ Article 43(2) of Law on Insurance Business 2000

¹²⁰⁵ Article 233(3) of Maritime Code 2005: "Where the insured sum as specified in the contract exceeds the insurable value, the amount in excess of the insurable value shall not be accepted."

Article 42(2) of LIB 2000: "Where an over-insurance contract is entered into due to the unintentional wrongful act or omission of the insured, the insurer must refund to the insured the amount of paid insurance premium corresponding to the insured sum which exceeds the market value of the insured property, after deducting legitimate related expenses. Upon occurrence of the insured event, the insurer shall only be responsible to indemnify for damage not exceeding the market value of the insured property."

¹²⁰⁶ This situation has been critically analyzed above at section 4.1.1.1 of this Chapter

against the third party wrongdoer. However, in both situations, the insured cannot achieve full compensation for his total loss.¹²⁰⁷

It can be said that the Vietnamese approach is in contrast to the English approach. Under English law, where the insured is not fully insured under an unvalued policy, the insured is entitled to retain such amount of the subrogation recovery which is necessary to cover the uninsured loss before accounting for the balance to the insurer.¹²⁰⁸ The English approach to this aspect is fair to the insured. The insured is given priority to the third party's payment, leaving any surplus for the benefit of the insurer, which is consistent with the principle of indemnity.

4.1.5. Who bears the loss under a valued policy?

In the case of a valued policy, there are two situations in which the problem of competition between the insurer and the insured in their claims to the third party's payment may arise. First, the actual value of the subject matter insured is greater than the agreed value and the sum insured. Second, the sum insured is less than the agreed and actual value of the subject matter insured. Under English insurance laws, there are different rules¹²⁰⁹ on allocation of the sum recovered from the third party in the two situations, whereas the same rules are applied under Vietnamese laws.¹²¹⁰

According to Vietnamese insurance laws, the insured is deemed to be his own insurer for the amount equal to the difference between the sum insured and the actual value of the subject

¹²⁰⁷ The critical evaluation of these two situation has been made at section 4.1.1.2 and 4.1.1.3 of this Chapter

¹²⁰⁸ *Hobbs v Marlowe* (1978) A.C. 16, H.L.

¹²⁰⁹ English rules will be critically analysed below at section 4.2 of this Chapter

¹²¹⁰ Article 43 of LIB 2000: "*Contract of property insurance below value*: (1). A contract of property insurance below value means a contract in which the sum insured is less than the market value of the insured property at the time of entering into the contract. (2). In the case where a contract of property insurance below value is entered into, the insurer shall only be responsible to indemnify in accordance with the ratio of the sum insured to the market value of the insured property at the date of entering into the contract."; Article 233 of Maritime Code 2005: "*The insured sum*: (1). Upon concluding a contract of marine insurance, the insured must declare the sum for which the subject of insurance is insured (hereinafter referred to as the insured sum). (2). Where the insured sum as specified in the contract is lower than the insurable value, the insurer shall be liable for losses in such proportions as the insured amount bears to the insurable value, including other expenses under the insurance. (3). Where the insured sum as specified in the contract exceeds the insurable value, the amount in excess of the insurable value shall not be accepted."; Article 243 of Maritime Code 2005: "*The insurer's liability to refund*: The insurer shall have to refund to the assured all reasonable and necessary expenses incurred for the purpose of averting the loss or lessening its extent; expenses incurred in the implementation of the instructions of the insurer as provided for in Article 242 of this Code, or expenses incurred for identifying the cause and extent of the loss within the scope of liability of the insurer, and expenses contributed to the general average. **These expenses shall be refunded in such proportion as the insured sum bears to the insurable value.**"

matter insured, and must bear a rateable proportion of the loss accordingly.¹²¹¹ The insurer is only liable to pay to a proportion of the loss.¹²¹² This is different from the English laws that the principle of average is not automatically applied to both situations.¹²¹³

The measure of indemnity is not in favour of the insured under Vietnamese insurance laws. Where the insurer can prove that the actual value of the subject is less than the agreed value and the sum insured, the insurer is not liable for the amount in excess of the actual value.¹²¹⁴ The amount in excess of the actual value is not permitted by Vietnamese laws.¹²¹⁵ The Vietnamese rules seem unreasonable since it is open to the insurer to dispute that the policy valuation is not the same as the actual value of the subject matter insured.¹²¹⁶ It means that the value of the subject matter insured, which was specified by the insurer and the insured, is not binding on the insurer.

Regarding the allocation of the subrogation recovery from the third party, the Vietnamese rules have been critically analysed above.¹²¹⁷ First, where the insured has received payment from the third party, the insurer is only liable for the sum equal to the difference between the sum insured and the third party's payment. Second, where the insured has made a claim against the insurer before bringing an action against the third party wrongdoer, the insured and the insurer may either separately or jointly take an action against the third party. This creates difficulties for the insured to achieve full compensation for his total loss. The Vietnamese rules are inconsistent with the principle of indemnity.

¹²¹¹ Article 43 of Vietnam's Law on Insurance Business 2000, article 233 of Vietnam's Maritime Code 2005

¹²¹² Hiep hoi bao hiem Viet Nam, *Cam nang bao hiem phi nhan tho*, (NXB Tai chinh, 2011) [Trans: Association of Vietnamese Insurance, *Guidelines on non-life insurance*, (Finance Publishing House, 2011)], p119-120

¹²¹³ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p505; see also section 4.2.6 and 4.2.7 of this Chapter

¹²¹⁴ It is in contrasted with English rule. See *Elcock v Thomson* [1949] 2 All.E.R. 381

¹²¹⁵ Article 42 of Vietnam's Law on Insurance Business 2000: "*Contract of property insurance above value*: (1). A contract of property insurance above value means a contract in which the sum insured is greater than the market value of the insured property at the time of entering into the contract. An insurer and a purchaser of insurance may not enter into a contract of property insurance above value. (2). In the case where a contract of property insurance above value is entered into due to the unintentional wrongful act or omission of the purchaser of insurance, the insurer must refund to the purchaser of insurance the amount of paid insurance premium corresponding to the insured sum which exceeds the market value of the insured property, after deducting legitimate related expenses. Upon occurrence of the insured event, the insurer shall only be responsible to indemnify for damage not exceeding the market value of the insured property."; Article 233(3) of Vietnam's Maritime Code 2005: "Where the insured sum as specified in the contract exceeds the insurable value, the amount in excess of the insured sum shall not be accepted."

¹²¹⁶ It is in contrasted with English rule; the policy valuation is a conclusive evidence of the value of the subject matter insured; see also *North of England Ins Assn v Armstrong* (1870) LR 5 QB 244; *Goole & Hull Steam Towing Co Ltd v Ocean Marine Ins Co Ltd* (1928) 1 KB 589

¹²¹⁷ See section 4.1.1 of this Chapter

Under English insurance laws, where the insured is deemed to be his own insurer for the uninsured balance because of under-insurance, any amount recovered from a third party is to be apportioned between the insurer and the insured in proportion to their respective interests.¹²¹⁸ For example, a property is worth £100,000, but is insured for £50,000. The insurer pays out the full sum insured and the insured then recovers £50,000 from the third party for destruction of the property. The insured is entitled to £25,000 of the recovery sum, and the insurer may recoup £25,000. However, under Vietnamese insurance laws, the principle of average does not play any role in the distribution of the recovery sum from a third party wrongdoer. The insurer is entitled to £50,000, the entire amount of subrogation recovery.¹²¹⁹

Under English law, where the actual and agreed value of the subject matter insured is greater than the sum insured in a valued policy, not subject to average clause, it is asserted that the insured should have a first claim for an amount equal to the difference between the policy valuation and the sum insured, because it is expressed in the agreement between the parties that the insured is under-insured.¹²²⁰ This assertion is consistent with the principle of indemnity. The insured is fully compensated for his total loss, and the amount in excess of the insured's total loss is recouped by the insurer.

Vietnamese insurance laws are unfair to the insured since the latter cannot share with the insurer in any amount of the subrogation sum recovered from a third party wrongdoer until the insurer fully recoups his payment under the policy. It should be emphasised that the principle of subrogation is designed to prevent the insured from unjust enrichment, not to give priority to the insurer as to recoupment from subrogation recovery. The result of allocation of subrogation recovery from the third party wrongdoer under Vietnamese laws is wrong in principle. It not only deprives the insured of the right to be fully compensated for his loss but also the right to share with the insurer, in proportion, any amount recovered from the third party.

¹²¹⁸ *The Commonwealth* (1907) P 216 CA

¹²¹⁹ Article 248 of Vietnam's Maritime Code 2005; article 577 of Vietnam's Civil Code 2005; article 49 of Vietnam's Law on Insurance Business 2000

¹²²⁰ SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p134-135; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p505

4.2. The English approach

As has been seen, the Vietnamese approach is not effective in solving the problem of distribution of subrogation recovery from the third party, and it is inconsistent with the principle of indemnity. The insured cannot achieve full compensation for his total loss. There is a burden on the third party wrongdoer since a same cause of action could be litigated twice. It costs time and money for the parties involved in subrogation disputes. English insurance laws could be referenced as a model for the reform of Vietnamese insurance laws. The English approach will be critically analysed to examine whether or not it is consistent with the principle of indemnity, and to give some directions regarding the reform of Vietnamese insurance laws.

The general principles governing allocation of subrogation recovery from a third party will be examined, and the application of these principles to particular cases will be critically analysed in order to evaluate the effectiveness of the English approach to solving the competition between the insurer and the insured in their claims to subrogation recovery from a third party.

4.2.1. Principles governing distribution of the sum recovered from the third party

Where a subrogation action against a third party wrongdoer has succeeded, the question arises of how the subrogation recovery is to be distributed between the insured and the insurer. This question has been discussed at length under English insurance laws. There are five guiding principles governing allocation of recoveries as between insurer and insured in English insurance law.

(i) If the insured is not fully compensated under the insurance policy, he is initially entitled to the amount recoverable from the third party liable for the loss,¹²²¹ but holds any surplus of his actual loss for the benefit of the insurer.¹²²²

(ii) Where the insured's shortfall results from a deductible or excess clause, the insurer has priority to the amount recoverable from the wrongdoer, because the loss falling below the

¹²²¹ *Commercial Union Assurance Co v Lister* (1874) L.R. 9 Ch.App. 483; Even if the insurer has met its liability under the policy, but the insured has not been fully compensated, he is entitled to start proceedings himself against the third party and remain *dominus litis*, provided that he protects the insurer's interest as well as his own.

¹²²² *Castellain v. Preston* (1883) 11 QBD 380; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p503

excess or deductible clause is to be disregarded in ascertaining whether the insured has received an indemnity.¹²²³

(iii) The principle that the insured must receive a full indemnity before the insurer is entitled to any subrogation recovery is modified where the policy is subject to average clause.¹²²⁴ Therefore, the allocation of the sum received from the third party as between the insured and the insurer is based on pro rata apportionment according to their respective interests.¹²²⁵

(iv) In the case of valued policies,¹²²⁶ the insurer who has paid the insured the agreed value has priority with respect to the proceeds of an action against the third party for restitution of that sum.¹²²⁷

(v) The insurer is only entitled to recover up to the extent of his payment to the insured.¹²²⁸ Thus, if the sum recovered from the third party exceeds the amount paid by the insurer to the insured, the insured is entitled to keep the surplus, even if the surplus combined with the insurer's payment gives the insured more than an indemnity.¹²²⁹

The following particular cases will be discussed to illustrate the interrelationship between the above principles and to examine whether or not the English approach is consistent with the principle of indemnity.

4.2.2. The insured is fully compensated by the insurance indemnity

Where the insured is insured for his full loss, the insurer who has already paid the full indemnity is entitled to be recouped by having that amount back, although any amount in excess of the insurer's payment to the insured¹²³⁰ may be retained by the insured.¹²³¹ It is

¹²²³ *Napier v Hunter* (1993) A.C. 713; *England v Guardian Insurance Ltd* (2000) Lloyd's Rep.I.R. 404; the concept of indemnity under English insurance law refers to only parts of the insured's loss which is acknowledged by the policy because of a matter of general contractual interpretation.

¹²²⁴ under a policy of that nature the insurer and insured are deemed to be co-insurers where the policy does not cover the full amount of the insured's loss; see also Section 81 of MIA 1906; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p504

¹²²⁵ *The Commonwealth* (1907) P 216

¹²²⁶ The valuation agreed between the insurer and the insured is conclusive of the insurable value of the subject-matter insured; see also s.27(3) & 68(1) MIA 1906

¹²²⁷ *North of England Ins Assn v Armstrong* (1870) LR 5 QB 244; *Thames & Mersey Marine Insurance Co v British & Chilean Steamship Co* (1915) 2 K.B. 214; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p504; H Bennett, "The law of marine insurance", (2nd edn, Oxford University Press, 2006), p795

¹²²⁸ *Glen Line v Attorney General* (1930) 6 Com Cas 1; see also R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p505

¹²²⁹ *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330

¹²³⁰ *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330

¹²³¹ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p504

submitted that this rule is consistent with the principle of indemnity. The insurer cannot recoup more than what he has paid out under the insurance policy, and he cannot make profit from exercise of his subrogation rights.

In *Yorkshire Insurance Co v Nisbet Shipping Co*¹²³², an insured ship was lost in 1945 as the result of a collision with and caused by a Canadian naval vessel. The insurer paid its agreed value of £72,000. The insured, with the insurer's consent, brought an action against the Canadian government for damages and recovered the value of the vessel (£75,500). This sum was properly converted into Canadian dollars. Before the money was paid in 1958, however, the pound sterling was devalued, rendering the sum when paid worth £125,000. The insured accounted to the insurer for £72,000 but the latter claimed the balance. Diplock J held that the subrogation rights of the insurers extended only to the sums they had paid out.

The question of who can get the fruit from the proceedings against the third party has been critically analysed by Derham.¹²³³ Several arguments have been thoroughly discussed. A number of strong grounds for granting the fruit from the proceedings against the third party wrongdoer to the insured have been stated, as follows: (i) the insurer cannot recover more than he has paid to the insured by exercising his rights of subrogation; thus, he is limited to recovering the amount of his payment; (ii) there may be no strong ground for allowing the insurer to make profit out of subrogation. Subrogation merely provides a legal mechanism to prevent the insured from recovering a double indemnity through the aggregation of both insurance moneys and compensation from a third party wrongdoer.¹²³⁴ In no way can it transfer to the insurer the benefit of the third party action;¹²³⁵ (iii) in the action brought in the name of the insured, it is the insured who recovers judgment against the third party, and the judgment can be satisfied only by payment to him;¹²³⁶ (iv) the sum recovered from the third party could not change its character in the hands of the insured on conversion into sterling. The circumstance is the same as that of an English manufacturer, for example, who sells goods through a Canadian agent and receives the proceeds of the sale in dollars before

¹²³² (1962) 2 Q.B. 330

¹²³³ Derham, *Subrogation in Insurance Law*, (Law Book Company, 1985), p136-143

¹²³⁴ Brett LJ in *Castellain v Preston* (1883) 11 QBD 380, at 387

¹²³⁵ H Bennett, "The law of marine insurance", (2nd edn, Oxford University Press, 2006), p795; in this respect, subrogation is contrasted with assignment of the action to the insurer. Assignment transfers the benefits of the action to the insurer, entitling him to retain the full sum recovered from a third party, including any surplus over the amount paid by the insurer to the insured.

¹²³⁶ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p501

devaluation and remits them to England after devaluation: the English manufacturer would be entitled to claim the benefit.¹²³⁷

4.2.3. The insured is insured for his full loss, subject to an excess

Where there is an excess clause under the insurance policy, the question arises as to who should bear the loss under the excess clause if the payment from the third party is insufficient to meet the insured's total loss. This situation was analysed in the case of *Napier v Hunter*. In this case, the House of Lord gave a simple set of figures for the purposes of argument and decision. The loss suffered by the insured was £160,000. The limit of the insurers' liability, that is the sum insured, was £125,000, and there was an excess of £25,000. The sum recovered from the third party responsible for the loss was £130,000. The insurers paid the insured £100,000, namely the sum insured less the excess.¹²³⁸ In this situation, Lord Templeman determined that the order of the distribution could be dealt with by looking at the matter as if there were three insurance layers: the first up to £25,000 to be borne by the insured under the excess; the next £100,000 (between £25,000 and £125,000) agreed to be borne by the insurers; and the last £35,000 (above £125,000) to be borne by the insured as a sum above the policy limit.

A "recover down" principle was applied; the upper insurer could expect to run a lesser risk and he had priority to subrogation money recoverable from the third party because he only agreed to pay if the other insurers did not cover the loss. In this case, the insured was entitled to the first £35,000 of the £130,000 sum recovered from the third party; the insurers would then be entitled to the rest (£95,000). The insured had to bear the loss under the excess because there was insufficient money to be recovered by the insured under the excess. Therefore, the ultimate loss was £30,000, namely the initial loss of £160,000 less the recovery of £130,000. The relevant policy term was the excess clause of £25,000 and so the insured recovered from the insurer only £5,000.¹²³⁹

The decision in *Napier's* case is not without its critics. Perhaps there is insufficient justification for granting the insurer initial right to claim over the insured's loss under the excess clause. This is so for three reasons. First, the issue of assumption of risk should be

¹²³⁷ *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330, p334

¹²³⁸ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p327

¹²³⁹ J Birds, "Insurance: subrogation in the House of Lords", (1993) J.B.L 294, p298; see also M Hemsworth, "Subrogation: the problem of competing claims to recovery monies", (1998) J.B.L 111, p113

taken into account where there is an excess clause in an insurance policy.¹²⁴⁰ The reasoning of Lord Templeman was based on the assumption that the insured had agreed to bear the loss covered by the excess and the loss in excess of the limit of the insurer's liability. He argued that "an insured is not entitled to be indemnified against a loss which he has agreed to bear".¹²⁴¹ It is not evident why this should preclude the insured from appropriating from the third party to the uninsured loss before becoming liable to account to the insurer.

Regarding the insurance contract between the parties, the insured promises to bear the first layer of the risk under an excess clause and the insurer promises indemnity only in respect of loss greater than the excess. As a matter of contract, where the insured suffers the loss which is less than the amount of the excess, the insurer is not obliged to pay. This is so if there is no third party involved.¹²⁴² In respect of distribution of the subrogation sum recovered from a third party wrongdoer, there is no clear assumption that where the insured agrees to be his own insurer in respect of the excess, he should be the last person who has right to claim from the recovery money in the "recover down" principle. It seems unfair to infer from the fact that the insured agrees to bear the risk under the excess clause means that he must be at the last layer.

Second, Lord Templeman's assumption about three insurance policies is suspect. It is not clear that the issue of competing interests between the insured and the insurer is the same as that of allocation of recoveries between insurers.¹²⁴³ The relevant consideration and principles to be applied in the two scenarios are not necessarily identical.¹²⁴⁴ The former is based on the principle of indemnity, whereas the latter depends on allocation of risks between insurers.

Third, the indemnity principle does not prevent the insured from attaining full compensation for his total loss; it merely prevents retention of any further profit.¹²⁴⁵ The authority resulting from the case of *Napier* emphasizes the fact that, in the context of recoveries, subrogation is concerned only with the insured loss rather than any general loss. Consequently, where the insured has suffered an insured loss and an uninsured loss, full indemnification of the former

¹²⁴⁰ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1029

¹²⁴¹ Lord Templeman in *Napier v Hunter* (1993) A.C. 713, p731

¹²⁴² See also section 4.1.3 of this Chapter

¹²⁴³ F Rose, *Marine Insurance: Law and Practice*, (LLP, London, 2004), p562

¹²⁴⁴ Harris, "Insurance subrogation", (1993) 22 Can. Bus. L.J 308, p316

¹²⁴⁵ Derham, *Subrogation in Insurance Law*, (Law Book Company, 1985), p133-134. To support his arguments, Derham discussed cases which are in favour of full compensation approach, namely: *Castellain v. Preston*, *Driscoll v Driscoll*, and *National Fire Insurance Co v McLaren*; M Luey, "Proprietary remedies in insurance subrogation", (1995) 25 Victoria.U.Wellington.L.Rev. 449, p457

subrogates the insurers, irrespective of the fact that the insured has not yet recovered the uninsured loss.¹²⁴⁶ It is illogical because there is no double recovery or unjust enrichment to be prevented where the insured is not fully compensated for his actual loss.

Moreover, there is an authority which expresses the view that, where the insured's loss includes damage which is not covered by the policy, the insurer is not entitled to be subrogated to any payment or liability in respect of the uninsured loss.¹²⁴⁷ It is suggested that the rules on allocation of subrogation recovery should be interpreted in order to ensure that the insured obtains a full compensation rather than protecting insurers who have received valuable consideration in return for assuming risk as his business.

4.2.4. The insured is not fully insured under an unvalued policy.

Where the insured is not fully insured under an unvalued policy, the insured is entitled to retain such amount of the subrogation recovery as is necessary to cover the uninsured loss before accounting for the balance to the insurer.¹²⁴⁸

The leading case of *Hobbs v Marlowe*¹²⁴⁹ illustrates this principle. In this case, the plaintiff's car was damaged in a collision caused by the negligence of the defendant. The cost of repairs was £237.59. The plaintiff hired another car for the duration of the repairs. This cost £63.53. His insurers paid him £227.59 under his policy for the repair costs, because there was an excess of £10. The hiring costs were not covered by the policy. To recover his shortfall of £73.53, he brought an action against the third party for his total loss of £301.12. His insurers had no interest in the proceedings, since they had a "knock-for-knock" agreement with the defendant's insurer. The House of Lords held that the plaintiff had the right to sue for the full amount of his damages and was entitled to retain £73.53 out-of-pocket expenses.

Therefore, if the insured's loss includes damage which is not covered by the policy, the insurer is not entitled to be subrogated to any payment or liability in respect of the uninsured loss.¹²⁵⁰ Similarly, if the insured has a right of action against the third party for an

¹²⁴⁶ Lord Jauncey in *Napier v Hunter* (1993) A.C. 713, p747

¹²⁴⁷ *Law Fire Assurance Co v Oakley* (1888) 4 T.L.R. 309

¹²⁴⁸ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p504

¹²⁴⁹ (1978) A.C. 16.

¹²⁵⁰ *Law Fire Assurance Co v Oakley* (1888) 4 T.L.R. 309.

independent form of loss additional to the insured loss, any sum received from the third party in discharge of that liability cannot be claimed by the insurer.¹²⁵¹

It is submitted that this rule is consistent with the principle of indemnity. The insured should be given priority to the third party's payment until full compensation is achieved. Any sum in excess of the insured's full compensation should be recouped by the insurer.

4.2.5. The insured, under a valued policy not subject to average, is insured to the full agreed value of the subject matter, although its agreed value is less than its actual value

Where the actual value is greater than the agreed value, the insured may allege that he should have a first claim to the subrogation recovery¹²⁵² or that the subrogation recovery should be divided between the insured and the insurer in proportion to their respective losses.¹²⁵³ It is submitted that this allegation should be dismissed because the agreed value is binding on the insurer as well as the insured, so that the insurer is also precluded from alleging that the agreed value is greater than the actual value. It should be emphasised that the primary purpose of fixing an agreed value on a valued policy is to avoid any dispute over the value of the subject matter insured.¹²⁵⁴ The agreed value removes any need to prove the true market value of the insured subject matter.¹²⁵⁵ Moreover, it is difficult for the insured, in practice, to prove that the actual value is greater than the agreed value, and it is easier for the insurer to prove the contrary.

Furthermore, a valued policy is a contract of conventional rather than true indemnity. The parties are free to conclusively agree that a certain sum is payable in the event of loss.¹²⁵⁶ The measure of indemnity for a total loss is a sum equal to the policy valuation. This sum is conclusive evidence of the insurable value of the subject matter insured. Consequently, the insured who has received this sum from the insurer cannot dispute that he has not been fully indemnified for his total loss. This means that the insurer who has met his full obligation

¹²⁵¹ *Young v Merchants' Marine Insurance Co Ltd* (1932) 2 K.B. 705

¹²⁵² R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p504

¹²⁵³ In *Goole & Hull Steam Towing Co Ltd v Ocean Marine Ins Co Ltd* (1928) 1 KB 589, at p594, it was alleged that the £2,500 recovered from the third party wrongdoer should be apportioned 4:1 between insurer and insured as regards the £5,000 loss – cost of repairing the vessel with an agreed value of £4,000.

¹²⁵⁴ The insurer cannot contest the valuation for any reason unless the insured has been guilty of fraud in presenting the valuation or has over-valued the subject matter in a material fashion or has failed to disclose or has misrepresented the valuation (see *The Grecia Express* (2002) EWHC 203, *Lewis v Rucker* (1761) 2 Burr 1167; *General Shipping & Forwarding Co v British General Ins Co* (1923) 15 Ll.L.R 175; *Balmoral Steamship Co v Marten* (1902) AC 511; *Haigh v de la Cour* (1812) 3 Camp 319)

¹²⁵⁵ *Lidgett v Secretan* (No2) (1871) LR 6 CP 616, p627

¹²⁵⁶ H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p802

under a valued policy has a first claim to the sum recovered from the third party wrongdoer.¹²⁵⁷

The leading case in this respect is *North of England Ins Assn v Armstrong*.¹²⁵⁸ It was held that the insurer was entitled to recoup the full amount of recovery from the owners of another ship involved in a collision, despite the fact that the real value of the insured vessel was greater than the policy valuation. However, this case has been criticised for confusion between the concepts of abandonment and subrogation as it implied that the insurer may recover in excess of his payment under the policy.¹²⁵⁹ Cockburn C.J in this case thought that if a ship is insured for the full amount of its valuation but the policy valuation is less than its actual value, and damages are recovered to the extent of this actual value, then the insurer would be entitled to the full amount of these damages, even though they exceed the amount of his own payment under the policy. This is certainly wrong. The insurer cannot claim more than what he actually paid to the insured, and he cannot get profit from subrogation proceeds. Derham submitted that little weight should be attached to this case as an authority.¹²⁶⁰

This decision was followed in *Thames & Mersey Marine Insurance Co v British & Chilean Steamship Co*,¹²⁶¹ a vessel with an agreed value of £45,000 was insured for that sum and was sunk as a result of a collision. The insurer paid for that sum. The true value of the vessel was £65,000. Both vessels being to blame for the collision, the insured recovered as damages equivalent to five-twelfths of the real value of the vessel. It was held that the insurer was entitled to the entire sum recovered.

Similarly, the agreed valuation is conclusive evidence of the insurable value of the subject-matter insured in the event of a partial loss.¹²⁶² It was held that the insurer was entitled to claim the whole amount recovered from the third party wrongdoer, despite the fact that the insured's actual loss was greater than the policy valuation. The reason for this is that the

¹²⁵⁷ H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p802

¹²⁵⁸ (1870) LR 5 QB 244

¹²⁵⁹ A distinction between abandonment and subrogation was made clearly by Lord Blackburn several years later in *Simpson v Thomson* (1887) 3 App. Cas. 279, at p292.

¹²⁶⁰ SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p136

¹²⁶¹ (1915) 2 K.B. 214

¹²⁶² H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p802

insurer was only liable for the difference between the amount valued in the policy and the amount recovered by the insured from the third party.¹²⁶³

Another issue which should be discussed is the situation where the amount recovered in a third party action exceeds the agreed value. The conclusiveness of the agreed value applies only as between the insurer and the insured, not between the insured and the third party wrongdoer. It is the market value that determines loss as between the insured and the third party wrongdoer.¹²⁶⁴ The question arises as to whether the insured or the insurer was entitled to any surplus recovery, once the insurer's priority to the extent of his liability under the valued policy has been satisfied.¹²⁶⁵

The principle that the insurer is only entitled to recover up to the extent of his payment to the insured applies in this situation. The reason is that the action against the third party is actually the insured's action which must give the insured any surplus and that, once the insurer has recouped in full the indemnity paid to the insured, there is no unjust enrichment by double payment to the insured.¹²⁶⁶ Consequently, where the insurer has recouped in full his payment, the insured is entitled to any surplus recovery from the third party. For example, a property is fully insured for an amount of £8,000, but the actual value of the property is £10,000. The property is completely destroyed due to a third party's negligence. If the full amount of £10,000 is recovered from the third party, the insured is entitled to retain £2,000 for his own benefit. If the recovery sum is £9,000, the insurer should be entitled to £8,000 and the insured to £1,000.

¹²⁶³ *Goole & Hull Steam Towing Co Ltd v Ocean Marine Ins Co Ltd* (1928) 1 KB 589. In this case, a vessel with an agreed value of £4,000 was insured and was damaged because of a collision. The cost of repair was £5,000. The insured recovered £2,500 from the owners of the other ship on a both to blame basis. The insured claimed to the insurer for the remaining £2,500. The court upheld the insurer's intention that his liability was limited to £1,500, being the difference between the sum recovered and the amount of maximum liability on the valued policy.

¹²⁶⁴ *Thames & Mersey Marine Insurance Co v British & Chilean Steamship Co* (1915) 2 K.B. 214; see also H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p803

¹²⁶⁵ In *North of England Ins Assn v Armstrong* (1870) LR 5 QB 244, it was argued that surplus recovery should belong to the insurer on the basis that the insurer had indemnified in full the agreed value of the subject matter insured, he would be entitled to all that can be recovered in respect of the loss of the subject matter insured. This case is criticised because of confusion between the concepts of subrogation and abandonment; see also *Thames & Mersey Marine Insurance Co v British & Chilean Steamship Co* (1915) 2 K.B. 214; *Goole & Hull Steam Towing Co Ltd v Ocean Marine Ins Co Ltd* (1928) 1 KB 589

¹²⁶⁶ *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330

4.2.6. The insured under a valued policy subject to average clause is not fully insured, in which the insured sum is less than the agreed value and the actual value of the insured subject matter

Where the policy is a valued policy subject to average clause, and the subject matter is not insured for its full amount of the policy valuation, any sum recovered from the third party wrongdoer should be apportioned between the insurer and the insured in proportion to their respective interests. The reason is that there is an expressed average clause in the agreement between the parties. The average clause has an effect on allocation of subrogation recovery from the third party wrongdoer.

For example, the insured is insured for £8,000 under a valued policy subject to average, where the agreed value and the actual value of the insured subject matter are £10,000. In this example, the insured is under-insured and the policy is subject to average clause. According to the principle of average, the insured is his own insurer for the sum of £2,000, he shall bear one-fifths of the risk himself.¹²⁶⁷ For a total loss, he can only recover from the insurer £8,000. For a partial loss of £5,000, he can claim for £4,000.

The principle of average also has an effect on allocation of recovery money. Thus, the average principle requires the insured and the insurer to apportion any sum recovered from the third party wrongdoer in the proportion to their respective interests (2:8).¹²⁶⁸ This is held in *The Commonwealth* (1907)¹²⁶⁹. Sir Gorell Barnes stated that: “when the underwriter pays the assured he is subrogated to his rights having regard to the risk he has taken- that is to say, in the present case, when the assured’s name is used for the purpose of enforcing an action against the wrongdoer, the remedy is sought for the underwriter to the extent to which he had insured, and for the assured to the extent to which he had left himself uninsured. That being so, it seems logically to follow that when the money which is recovered is in hand it ought to be divided in proportion to their respective interests.”¹²⁷⁰

The principle of average is implied in marine policies by virtue of s.81 of MIA 1906.¹²⁷¹ Section 81 of MIA provides that, where an insured is insured for an amount less than the

¹²⁶⁷ In case of marine insurance, average principle is implied by virtue of s81 of MIA 1906

¹²⁶⁸ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p505; see also S Hodges, *Law of Marine Insurance*, (Cavendish Publishing Limited, London, 2005), p14

¹²⁶⁹ (1907) P216

¹²⁷⁰ *Ibid*, p223

¹²⁷¹ *The Commonwealth* (1907) P 216 CA

agreed value in a valued policy, or for an amount less than the insurable value in an unvalued policy, 'he is deemed to be his own insurer in respect of the uninsured balance'.¹²⁷² This implication is applied broadly not only to the allocation of recovery but also to the adjustment of losses and expenses, and to cases of partial insurance in relation to particular average losses and sue and labour expenses. Any third party recovery is allocated between the insurer and the insured in proportion to their respective interests in the subject matter.

However, it is submitted that this implication in respect of allocation of subrogation recovery from a third party wrongdoer should be excluded unless the policy contains an express average clause. In fact, this implication does not operate in non-marine insurance unless the policy contains an express average clause. The parties to an insurance contract are free to contract which terms or conditions should be applied in their contract, such as an average clause.

In the non-marine case of *Kuwait Airways Corp v Kuwait Insurance*,¹²⁷³ fifteen aircraft belonging to the insured were removed from Kuwait airport by invading Iraqi forces. The insurer's liability was limited to USD300 million, which they duly paid, leaving the insured underinsured by USD 392 million. Subsequently, the insured had recovered a number of the planes. The question arises as to whether the value of recovery should be allocated to insured until fully indemnified or whether the recovery should be divided between the insurer and the insured in proportion to the sums insured and uninsured. Rix J considered that it was proper to adopt the 'top down' approach in the *Napier* rather than the proportionate sharing approach which was adopted in cases of underinsurance in marine insurance cases. He considered the top down principle as 'the principle which most closely conforms to the underlying rationale of subrogation',¹²⁷⁴ assuming that the rationale is the avoidance of unjust enrichment. Therefore, he held that the insured should have priority with respect to recoveries until full compensation had been achieved.

It is implied that Rix J clearly favoured the approach that supports full compensation for the insured. In doing so, he relied on the top-down principle in the *Napier*, although it is not quite

¹²⁷² S.81 of MIA 1906: "Effect of under insurance: Where the assured is insured for an amount less than the insurable value or, in the case of a valued policy, for an amount less than the policy valuation, he is deemed to be his own insurer in respect of the uninsured balance."

¹²⁷³ (1996) Lloyd's Rep 664

¹²⁷⁴ *Ibid* at p695

clear that the top down approach would apply to under-insurance or partial insurance.¹²⁷⁵ In this way, the ‘top down’ principle would support priority to the insured in cases of under-insurance until full compensation is achieved.

It is submitted that Rix J’s approach is fair, and consistent with the principle of indemnity. Where there is no expressed average clause in the insurance policy, the principle of average should not be implied in respect of allocation of the subrogation recovery from the third party. The parties to the insurance contract have freedom of contract. Thus, the insurer should expressly incorporate the average clause into the policy if he wishes to share with the insured any recovery sum from the third party.

Further complication may occur where the sum, which the insurer could recoup in accordance with the principle of average, is in excess of his payment under the policy. The question arises as to whether the insurer can get more than what he has paid under the policy. He may argue that the expressed average clause in the agreement is absolutely binding on the parties. For example, the insured is insured for £5,000 under a valued policy subject to average; the agreed value of the subject matter insured is £8,000, but its actual value is £10,000. The subrogation sum of £9,000 has been recovered from the third party. The average position requires the insured must share with the insurer in the proportion (5:3) to the amount recovered from the third party, as £8,000 is the conclusive evidence of the insurable value of the subject matter. That calculation produces a recovery by the insurer of £5,625. However, as there is a general rule that the insurer cannot recover more than his own payment of £5,000, the insured would receive £4,000 of the recovery. If the subrogation recovery had been just £6,000, the insurer and the insured, on the basis of the (5:3) proportion demanded by average, would have recovered £3,750 and £2,250 respectively.¹²⁷⁶ It is submitted that this rule is fair, and consistent with the principle of indemnity. The insurer cannot make profit from the subrogation proceedings, and the policy valuation is the conclusive evidence of the insurable value of the subject matter insured. On the other hand, the insured is also prevented from disputing that the actual value of the subject matter insured is greater than the policy valuation.

¹²⁷⁵ Arnould notes that it is difficult to see how the ‘top down’ principle, and the reasoning that led to it, can be applied to partial insurance. Bennet suspects about this application by distinguishing the facts of the *Napier* and *Kuwait Airways Corp*; the former was concerned with a policy that expressly created three vertical layers of risk, whereas the latter related with insured and uninsured risk rank equally and horizontally. However, Birds states that top down approach would apply to a case of under insurance.

¹²⁷⁶ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p505

4.2.7. The insured under a valued policy not subject to average clause is not fully insured, when the insured sum is less than the agreed value and the actual value of the insured subject matter

Where the policy is a valued policy not subject to average clause, and the subject matter is not insured for its full amount of the policy valuation, there is no presumption that the insured is his own insurer for the underinsured balance. The insurer's maximum liability is the sum insured. For example, the insured is insured for £8,000 under a valued policy not subject to average clause, on a subject matter of an agreed and actual value of £10,000. If the insured suffers a total loss of £10,000, he is only entitled to recover £8,000 from the insurer.¹²⁷⁷

However, where the subrogation sum from the third party is available, it is suggested that the insured can retain whatever he recovers from third party until he has received a full compensation and need only hand over the balance to the insurer.¹²⁷⁸ For instance, if the insured suffers a total loss and the sum recovered from the third party is only £7,000, it would seem that the insured may retain £2,000 in order to make up the full indemnity, leaving the balance of £5,000 for the insurer.

In the situation where there is no express average clause in the policy, but there is an express agreement between the parties that the insured is underinsured, the principle that the insured is initially entitled to claim for the amount equal to the difference between the valuation and the sum insured applies.¹²⁷⁹ The insured should be fully compensated before the insurer may recover anything from the third party wrongdoer. The reason for this is that the insurer assumed the risk of loss by accepting the insured's premiums, and the insurer's payment under the policy is not prima facie fully compensated for the insured's entire loss. Consequently, there is nothing to estoppel the insured from disputing that he is not fully compensated by the insurer's payment and that he should be given first priority over any money recovered from a third party wrongdoer.¹²⁸⁰

¹²⁷⁷ John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p721

¹²⁷⁸ *Kuwait Airways Corp v Kuwait Insurance SAK (No1)* (1996) Lloyd's Rep 664. In this case, Rix J held that the insured should have priority with respect to recoveries until full indemnification have been achieved; see also John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p721

¹²⁷⁹ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p505; see also SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p134

¹²⁸⁰ *Sea Ins Co v Hadden* [1884] 13 Q.B.D. 706; *Law Fire Assurance Co v Oakley* (1888) 4 T.L.R. 309; SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p134

There are a number of authorities which support this view. In the marine insurance case of *Sea Insurance co v Hadden*,¹²⁸¹ which was concerned with under insurance, it was held that the recovery sum should go first in favour of the insured in respect of his losses not covered by the policy.¹²⁸² It was held in *Law Fire Assurance Co v Oakley*¹²⁸³ that if the insured's loss includes damage which is not covered by the policy, the insurer is not entitled to be subrogated to any payment or liability in respect of the uninsured loss.

4.3. Comparison between the English approach and the Vietnamese approach, and recommendations for amendment to Vietnamese insurance laws:

After having critically analysed the Vietnamese approach and the English approach to the issue of distribution of subrogation recovery from the third party, four important points can be concluded.

First, a general view on comparison of the two approaches is that English rules are comprehensive, complicated and detailed; however, those rules are not always consistent with the principle of indemnity. There are several problems under Vietnamese insurance laws, such as confusion between the principle of subrogation and the principle of assignment. The insurer is commonly given priority to the third party's payment, regardless of the fact that the insured is not fully compensated for his total loss. The insurer's interests are excessively protected by Vietnamese insurance laws, whereas the insured's interests do not receive an appropriate amount of attention.

Although English laws are not completely consistent with the principle of indemnity, the English approach can be a good model in respect of reforming Vietnamese insurance laws. Under English laws, the insured has a greater chance of achieving full compensation for his total loss. For example, the fruit of proceedings against the third party wrongdoer is given to the insured.¹²⁸⁴ Under an unvalued policy, the insured has a first claim to the third party's payment.¹²⁸⁵ Under a valued policy, not subject to average clause, where there is an express agreement between the insured and the insurer that the subject matter is not fully insured, the

¹²⁸¹ (1884) 13 Q.B.D 706; see also *Glen Line v Attorney General* (1930) 6 Com Cas 1

¹²⁸² M Hemsworth, "Subrogation: the problem of competing claims to recovery monies", (1998) J.B.L 111, p114

¹²⁸³ (1888) 4 T.L.R. 309

¹²⁸⁴ *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330

¹²⁸⁵ *Hobbs v Marlowe* (1978) A.C. 16

subrogation recovery from the third party wrongdoer may go first to the insured.¹²⁸⁶ A few changes could bring English insurance laws into compliance with the principle of indemnity.

It is suggested that this direction could be followed to reform Vietnamese insurance laws. It is believed that the new rules on distribution of subrogation recovery from the third party under Vietnamese insurance laws are effective in solving the problems relating to competition between the insured and the insurer in their claims to the third party's payment. The new rules would remove the confusion between the doctrine of subrogation and the doctrine of assignment under Vietnamese insurance laws, and also eliminate unnecessary legal proceedings against the third party wrongdoer. The insured would be entitled to receive full compensation for his total loss, but no more than full compensation. This is consistent with the principle of indemnity.

Second, it suggested that allocation of recovery money under a valued policy is an exception to the principle of indemnity. A valued policy is a contract of conventional rather than true indemnity. In *Irving v Manning*,¹²⁸⁷ it was held that “a policy of insurance is not a perfect contract of indemnity. It must be taken with this qualification that the parties may agree before-hand in estimating the value of the subject assured by way of liquidated damages.”¹²⁸⁸ The parties are free to conclusively agree that a certain sum is payable in the event of loss.¹²⁸⁹ The measure of indemnity for a total loss is a sum equal to the policy valuation. This sum is conclusive evidence of the insurable value of the subject matter insured. The policy valuation is binding on both the insurer and the insured. The parties should not be allowed to dispute that the actual value of the subject matter insured is greater or less than the agreed value. The reason for this submission is that the primary purpose of fixing an agreed value on a valued policy is to avoid any dispute over the value of the subject matter insured.¹²⁹⁰ The agreed value removes any need to prove the true market value of the insured subject matter.

¹²⁸⁶ *Sea Ins Co v Hadden* (1884) 13 Q.B.D. 706

¹²⁸⁷ [1847] 1 HLC 287

¹²⁸⁸ *Ibid*, p307

¹²⁸⁹ H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p802

¹²⁹⁰ The insurer cannot contest the valuation for any reason unless the insured has been guilty of fraud in presenting the valuation or has over-valued the subject matter in a material fashion or has failed to disclose or has misrepresented the valuation (see *The Grecia Express* (2002) EWHC 203, *Lewis v Rucker* (1761) 2 Burr 1167; *General Shipping & Forwarding Co v British General Ins Co* (1923) 15 Ll.L.R 175; *Balmoral Steamship Co v Marten* (1902) AC 511; *Haigh v de la Cour* (1812) 3 Camp 319)

Where the subject matter is insured for its full agreed value, it is submitted that the insurer will have a first claim to the extent of his payment under the policy, even if the value of the property destroyed is greater than the valuation in the policy; and the insured is then entitled to the remainder in order to achieve full compensation.

However, if there are other losses rather than the loss of the subject matter insured, the recovery sum should go first to that uninsured loss, leaving the balance to the insurer. For example, a truck is insured for its full agreed value, and on the occurrence of the peril, the truck and the goods on the car are damaged due to negligence of a third party wrongdoer. The insured should be entitled to have a first claim to the subrogation recovery in respect of the uninsured loss of the goods.

Where the policy is a valued policy not subject to an average clause and the parties expressly stipulate that the sum insured is less than the policy valuation, the insured should have a first claim to the third party's payment for the difference between the sum insured and the valuation. The reason for this submission is that there is no presumption that the insured is his own insurer for the under-insured balance. The underlying rationale behind the principle of indemnity is that the insured should be fully compensated for his total loss.

Third, there is difference between the English law and the Vietnamese law as to how to interpret an express agreement on allocation of subrogation recoveries. In Vietnamese commercial practice, on payment of the insured loss, the insured commonly provides the insurer with a receipt and subrogation form. This form is considered by Vietnamese courts as an express agreement between the parties in respect of transfer of subrogation rights from the insured to the insurer. However, it is submitted that the terms and conditions in this form should be interpreted narrowly as generally stating the law, because this form is issued at the time when the insured follows the procedure for making a claim against the insurer. In order to receive insurance benefits, the insured may agree to some terms and conditions which are not in his favour.

Under English law, it is recognised that the subrogation principle is mainly governed by equitable principles and its application can be modified, excluded or extended by contract.¹²⁹¹

¹²⁹¹ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p324; see also: J Birds, "Contractual Subrogation in Insurance", [1979] J.B.L. 124; A Brown, "An insurer's rights in litigation or contractual subrogation: an oxymoron?", (1996) 8 Ins.L.J. 60; R Hodgkin, "Subrogation in insurance law", (1975) J.B.L 114

In *Banque Financière de la Cité v Parc (Battersea) Ltd and others*,¹²⁹² Lord Hoffmann stated that: “although in *Lord Napier and Ettrick v Hunter*, *Lord Napier and Ettrick v R F Kershaw Ltd* [1993] 1 All ER 385, [1993] AC 713 your Lordships rejected the exclusivity of this claim for the common law and assigned a larger role to equitable principles, there was no dispute that the doctrine of subrogation in insurance rests upon the common intention of the parties and gives effect to the principle of indemnity embodied in the contract.”¹²⁹³

It is submitted that the parties are free to contract as to distribution of subrogation recovery but cannot, however, reverse the general equitable rules of the subrogation principle. Any terms and conditions relating to distribution of subrogation recovery should be negotiated and agreed at the time of entering into the insurance contract. Any express agreement conflicted with the general equitable rules of the subrogation principle should be void.

This submission is compatible with the English approach to contractual subrogation in insurance. In English commercial practice, it is common that the principle of subrogation may be modified or extended by express provisions in standard form contracts.¹²⁹⁴ Obviously, the exact terms of such provisions may vary from policy to policy and from insurer to insurer, some of which restate the rules of law.¹²⁹⁵

It is suggested that the general equitable rules of the subrogation principle should not be modified or excluded by an express term.¹²⁹⁶ Those rules are: (i) the insurer should not recover more than his payment, (ii) full compensation is a condition precedent to the insurer’s exercise of subrogation rights, and (iii) the insurer must act in good faith and with due regard to the interests of the insured when the insurer brings an action against the third party wrongdoer.

In *Lucas Ltd v. Export Credits Guarantee*,¹²⁹⁷ the House of Lords rejected the insurer’s claim to an amount which was greater than his payment, even though clause 17 of the guarantee

¹²⁹² (1998) 1 All.E.R 737

¹²⁹³ *Ibid*, p744

¹²⁹⁴ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p339; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1024; S Kimball & D Davis, “The extension of insurance subrogation”, (1962) 60 Mich.L.Rev. 841, 860; G Veal, “Subrogation: The duties and obligations of the insured and rights of the insurer revisited”, (1992) 28 Tort & Ins.L.J 69, 74; A Brown, “An insurer’s rights in litigation or contractual subrogation: an oxymoron?”, (1996) 8 Ins.L.J. 60

¹²⁹⁵ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p339

¹²⁹⁶ *Banque Financière de la Cité v Parc (Battersea) Ltd and others* (1998) 1 All.E.R 737; SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), pp 114-151; R Hodgkin, “Subrogation in insurance law”, (1975) J.B.L 114; J Birds, “Contractual Subrogation in Insurance”, [1979] J.B.L. 124, p131

¹²⁹⁷ [1974] 1 W.L.R. 909.

between the parties stated: “any sums recovered by the merchant or the guarantors in respect of a loss to which this guarantee applies, after the date at which the loss is ascertained, whether from the buyer or any other source shall ... be divided between the guarantors and the merchant in the proportions of 90 and 10...” The decision of the House of Lords implied that the express terms were taken into account before the general principles of subrogation. However, where the interpretation of such a term represents conflicts of opinion, the general principles of subrogation in insurance were looked upon for guidance.¹²⁹⁸ In this case, one such general principle was that the insurer should not recover more than he paid out.¹²⁹⁹

Express terms commonly entitle the insurers to take proceedings before or after indemnifying the insured, and may well entitle them to control or take over the proceedings.¹³⁰⁰ However, under the general principles of subrogation, full indemnity is a condition precedent to an action for the use of the insured’s name¹³⁰¹ and, even if the insured has been fully indemnified, he is perfectly entitled to proceed against the wrongdoer provided that he pays proper regard to the insurer’s interest.¹³⁰²

Express terms may well permit the insurers to take control and thus abandon such an action. It is suggested that this should only be permissible if the insurers act in good faith and with due regard to the interests of the insured.¹³⁰³ If the insurer’s abandonment of taking an action against the third party results in impossibility of recovery of the uninsured loss suffered by the insured, the insured should be enabled to seek compensation.¹³⁰⁴

Express terms may change priority between the insured and the insurer regarding the third party’s payment.¹³⁰⁵ In *Oss v United Services Automobile Association*,¹³⁰⁶ the insurer attempted by the subrogation clause in its policy to reverse the priority of rights between insured and insurer to any recovery from a third party. The Fifth Circuit Court of Appeal rejected that attempt on the ground of equitable subrogation: that the equitable principles may restrict the insurer’s rights of subrogation taken by contractual subrogation. In another

¹²⁹⁸ R Hodgkin, “Subrogation in insurance law”, (1975) J.B.L 114, p115

¹²⁹⁹ *Burnard v Rodocanachi* (1882) 7 App Cas 333

¹³⁰⁰ J Birds, “Contractual Subrogation in Insurance”, [1979] J.B.L. 124, p127

¹³⁰¹ M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1028

¹³⁰² *Hobbs v Marlowe* (1978) A.C. 16; *Bovis Construction Ltd v Eagle Star Insurance Co Ltd* (2002) Lloyd’s Rep.I.R. 321; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p501

¹³⁰³ J Birds, “Contractual Subrogation in Insurance”, [1979] J.B.L. 124, p136

¹³⁰⁴ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p339

¹³⁰⁵ G Veal, “Subrogation: The duties and obligations of the insured and rights of the insurer revisited”, (1992) 28 Tort & Ins.L.J 69, p74

¹³⁰⁶ (1987) 807 F.2d. 457

American case of *Powell v Blue Cross and Blue Shield of Alabama*,¹³⁰⁷ the Alabama Supreme Court, on the same ground, denied any subrogation recovery by the insurer because the insured had not been fully compensated, despite the express and very clear language. It was held that any subrogation provision in an insurance policy is void unless the insured has been fully compensated.¹³⁰⁸

However, there is an opposite view on this issue. It is argued that the parties are free to allocate priority by express agreement in the contract.¹³⁰⁹ It is submitted that the insurer and the insured are free to contract as to changing priority to the third party's subrogation recovery at the time of entering into the insurance contract. However, where this change is made by express terms of the subrogation and receipt form at the time when the insured makes his claim against the insurer in accordance with the insurance policy, these express terms should be declared void. The reason for this argument is that the insured is put in a weaker position when following the procedure for making a claim against the insurer, and it is unconscionable conduct if the insurer makes the change in the priority to the third party's payment at the time he makes payment rather than at the time of entering into the insurance contract.

Fourth, by critically examining Vietnamese rules on distribution of subrogation recovery from the third party wrongdoer in comparison to English rules, it is revealed that a fundamental problem under Vietnamese insurance laws is the confusion between the subrogation principle and the assignment principle. The provisions relating to subrogation under Vietnamese insurance laws are a mixture of subrogation principle and assignment principle. Subrogation under Vietnamese insurance laws is considered as the assignment of an obligatory right from the insured to the insurer. The insured who has been indemnified by the insurer in accordance with the insurance policy must transfer his rights or remedies against the third party wrongdoer to the insurer. The insurer is allowed to bring action against the third party wrongdoer in his own name to recoup his payment to the insured. The insured must take the other proceeding against the third party wrongdoer for his uninsured loss. This means that the insurer and the insured have separate rights to sue the third party wrongdoer in their own interests.

¹³⁰⁷ (1990) 581 So.2d 772

¹³⁰⁸ Ingram, "Priority between insurer and insured in subrogation recoveries", (1996-1997) 3 Conn.Ins.L.J. 106, p114; J Parker, "The made whole doctrine: Unraveling the enigma wrapped in the mystery of insurance subrogation", (2005) 70 Mo.L.Rev 723, p749

¹³⁰⁹ H Bennett, *The Law of Marine Insurance*, (2nd edn, Oxford University Press, 2006), p797

Misunderstanding of the nature of the principle of subrogation and confusion between the subrogation principle and the assignment principle cause several problems relating to judicial and commercial practices. Moreover, this confusion makes it difficult for the insured to achieve full compensation for his total loss. This is not consistent with the principle of indemnity.

5. CONFUSION BETWEEN THE PRINCIPLE OF SUBROGATION AND THE PRINCIPLE OF ASSIGNMENT UNDER VIETNAMESE INSURANCE LAWS

In English laws of insurance, it has been long established that the proceedings to recover the money from the third party wrongdoer conducted by the insurer must be brought in the name of the insured and that the insurer is not permitted to bring an action in his own name.¹³¹⁰ However, under Vietnamese insurance laws, the insurer and the insured have separate rights to bring proceedings against the third party wrongdoer. The insurer has the right to make a claim against the third party for an amount that the insurer has paid to the insured, and the insured is entitled to claim for his uninsured loss. The insurer can use his own name to sue the third party. The provisions relating to subrogation in Vietnamese laws are not compatible with the nature of the subrogation principle and the general rules of subrogation. There is confusion between the doctrine of subrogation and the doctrine of assignment under Vietnamese insurance laws. Subrogation is not assignment. Although there are similarities between them, they are different doctrines and each doctrine has its own rules.¹³¹¹

This confusion creates several problems in judicial and commercial practice. The third party wrongdoer can be taken to court twice due to the same cause of action. It costs the parties involved in a subrogation dispute considerable time and money. It also causes enormous difficulties for the insured in achieving full compensation.

¹³¹⁰ *Yates v Whyte* (1838) 4 Bing.N.C. 272; *King v Victoria Insurance Co* (1896) A.C. 250; *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330, 340; *Morris v Ford Motor Co Ltd* (1973) QB 792, 800, 812; *Simpson v Thomson* (1877) 3 App. Cas. 279, 284; *Central Insurance Co v Seacalf Shipping Corp.* (1983) 2 Lloyd's Rep. 25, 33; *Smith v Mainwaring* (1986) 2 Lloyd's Rep 244; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p497; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p708-709

¹³¹¹ Z Jing, "The Confusion between Subrogation and Assignment in the Insurance Law of the People's Republic of China 1995-A Critical Analysis on Article 44 of the Insurance Law", (2002) J.B.L. 608, p613

5.1. Whose name should be used in a subrogation action?

The question of whose name is to be used relates not only to essential matters but also to procedural matters. Under English insurance laws, this may not be an issue as it is well established that the insurer brings proceedings against the third party wrongdoer in the insured's name.¹³¹² However, in Vietnam, this is a real issue in both law and practice. The provisions of Vietnamese insurance laws relating to subrogation state that the insurer is entitled to take an action against the third party wrongdoer in his own name.¹³¹³

5.1.1. The Vietnamese legislation

Article 577 of Vietnam's Civil Code 2005 provides that : “(1) Where a third party is at fault for causing damage to the insured, and the insurer has paid insurance benefits to the insured, the insurer has the right to demand the third party indemnify the insurer for the insurance benefits already paid. The insured must provide the insurer with all necessary information, documentation and evidence of which the insured has knowledge in order to enable the insurer to exercise its right to demand the third party [to indemnify].

(2) Where an insured has received monetary compensation for damage from a third party which is less than the amount payable by the insurer, the insurer is only required to pay the difference between the [total] insurance benefits [otherwise payable] and the amount paid by the third party, unless otherwise agreed. If the insured has received insurance benefits but the insurance benefits are less than the damage caused by the third party, the insured has the right to demand the third party indemnify [the insured] for the difference between the insurance benefits and the monetary compensation for the damage.

An insurer has the right to demand the third party indemnify fully [the insurer] for the amount it has paid to the insured.”

It can be seen that this provision is a mixture of the subrogation principle and the assignment principle. The first paragraph of this provision states the general rule of the principle of subrogation. It deals with the situation where the insured is fully insured. The insurer who has fully indemnified the insured is entitled to make a claim against the third party responsible

¹³¹² *Mason v Sainsbury* (1782) 3 Doug. K.B. 61, p64; *London Assurance Co v Sainsbury* (1783) 3 Doug 245; *Simpson v Thomson* (1877) 3 App. Cas. 279

¹³¹³ Article 577 of Vietnam's Civil Code 2005; article 49 of Vietnam's Law on Insurance Business 2000; article 248 of Vietnam's Maritime Code 2005

for the loss for an amount equal to his payment to the insured. It is compatible with the general rule of the doctrine of subrogation. The insured cannot receive both payments from the insurer and from the third party wrongdoer. The burden of making payment ultimately falls on the third party who is at fault, and the insurer is entitled to recover what he has paid out under the policy.

However, as discussed above,¹³¹⁴ after having fully indemnified the insured, the insurer can use his own name to sue the third party wrongdoer, and the judgment may be given to him. It is implied that the insurer may retain the fruit of action against the third party wrongdoer. The insurer can obtain more than his payment under the insurance policy. This is inconsistent with the general rule of subrogation, that the insurer cannot recoup more than what he has paid out.

The situation where the insured is not fully insured is covered in the second paragraph of the provision. This paragraph has the features of the assignment principle.¹³¹⁵ Where the insured has received payment from the third party wrongdoer, the insurer is entitled to deduct that amount from his payment to the insured. The insured will subsequently assign the right of action to the insurer to claim against the third party wrongdoer. The insurer must bring an action against the third party wrongdoer in his own name. This is inconsistent with the principle of subrogation, that the insurer must step in the shoes of the insured to sue the third party wrongdoer.¹³¹⁶ However, according to the principle of assignment, the insurer can use his own name to sue the third party wrongdoer.

The last two sentences of the second paragraph refer to the assignment principle. After indemnifying the insured, the insurer is entitled to be subrogated to the insured's rights or remedies against the third party wrongdoer, irrespective of the fact that the insured has not been fully compensated for his total loss. The insurer has a right to sue the third party in his own name for his payment. The insured uses his own name to bring an action against the third party for his uninsured loss. This is inconsistent with the general rule of the principle of

¹³¹⁴ See section 4.1.1 of this Chapter

¹³¹⁵ See also Z Jing, "The Confusion between Subrogation and Assignment in the Insurance Law of the People's Republic of China 1995-A Critical Analysis on Article 44 of the Insurance Law", (2002) J.B.L. 608, p615

¹³¹⁶ *Mason v Sainsbury* (1782) 3 Doug. K.B. 61, p64; *London Assurance Co v Sainsbury* (1783) 3 Doug. 245

subrogation, that the insurer cannot control the proceedings until the insured has been fully compensated.¹³¹⁷

5.1.2. Commercial practices

In commercial practices, where the insurer has indemnified the insured and the third party is responsible for the loss, the insured must sign a receipt and subrogation form which expresses the insured's agreement to transfer and assign all his rights or remedies against the third party wrongdoer. Signing the receipt and subrogation form is a requisite for receiving indemnification by the insured. In the proceedings against the third party wrongdoer, this form is important evidence which shows that the insurer has paid out to the insured. If the insurer cannot submit this evidence to the court, the court may refuse to hear the case.

The standard terms of the receipt and subrogation form typically state that: "In consideration of having received this payment, we hereby agree to assign, transfer and subrogate to you, to the extent of your interest, all our rights and remedies in and in respect of the subject matter insured, and to grant you full power and give you any assistance you may reasonably require of us in the exercise of such rights and remedies in our or your name and at your own expenses." This typical form has two functions: a receipt of the insurance payment and the agreement to transfer from the insured to the insurer all rights and remedies which the insured may have against the third party wrongdoer.

The receipt and subrogation form is unambiguous evidence that there is confusion between the principle of subrogation and principle of assignment in commercial practices in Vietnam. The words "assign, transfer and subrogate" are used concurrently to vest in the insurer the insured's rights and remedies against the third party wrongdoer, and the insurer is allowed to take an action against the third party in either the insured's name or his own name for the amount he paid to the insured. The subrogation principle and the assignment principle are two distinct doctrines, one or the other occurs, but never both.¹³¹⁸ The insurer can exercise his subrogation rights or rely on his assignment rights, but these two rights cannot be possessed by the insurer concurrently to sue the third party wrongdoer. Where the insurer exercises his subrogation rights, the legal chose in action remains with the insured and the rules of

¹³¹⁷ *Commercial Union Assurance Co v Lister* (1874) L.R. 9 Ch.App. 483; *Globe & Rutgers Fire Insurance Co v Truedell* (1927) 2 D.L.R 659

¹³¹⁸ Z Jing, "The Confusion between Subrogation and Assignment in the Insurance Law of the People's Republic of China 1995-A Critical Analysis on Article 44 of the Insurance Law", (2002) J.B.L. 608, p619

subrogation apply. Where the insurer relies on his assignment rights, the legal chose in action vests in the insurer and the rules of assignment should operate.¹³¹⁹

5.1.3. Judicial practices

The confusion between assignment and subrogation causes several problems in respect of judicial matters. The following cases will reveal these problems. In *Tan Viet Ltd v Thanh Long Ltd*,¹³²⁰ the insured (Tan Viet) suffered a fire loss to his husking factory and other property. The insurer paid VND 2.5 billion to the insured in respect of the property damage claim. This payment constituted the limit payable under the policy, but the total loss of the insured was VND 7.5 billion. The insured subsequently brought an action against the third party wrongdoer (Thanh Long) for his uninsured loss of VND 5 billion. Knowing that the insured had conducted the litigation, the insurer (Bao Viet) asked the insured to join the proceedings, but the insured refused. The insurer later applied to the court to join the legal action as a co-plaintiff. The insurer's application was rejected by the court on the ground that there was no litigation agreement between the parties and the insurer was entitled to take an action against the third party in another case.

As far as the principle of subrogation is concerned, this was a wrong rejection by the court. The court confused the principle of subrogation and the principle of assignment and treated the receipt and subrogation form as evidence of assignment to the insurer of the rights to sue the third party wrongdoer. The court also considered that where the insured and the insurer could not reach a litigation agreement on the action against the third party wrongdoer, the insurer who had been assigned the right to sue would have to bring the other proceedings in his own name.

However, as a general rule of the principle of subrogation, the legal chose of action remains with the insured, and the insurer is not vested with a new cause of action.¹³²¹ The court was wrong to deny the insurer's right to join with the insured in the proceedings against the third party wrongdoer. The insurer needn't to set up a new cause of action in the other litigation

¹³¹⁹ *Ibid*

¹³²⁰ Vinh Long People's Court 2009

¹³²¹ *Yates v Whyte* (1838) 4 Bing.N.C. 272; *King v Victoria Insurance Co* (1896) A.C. 250; *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330, 340; *Morris v Ford Motor Co Ltd* (1973) QB 792, 800, 812; *Simpson v Thomson* (1877) 3 App. Cas. 279, 284; *Central Insurance Co v Seacalf Shipping Corp.* (1983) 2 Lloyd's Rep. 25, 33; *Smith v Mainwaring* (1986) 2 Lloyd's Rep 244; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p498; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), 708-709

against the third party wrongdoer. Under English law, if the insured refuses to lend his name to the proceedings, he may be compelled to do so.¹³²² The insured is entitled to control the proceedings against the third party wrongdoer, and the insurer is allowed to join the proceedings as a co-plaintiff. The parties will sue the third party for the insured's total loss, and then the subrogation recovery shall be divided between the parties. In fact, the court's refusal of the application of the insurer to join the proceedings against the third party wrongdoer costs the parties involved in the subrogation dispute money and time. The insurer must set up a new action against the third party, and the third party must engage in the other litigation for the same cause of action.

A more serious problem arose in another case, that of *Vien Dong Insurance Co. v Hanjin*.¹³²³ It is a case which shows Vietnamese laws to be ambiguous and inconsistent with the principle of indemnity. The insured had entered into a contract for carriage of goods by sea with the defendant. Upon arrival at Haiphong port, the cargo was damaged due to the carrier's fault. After being fully indemnified by the insurer, the insured signed the receipt and subrogation form. The insurer took an action against the carrier for his payment under the policy in Haiphong People's Court in his own name, and sought for the court's order to lien on the carrier's vessel. The carrier opposed the jurisdiction of the Haiphong People's Court on the ground that there was an agreement between the insured and the carrier that any disputes arising out of the contract for carriage of goods should be settled by Korean arbitration. However, the court still accepted for settlement the subrogation dispute and issued the order to lien on the vessel.

The court's acceptance for settlement of the case was fundamentally wrong. According to the general rules of the principle of subrogation, from the outset, the plaintiff was the insured. Therefore, all the agreements between the insured and the third party wrongdoer, such as the arbitration clause, were binding on the insurer.¹³²⁴ The insurer should not have been allowed to take the action against the third party wrongdoer at a Vietnamese court. The insurer was wrong to argue that he was entitled to bring the proceedings against the third party in his own name, and that the agreement between the insured and the carrier on dispute resolution did

¹³²² *Commercial Union Assurance Co v Lister* (1874) L.R. 9 Ch.App. 483; *Wilson v Raffalovich* [1881] 7 QBD 553; *King v Victoria Insurance Co* (1896) A.C. 250; *Yorkshire Insurance Co v Nisbet Shipping Co* (1962) 2 Q.B. 330; *Esso Petroleum Co Ltd v Hall Russell & Co Ltd* [1989] 1 All ER 37

¹³²³ Hai Phong People's Court 2008

¹³²⁴ *Schiffartsgesellschaft Detlev von Appen GmbH v Voest Alpine Intertrading GmbH* [1997] 2 Lloyd's Rep. 279; *West Tankers Inc v Ras Riunione Adriatica di Sicurta Spa* [2007] All ER 249

not bind him. Since the cause of action remained with the insured, the dispute between the insurer and the carrier in fact arose from the contract for carriage of goods. The insurer who made a claim by rights of subrogation was therefore bound by the agreement to refer it to arbitration in Korea.

5.2. Analysis and recommendation:

It is submitted that both the insurer and the insured having separate rights to take proceedings against the third party wrongdoer does not preserve the principle of indemnity. Where the insurer who has made payment to the insured acts before the latter to claim against the third party wrongdoer for his payment, he is entitled to recover up to the amount he has paid out. The insurer can keep all the subrogation recoveries, even if the insured later brings an action against the third party wrongdoer and recovers nothing. This is so simply because the insurer can use his own name to sue the third party wrongdoer, and judgment is given in his favour. The insured himself must bear the uninsured loss.¹³²⁵ It can be said that Vietnamese insurance laws vest the insurer assignment rights rather than subrogation rights.

This problem is more serious where there is limitation of the third party wrongdoer's liability or the third party wrongdoer is insolvent. There is a competition between the insurer and the insured in their claims for an insufficient amount¹³²⁶ of subrogation recovery from the third party wrongdoer. Under Vietnamese insurance laws, the insurer is vested assignment rights and is entitled to keep the whole amount which he may recover from the third party wrongdoer. This is inconsistent with the principle of indemnity. Balancing the insurer's right to recoup benefits he has paid against the insured's right to obtain full compensation for his loss, it is submitted that the insured should be able to take priority over the claim of the insurer.¹³²⁷ The confusion between the doctrine of subrogation and the doctrine of assignment under Vietnamese insurance laws needs to be clarified.

The problem also arises where there is an excess clause under the insurance policy. It may not be worthwhile for the insured to bring an action against the third party wrongdoer for a relatively small amount. It costs considerable time and money to conduct litigation. In Vietnamese culture, bringing legal proceedings against someone is the last resort. Vietnamese

¹³²⁵ For more details see 4.1 of this Chapter

¹³²⁶ The payment of the third party wrongdoer does not satisfy all the claims, including the insurer's payment under the policy and the insured's uninsured loss.

¹³²⁷ The reason for this view is critically analysed at 3.3 of this Chapter

insurance laws vesting in the insurer the right of assignment create unnecessary legal proceedings. Consequently, the insured is deprived of the right to achieve full compensation for his loss. It is submitted that only one lawsuit against the third party wrongdoer which is conducted by either the insurer or the insured in the insured's name should be imposed by Vietnamese insurance laws. The subrogation recovery from the third party wrongdoer should subsequently be divided between the insurer and the insured, with priority to the insured. This submission gives the insured a greater chance to achieve full compensation.

The confusion between the doctrine of subrogation and the doctrine of assignment under Vietnamese insurance laws creates a burden on the third party wrongdoer and problems for the parties involved in a subrogation dispute. The third party wrongdoer must become involved in two proceedings for the same cause of action. Vietnamese insurance laws' consideration of the insured's and the insurer's interests as separate claims against the third party wrongdoer causes unnecessary legal proceedings. Moreover, as far as the case of *Tan Viet Ltd v Thanh Long Ltd* is concerned,¹³²⁸ the judicial practice that the insurer had been deprived of the right to join with the insured in the proceedings against the third party wrongdoer by a Vietnamese court also leads to unnecessary expense of legal cost and unnecessary waste of time for the parties involved in a subrogation dispute. It is submitted that this wastefulness is against the public interest.

In contrast, under English laws, there is a general rule that a cause of action may not be litigated twice.¹³²⁹ In *Brunsdon v Humphrey*,¹³³⁰ Bowen LJ states that: "a well settled rule of law that damages resulting from one and the same cause of action must be assessed and recovered once for all." This rule results in no possibility of two courts reaching inconsistent decisions on the same facts and the same issue. This rule also saves any wasteful cost or expense in litigation and removes a heavy burden on the third party wrongdoer since he is not to be the defendant more than once in what is really the same claim.

It is submitted that the public interest in avoiding any possibility of two courts reaching inconsistent decisions on the same issue is undoubted and that two actions based on the same cause of action should never be allowed. Under Vietnamese insurance laws, two actions

¹³²⁸ This case has been analysed in section 5.1.3 of this Chapter

¹³²⁹ *Brunsdon v Humphrey* (1884) 14 Q.B.D 141; *Buckland v Palmer* (1984) 3 All.E.R. 554; R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p501; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1042

¹³³⁰ (1884) 14 Q.B.D 141, p147

based on the same cause of action against the third party wrongdoer are accepted.¹³³¹ There is a possibility of different judges taking different views on the liability of the third party wrongdoer. This may cause harassment of the parties involved in a subrogation dispute by exposing them to the anxiety and expense of unnecessary legal proceedings. It is clear that there are public interests in finality in litigation. A plaintiff should prove and recover damage, arising from one and the same cause of action, once for all. There is no reason for measuring the plaintiff's damage in one way in one case and in a different way in the other.

In this aspect, English laws can be a good model in respect of reforming Vietnamese insurance laws. In English laws of insurance, under the doctrine of subrogation, the insurer must step into the shoes of the insured to bring proceedings against the third party wrongdoer. In the leading case of *Mason v Sainsbury*¹³³², Lord Mansfield stated that: "every day the insurer is put in the place of the assured."¹³³³ In the later case of *London Assurance Co v Sainsbury*¹³³⁴, he had justified his conclusion that the insurer could not proceed in his own name but must proceed in the name of the insured on the ground that: "if the insurer could sue in his own name, no release by the insured would bar, nor would a verdict by him be a bar. It is impossible that the insured should transfer, and yet retain his right of action. Trustee and cestui que trust cannot both have a right of action."¹³³⁵ In *Simpson & Co v Thomson*¹³³⁶, Lord Cairns concluded that: "the right of the underwriters is merely to make such claim for damages as the insured himself could have made, and it is for this reason that (according to the English mode of procedure) they would have to make it in his name".¹³³⁷

Professor Merkin states that the question of whose name to be used is not only related to the procedural matter but also to the substantive issue, because any legal obstacle applicable to the insured's right of action binds the insurer suing in the insured's name.¹³³⁸ There are a number of situations in which this becomes relevant: (i) a claimant cannot sue himself;¹³³⁹ (ii)

¹³³¹ Article 577 of Vietnam's Civil Code 2005

¹³³² (1782) 3 Doug. K.B. 61; see also J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p331

¹³³³ *Mason v Sainsbury* (1782) 3 Doug. K.B. 61, p64; See also *London Assurance Co v Sainsbury* (1783) 3 Doug 245; in *Esso Petroleum Co Ltd v Hall Russell & Co Ltd* (1988) 3 W.L.R 730, it was held that the general rule, that if an indemnifier was subrogated to the rights of someone whom he had indemnified he could only pursue those rights in the name of that person and not in his own name, applied even where the indemnifier also had a claim for damage to property arising out of the same act which gave rise to the indemnification.;

¹³³⁴ (1783) 3 Doug 245

¹³³⁵ *Ibid*, p253; *Napier v Hunter* (1993) A.C. 713, p750

¹³³⁶ (1877) 3 App Cas 279

¹³³⁷ *Ibid*, p 286

¹³³⁸ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p497

¹³³⁹ *Simpson v Thomson* (1877) 3 App. Cas. 279

any agreement between the insured and the third party wrongdoer which relieves the third party from some or all liability binds on the insurer;¹³⁴⁰ (iii) any agreement between the insured and the third party relating to dispute resolution provision, such as an arbitration clause or an exclusive jurisdiction clause, binds also to the insurer;¹³⁴¹ (iv) the insured's action might be time-barred. Any limitation provision applicable to the insured's action also is binding on the insurer;¹³⁴² (v) where the insured is a company which has been wound up and has ceased to exist, the insurer is no longer entitled to exercise his subrogation rights;¹³⁴³ (vi) the law applicable to the insured's cause of action against the third party similarly governs the subrogation action brought by the insurer, irrespective of the law applicable to the contract of insurance;¹³⁴⁴ (vii) the fact that the insurer is the de facto claimant is to be disregarded. Therefore, the defendant cannot seek disclosure from the insurer as the insurer is technically not a party to the action.¹³⁴⁵

Under English insurance laws, it has been recognised that the insurer is subrogated to all the rights which the insured is entitled to bring in proceedings against a third party to diminish his loss.¹³⁴⁶ The insurer is entitled to subrogate to any right of action subsisting when the insured has been fully indemnified.¹³⁴⁷ These rights can be rights in tort,¹³⁴⁸ in contract¹³⁴⁹, by statute¹³⁵⁰ or in accordance with an applicable custom or usage.¹³⁵¹

¹³⁴⁰ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p497

¹³⁴¹ *Schiffartsgesellschaft Detlev von Appen GmbH v Voest Alpine Intertrading GmbH* [1997] 2 Lloyd's Rep. 279; *West Tankers Inc v Ras Riunione Adriatica di Sicurta Spa* [2007] All ER 249

¹³⁴² *London Assurance Co v Johnson* (1737) Hardw. 269; *RB Policis v Butler* (1949) 65 T.L.R. 436

¹³⁴³ *Smith (Plant Hire) Ltd v Mainwaring* [1986] 2 Lloyd's Rep. 244

¹³⁴⁴ *West Tankers Inc v Ras Riunione Adriatica di Sicurta Spa* [2007] All ER 249

¹³⁴⁵ *James Nelson v Nelson Line* [1906] 2 K.B. 217

¹³⁴⁶ *Castellain v. Preston* (1883) 11 QBD 380, p388, Brett LJ stated that: "the underwriter is entitled to the advantage of every right of the assured, whether such right consists in contract, fulfilled or unfulfilled, or in remedy for tort capable of being insisted on or already insisted on, or in any other right, whether by way of condition or otherwise, legal or equitable, which can be, or has been exercised or has accrued, and whether such right could or could not be enforced by the insurer in the name of the assured by the exercise or acquiring of which right or condition the loss against which the assured is insured, can be, or has been diminished."; R Hodgkin, *Insurance Law: Text and Materials*, (Cavendish Publishing Limited, London, 1998), p565

¹³⁴⁷ *Napier v Hunter* (1993) A.C. 713, p734

¹³⁴⁸ The insurer may be subrogated to rights in tort (such as: negligence or deceit) against the third party wrongdoer; see also *Lister v Romford Ice and Cold Storage Co Ltd* (1957) 1 All.E.R. 125; *King v Victoria Ins Co* (1896) AC 250; *Assicurazioni Generali di Trieste v Empress Assurance Co Ltd* (1907) 2 K.B 814; M.A Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1035

¹³⁴⁹ Where the insured suffers due to breach of contract by the other party and the insured is insured against such loss. The insurer then, once he has paid out on the policy, may subrogate to the insured's claim in contract; *Darrell v Tibbitts* (1880) 5 Q.B.D 560; *Caledonia North Sea Ltd v British Telecommunications Plc* (2002) All ER (D) 85; M.A.Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1034

¹³⁵⁰ *Mason v Sainsbury* (1782) 3 Doug. K.B. 61; see also M.A. Clarke, *The Law of Insurance Contracts*, (6th edn, Infoma, 2009), p1035

The insurer is only entitled to make a claim which the insured himself could have made because the insurer steps into the insured's shoes. The insurer can assert claims no greater or different from the insured's rights.¹³⁵² Where there is an agreement, before a loss is incurred, between the insured and the third party wrongdoer, which limits the insured's rights to sue, that limitation binds to the insurer's rights to subrogate as well.¹³⁵³ For instance, a contract between a goods-owner and a carrier may provide that, if the carrier is liable for the loss, he shall have the benefit of any insurance effected on the goods. In such a case, even if the carrier is responsible for the damage, he can have the benefit of the insurance money which is incorporated into the contract of carriage, and the insurer has no right of subrogation. Another example is a dispute resolution provision¹³⁵⁴ in which it is stipulated that any dispute arising out of the contract between the goods-owner and the carrier shall be settled by an identified arbitral tribunal: the insurer is bound by that provision.

Regarding the issue of who controls the proceedings against the third party wrongdoer, under English insurance laws, the insured has the right to sue the third party wrongdoer and control the proceedings until the insured is fully compensated for his total loss.¹³⁵⁵ In the case of under-insurance, an under-insured insured who has been paid by his insurer is entitled to take an action against a wrongdoer and to exercise his rights to recover his uninsured loss, provided that he sues for his entire loss.¹³⁵⁶ The proper claimant against the third party wrongdoer, from the outset, is the insured.¹³⁵⁷ He is a party to the action so that judgment can be given in his favour.¹³⁵⁸ In *Commercial Union Assurance Co v Lister*,¹³⁵⁹ the court held that as the insured would not be fully compensated by his insurers, the insured was entitled to bring and control the action, provided his action was bona fide and he sued for the whole loss. The requirement on the insured to act in good faith in the interests of the insurer was

¹³⁵¹ *Tate v. Hyslop* (1885) 15 Q.B.D. 368; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p704

¹³⁵² John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p707; G Veal, "Subrogation: The duties and obligations of the insured and rights of the insurer revisited", (1992) 28 Tort & Ins.L.J 69, p70

¹³⁵³ *Lister v Romford Ice and Cold Storage Co Ltd* (1957) 1 All.E.R. 125

¹³⁵⁴ *Schiffartsgesellschaft Detlev von Appen v Voest Alpine Intertrading* (1997) 2 Lloyd's Rep. 279

¹³⁵⁵ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p333-334

¹³⁵⁶ J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p334

¹³⁵⁷ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p488

¹³⁵⁸ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p500

¹³⁵⁹ (1874) L.R. 9 Ch.App. 483

confirmed by the House of Lords in *Napier v Hunter*.¹³⁶⁰ Where the insured does not act in good faith, prejudicing the insurer's position, he shall be liable to the insurer in damages.¹³⁶¹

When the insurer has fully compensated the insured for the loss suffered, he can take over the control of proceedings on undertaking to indemnify the insured against his cost.¹³⁶² An insured who does not seek to invoke his right to sue the third party will be required by the doctrine of subrogation to lend his name to the insurer's action.¹³⁶³ If the insured refuses to hand over control to the insurer, he will be ordered by the court to do so.¹³⁶⁴ The insurer can take an action against the third party wrongdoer in his own name, joining the insured as a second defendant.¹³⁶⁵

Concerning the time when the rights against the third party wrongdoer transfers from the insured to the insurer, under English insurance laws, after having indemnified the insured, the insurer immediately becomes entitled to be subrogated to the right of the insured to sue and recover damages in an action against the third party wrongdoer.¹³⁶⁶ Subrogation arises by operation of law, and there is no need for the contract of insurance to contain an express stipulation as to the transfer of subrogation rights.¹³⁶⁷ In *Randal v Cockran*,¹³⁶⁸ Lord Hardwicke stated that: "the person originally sustaining the loss was the owner; but after satisfaction made to him, the insurer. No doubt, but from that time, as to the goods themselves, if restored in specie, or compensation made for them, the assured stands as a

¹³⁶⁰ *Napier v Hunter* (1993) A.C. 713, p736; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p334-335

¹³⁶¹ *West of England Fire Insurance Co v Isaacs* (1897) 1 Q.B. 226; *Phoenix Assurance Co v Spooner* (1905) 2 K.B. 753; *Re Law Fire Assurance Co* (1888) 4 T.L.R. 309; *Horse, Carriage & General Insurance Co v Petch* (1916) 33 T.L.R. 131; *Hayler v Chapman* (1989) 1 Lloyd's Rep. 490; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p331

¹³⁶² John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p711

¹³⁶³ R Merkin, *Law of Insurance*, (9th edn, Sweet & Maxwell, 2010), p500

¹³⁶⁴ *Commercial Union Assurance Co v Lister* (1874) L.R. 9 Ch.App. 483

¹³⁶⁵ *King v Victoria Insurance Co* [1896] A.C. 250; *Re Miller, Gibb & Co* [1957] 2 All ER 266; *Jubilee Motor Policies Syndicate 1231 at Lloyd's v Volvo Truck & Bus (Southern) Ltd* [2010] EWHC 3641; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), p710; J Birds, *Modern Insurance Law*, (8th edn, Sweet & Maxwell, London, 2010), p331

¹³⁶⁶ *Re Miller, Gibb & Co* [1957] 2 All ER 266, *Napier v Hunter* (1993) A.C. 713; Zhen Jing, "The Confusion between Subrogation and Assignment in the Insurance Law of the People's Republic of China 1995-A Critical Analysis on Article 44 of the Insurance Law", (2002) J.B.L. 608, p613; John Birds and others, *MacGillivray on Insurance Law*, (12th edition, Sweet & Maxwell, London, 2012), 692-693

¹³⁶⁷ T Brown and M Goode, "Conflict of interest in subrogation actions", (1986) 22 Tort & Ins.L.J. 16, p21

¹³⁶⁸ (1748), 1 Ves.Sen 98

trustee for the insurer, in proportion for what he paid ...” The subrogation rights of the insurer arise automatically upon payment of a loss, whether the loss is total or partial.¹³⁶⁹

In sum, the confusion between the doctrine of subrogation and the doctrine of assignment under Vietnamese insurance laws creates unnecessary legal proceedings against the third party wrongdoer and prevents the insured from achieving full compensation for his total loss. It is suggested that only one action against the third party wrongdoer in a dispute over subrogation recovery, which is conducted by either the insurer or the insured, should be imposed by Vietnamese insurance laws. The insurer or the insured should bring the proceedings to claim for the whole loss of the insured. The insurer should step into the shoes of the insured to take an action against the third party wrongdoer and must sue in the insured’s name.

6. CONCLUSION AND RECOMMENDATION

Many problems concerning subrogation in Vietnamese insurance laws and commercial practices have been critically analysed throughout this chapter. It can be seen that current Vietnamese insurance laws give priority to the insurer in respect of reimbursement from subrogation recovery. In addition, the confusion between the principle of subrogation and the principle of assignment under Vietnamese insurance laws and practices cause several problems for the parties involved in a subrogation dispute. This creates several obstacles for the insured in seeking to achieve full compensation for his total loss. It is suggested that, to solve these problems, all the features of assignment in the provisions governing subrogation disputes should be removed, giving them a pure feature of subrogation. The reform of Vietnamese insurance laws should be made in accordance with the nature and general rules of subrogation.

The following propositions are advocated:¹³⁷⁰

- No distinction is to be drawn between marine and non-marine policies in relation to the general principles of the allocation of subrogation recoveries.

¹³⁶⁹ SR Derham, *Subrogation in Insurance Law*, (Law Book Company, Sydney, 1985), p54. Derham states that: “the questions of the right of the insurer to commence an action and the destination of subrogation recoveries would be treated separately by English courts.”

¹³⁷⁰ A Tar, “Subrogation and the Ash Wednesday bushfire disaster”, (1987-1988) 11 Adel. L. Rev. 232, p235-238

- In no case may the insurer recover more than he has paid out under the insurance policy.
- Either the insurer or the insured, when taking an action against the third party wrongdoer, shall pay proper regard to the interests of the other parties and must sue for the insured's total loss.
- Where the insurer has indemnified the insured under the policy, the insurer is entitled to exercise subrogation rights against the third party wrongdoer. The insurer can request the insured to lend his name to the action against the third party wrongdoer. The insurer shall step into the shoes of the insured to bring proceedings against the third party wrongdoer for the insured's total loss.
- Where the insured is fully compensated for his total loss under the policy, the insured's rights against the third party wrongdoer pass completely to the insurer. The decision to proceed or not proceed against the third party wrongdoer should rest with the insurer. However, where the subrogation recovery from the third parties may exceed the insured's total loss, the insured is entitled to obtain the surplus.
- Where the total loss suffered by the insured exceeds the indemnity payable under the policy, the insured is entitled to take an action against the third party wrongdoer and is entitled to control the proceedings, provided that the insured sues the third party for the full amount of his total loss. Duty to account to the insurer for any surplus only arises when the insured is fully compensated for his total loss.
- Before making a claim against the insurer under the policy, if in any court or other proceedings, or by way of settlement, the insured with proper regard to the insurer's interests succeeds in recovering more than his uninsured loss, the insured must account to the insurer for the excess after recouping himself fully for the loss, costs and expenses. The duty to account arises only when the insured has been fully compensated, not on full indemnification under the policy, provided that the insured sues the third party wrongdoer for his total loss and pays regard to the insurer's interests.
- Where the insured brings proceedings against, or settles with, the third party wrongdoer without proper regard to the insurer's interests, the insured is liable to the insurer in damages for any loss which may occur.

- The rules on destination of subrogation recovery are modified in the case of policies containing average clauses. Average clauses provide that, if at the time of the loss the value of the subject matter insured exceeds the sum insured, the insured is deemed to be his own insurer for the difference in value and must bear a rateable proportion of the loss accordingly.
- Where the policy is a valued policy and the subject matter is insured for its full value, the policy valuation is conclusive evidence of the insured's total loss. The insurer has first claim on subrogation recovery. Any surplus in excess of the insurer's payment under the policy is obtained by the insured.
- Where on a valued policy the insured sum is less than the agreed stated value, the insured has priority over his insurer in pursuing subrogation recovery.
- Where the insurer and the insured, at the time of entering into the insurance contract, conclude express provisions governing the matter of subrogation rights and obligations, or prior to commencing any action against a third party wrongdoer, enter into a litigation agreement, the intention of the parties should be considered first in respect of allocation of subrogation recovery from a third party wrongdoer. If there is any ambiguity, the general rules of the principle of subrogation shall apply.

Therefore, it is recommended that relevant articles of Vietnamese insurance laws are amended as follows:

“Where a third party is at fault for causing damage to the insured, and the insurer has paid insurance benefits to the insured, the insurer shall be subrogated to the insured's right of action against the third party for demanding the compensation.

Where the insurer exercises his subrogation rights against the third party wrongdoer, he should sue in the insured's name, and claim for the amount of the whole loss the insured has suffered.

Subrogation recoveries shall firstly satisfy the insured with the portion which is excluded from the insurance coverage; the surplus will go to recoup the insurer. In no circumstance may the insurer recoup from the third party's payment more than his payment under the policy

Where the policy is a valued policy and the subject matter is insured for its full value, the policy valuation is conclusive evidence of the insured's total loss, and the insurer has first claim on subrogation recovery. Where on a valued policy the insured sum is less than the agreed stated value, the insured has priority over his insurer in pursuing subrogation recovery.

The rights of an insured and insurer under the preceding provisions are subject to any agreement made between them.”

CHAPTER 6: CONCLUSIONS AND RECOMMENDATIONS

There are two parts in this chapter: conclusions in the first part and recommendations in the second part. In the first part, the research results of the thesis will be summarised, with stress on the similarities and differences between English and Vietnamese insurance laws, followed by some explanations of why these similarities and differences exist.

In the second part, recommendations will be formulated for the amendment of the provisions of the Vietnam's Insurance Law in relation to the three fundamental principles, by referring to a number of better solutions from English and Australian or other countries. It is hoped that these recommendations may present useful models for the amendment of Vietnam's insurance laws.

1. CONCLUSIONS

1.1. Summary of the research

With the aim of proving the hypothesis question as to: "If insureds have suffered an actual economic loss caused by an insured risk, to what extent does the current Vietnamese insurance law on subrogation and insurable interest allow them to be compensated for their loss? And what reforms are necessary to protect the insureds' rights to obtain full compensation?", the thesis has thoroughly studied the three important principles in insurance laws, and in English and Vietnamese insurance laws in particular, namely: the principle of indemnity, the principle of insurable interest and the principle of subrogation.

Before doing this, the research presents a basic background of Vietnamese insurance industry, market practices and insurance legislation. A brief overview of Vietnam's judicial system is also given to show how Vietnamese courts deal with insurance cases.

The thesis examines briefly the nature of the principle of indemnity, evaluates the rationality and the complexity of the indemnity regime, and examines the purposes of its existence. Through a comparison and discussion of English and Vietnamese laws of insurance, it can be concluded that provisions relating to the indemnity principle in the Vietnamese laws of insurance are similar to English laws. In both English and Vietnamese insurance laws, there are several important principles derived from the principle of indemnity, such as the principle

of insurable interest, the principle of subrogation, the principle of double insurance and the principle of abandonment. In theory, those principles, on a rationale stemming from the principle of indemnity, preserve the objectives of the indemnity principle, namely: (i) to prevent the insureds from making an unfair profit from insurance contracts, and (ii) to ensure that the insurers give a full compensation for the insureds' actual losses, no more and no less. However, rules derived from those principles are not consistent with the nature of the principle of indemnity.

The research has critically examined the application of the two principles (the principle of insurable interest and the principle of subrogation) in connection with the indemnity principle in both English and Vietnamese laws. In order to be indemnified, an insurable interest of the insureds is still required in English and Vietnamese laws. However, in Australian laws, the requirement for insurable interest has been removed. The research has extensively discussed whether it is necessary that the insureds, in order to make a valid claim, are required to show an insurable interest in Vietnamese insurance laws.

Concerning the principle of subrogation, the allocation of subrogation recovery from a third party between the insureds and the insurers has been critically examined. In the triangular relationship of the insured, the insurer and the third party, where the insured is fully compensated for his total loss under the insurance policy or by the third party's payment, the problem of distribution of subrogation recoveries between the insurer and the insured does not arise. However, the third party payment is often insufficient to cover all the claims from the insured and the insurer, and insurance proceeds frequently do not fully compensate for damages suffered by the insured as a result of a loss. When this occurs, the insurer has a right to be subrogated of the insured's right to sue the third party wrongdoer, and the insured is also entitled to seek full compensation for his total loss from the third party wrongdoer. In such a case, a fundamental issue arises as to the distribution of any subrogation recovery between the insured and the insurer. Under Vietnamese insurance laws, it is difficult for the insureds to obtain a full compensation for their total loss. In addition, there is confusion between the doctrine of subrogation and the doctrine of assignment. This confusion also creates legal obstacles, barring the insureds from gaining full compensation. The analyses of the thesis show that the English approach is a suitable model for amendment of the provisions governing subrogation under Vietnamese insurance laws.

Through comparisons between Vietnamese and English insurance laws regarding the indemnity principle and other principles derived from the principle of indemnity, problems of the provisions in Vietnam's law are found: the pitfalls arising for litigants and commercial practices have been particularly highlighted.

1.2. Research findings:

Through the critical analyses in the above chapters, the following conclusions can be drawn:

1.2.1. Similarities between English and Vietnamese insurance laws

An important conclusion that can be reached through the study of English and Vietnamese insurance laws is that there are several similarities in the two laws. Both acknowledge that the principle of indemnity is a fundamental principle in insurance laws. The principle of subrogation and the principle of insurable interest are also recognised under both laws.

These similarities are understandable, because during the process of drafting any new legislation, Vietnam, a developing country, is able to save time when drafting and improving its laws by learning lessons and studying the experiences of the countries with similar social – political environments or of developed countries which are famous for and have a long history of development of the relevant legal areas.

English insurance laws have a long history of development, and are famous throughout the world, and are considered as model laws by a number of countries, including Vietnam. A number of provisions governing marine insurance under Vietnam's Maritime Code are similar to those of the MIA 1906. In particular, some of them are copied from the MIA 1906 (in presentation and wording). For example, the concept of insurable interest in Article 226 of Vietnam's Maritime Code 2005 is identical to that of section 5 of the MIA 1906.

These similarities suggest that Vietnamese lawmakers have for a long time made reference to English insurance laws in order to draft Vietnamese insurance laws. This is also shown in the documentation and materials on the history of development of Vietnamese insurance laws (such as provisions governing contracts of marine insurance in Vietnam's Maritime Code 1990 and Vietnam's Maritime Code 2005, Law on Insurance Business 2000). In addition, English companies' insurance policies (such as Lloyds) have provided standard practices, and

are used by most Vietnamese insurance companies. This again confirms that the study of English insurance laws with the aim of improving Vietnamese insurance laws is reasonable.

1.2.2. Insurable interest:

Although both laws apply the legal right approach, the concept of insurable interest under English laws is much broader than in Vietnamese law. Under Vietnamese law, a relation, which is sufficient to show an insurable interest, between the insureds and the insured properties must be recognised by laws. In most cases, it is the relation between the owners and the insured properties or the relation arising out of contracts. The rights which may give insureds an insurable interest are listed, and are restricted to right of ownership, right of possession, right of use and property right.¹³⁷¹ Moreover, in contrast to English law, there is no equitable relation which may give insureds an insurable interest in Vietnam's insurance laws, since the latter contain no equity law.

An example which illustrates the narrowness of the concept of insurable interest under Vietnamese law is the case relating to the interests of sub-contractors in a large construction or offshore project. A sub-contractor may have an insurable interest in the whole project in English law, but not in Vietnamese law.

Again, it can be seen that the rigid legal right approach to the application of the principle of insurable interest in Vietnam's insurance laws makes it inconsistent with the purposes of the principle of indemnity. The insureds who have suffered actual losses and are able to prove the losses still cannot receive compensation if they cannot show legal relationships to the insured property. The Vietnamese insurers may take advantage of this gap to gain unjust enrichment by entering into insurance contracts with questionable insurable interests, and then refusing to make a payment on the grounds of lack of an insurable interest. This behaviour of Vietnamese insurance companies is contrary to the principle of indemnity and the principle of utmost good faith, and can cause adverse effects on the insurance market, particularly in the markets that are developing, like that of Vietnam. Moreover, this legal right approach creates legal obstacles for insurance companies when they offer a new insurance product, which hinders the development of the property insurance market in Vietnam.

¹³⁷¹ Article 3(9) of Vietnam's Law on Insurance Business 2000

In England, besides the legal right approach, another approach has been developed over the past 200 years: the factual expectation approach. There is much controversy surrounding the two approaches, and the debate still exists. Both approaches may cause ambiguities and uncertainties over the interpretation and application of the principle in practice. Even if the factual expectation approach is applied, some inconsistencies with the principle of indemnity can be found.

1.2.3. Subrogation

As the subrogation principle is also one of the principles derived from the principle of indemnity, its application, in general, is to support and preserve the principle of indemnity. However, there are differences in English and Vietnamese approaches. Under English law, insurers are allowed to use the insureds' name to take actions against a third party wrongdoer and then allocate the subrogation recovery between them. Under Vietnamese law, the insurers and the insureds can bring actions against the third party wrongdoer in two separate cases:¹³⁷²

(i) after having indemnified the insureds, the insurers take an action in their own name to recoup the payment that has been made to the insureds, and (ii) the insureds bring another action against the third party for the difference between the actual loss and the insurance money. The confusion between the doctrine of subrogation and the doctrine of assignment under Vietnamese law leads to inadequate protection of the insureds' right to obtain full compensation for their actual losses. The insureds find difficulty in fully recovering their loss. This is a crucial difference between English and Vietnamese laws relating to the principle of subrogation. The English approach is more consistent with the principle of indemnity. A study of the English approach suggests ways to reform the provisions governing subrogation under Vietnamese insurance laws.

1.2.4. Other findings:

In addition to the above major findings, this research also points out the differences between English and Vietnamese laws in the application of those principles. In many cases, although the provisions in the two laws are similar, the practical application is quite different in practice. The English approach, which is more consistent with the principle of indemnity, is much more flexible than the Vietnamese approach.

¹³⁷² This is contrary to the fundamental rule: a course of action cannot be litigated twice.

For instance, in relation to the approaches to distribution of subrogation recovery from a third party between an insured and an insurer, English rules are more flexible and more justifiably suitable, giving the insured more chance to obtain full compensation. In *Yorkshire Insurance Co v Nisbet Shipping Co*,¹³⁷³ the insureds were given the fruit of proceedings against the third party wrongdoer. In Vietnam, the insurer and the insured have separate rights to take proceedings against the third party wrongdoer. This causes enormous difficulty for the insured in achieving full compensation, and creates a heavy burden for the third party wrongdoer- he can be taken to courts twice due to the same cause of action.

Those differences can be explained by the fact that Vietnam and England have two different legal systems (England- common law, and Vietnam- civil law). Common law is more flexible than the civil law because the common law courts have the authority to make law. On the other hand, Vietnam has adopted the civil law, and legislation is interpreted by judges to resolve a dispute. Sometimes the legislation is interpreted in accordance with the strictly literal meaning, resulting in rigidities. Moreover, Vietnamese insurance laws are not comprehensive, making the law impracticable in some circumstances.

2. RECOMMENDATIONS

2.1. Recommendations on provisions of the principle of subrogation

As discussed above, the application of the principle of subrogation in Vietnamese insurance laws is not consistent with the principle of indemnity. The confusion between the principle of subrogation and the principle of assignment has caused many problems in practice. Furthermore, the distribution of the subrogation recovery from a third party between insurers and insureds under Vietnamese laws does not fulfil the purpose of the indemnity principle (i.e., does not give the insureds full compensation for their actual losses). The legitimate interests of the insureds are not guaranteed. The relevant rules in English insurance laws are much more consistent and could be a model for amending Vietnam's insurance laws. Amendment and supplement to the provisions in Vietnam's insurance laws can be proposed, as follows:

¹³⁷³ (1962) 2 Q.B. 330

The current provision, Article 577 of Vietnam's Civil Code 2005: "Transfers of claims for indemnity: (1) Where a third party is at fault for causing damage to the insured, and the insurer has paid insurance benefits to the insured, the insurer has the right to demand the third party indemnify the insurer for the insurance benefits already paid. The insured must provide the insurer with all necessary information, documentation and evidence of which the insured has knowledge in order to enable the insurer to exercise his right to demand the third party to indemnify.

(2) Where an insured has received monetary compensation for damage from a third party which is less than the amount payable by the insurer, the insurer is only required to pay the difference between the total insurance benefits otherwise payable and the amount paid by the third party, unless otherwise agreed. If the insured has received insurance benefits but the insurance benefits are less than the damage caused by the third party, the insured has the right to demand that the third party indemnify the insured for the difference between the insurance benefits and the monetary compensation for the damage.

An insurer has the right to demand the third party to indemnify fully the insurer for the amount it has paid to the insured"

should be amended as follows:

Article 577 of Vietnam's Civil Code 2005 "Rights of subrogation"

(1) "Where a third party is at fault for causing damage to the insured, and the insurer has paid insurance benefits to the insured, the insurer shall be subrogated to the insured's right of action against the third party for demanding the compensation.

Where the insurer exercises his subrogation rights against the third party wrongdoer, he should sue in the insured's name, and claim for the amount of the whole loss the insured has suffered.

The insured must provide the insurer with all necessary information, documentation and evidence of which the insured has knowledge in order to enable the insurer to exercise his right to demand the third party to indemnify.

(2) Subrogation recoveries shall firstly satisfy the insured with the portion which is excluded from the insurance coverage, the surplus will go to recoup to the insurer. In no circumstance

may the insurer recoup from the third party's payment more than his payment under the policy.

(3) Where the policy is a valued policy and the subject matter is insured for its full value, the policy valuation is conclusive evidence of the insured's total loss, the insurer has first claim on subrogation recovery. Where on a valued policy the insured sum is less than the agreed stated value, the insured has priority over his insurer in pursuing subrogation recovery.

(4) The rights of an insured and insurer under the preceding provisions are subject to any agreement made between them.”

Sub-section (1) and (2) of Article 49 of Law on Insurance Business 2000, and Article 247 and Article 248 of Maritime Code 2005 should also be amended in accordance with the above provision.

2.2. Recommendations on provisions of insurable interest

May the factual expectation approach be the best solution for Vietnamese insurance laws? The answer is no. The reason for this is that this approach is still causing ambiguities and uncertainties over the application of the principle of insurable interest in English laws, and if this approach is applied in Vietnam, it can cause the same ambiguities and uncertainties. Many more difficulties can be found, for four reasons: (i) the Vietnamese insurance market is a new and developing market, and insurers often abuse their power to make profit at the expense of the insureds, (ii) the current Vietnamese insurance laws give enormous protection to insurers, (iii) the technical task of generalizing the concept of insurable interest from English case law in which the factual expectation approach is applied, and codifying the concept into Vietnamese laws is a difficult job, and (iv) the factual expectation approach itself still causes ambiguities and uncertainties over its application, preventing the insureds from exercising the rights to obtain full compensation for their actual loss in some circumstances.¹³⁷⁴

The solution provided by Australian law, in which the principle of insurable interest has been eliminated in indemnity insurance, suggests that a similar remedy could be applied in Vietnamese law. Therefore it is proposed that, article 3(9) of Vietnam's Law on Insurance

¹³⁷⁴ See section 5.3 of Chapter 4: Insurable interest

Business 2000 and article 225 and 226 of Vietnam's Maritime Code 2005 should be removed.

A question may arise as to whether the removal of the principle of insurable interest may provide an incentive to make an unfair profit from insurance contracts. The answer is no. In practice, the removal of the principle has not caused any serious problems in Australia, and only three cases of disputes concerning the issues of insurable interest have occurred in about 30 years. In Vietnam, there were also not many such cases. Thus, it seems that concern about profiteering from insurance contracts is probably excessive. Moreover, the insurers themselves, with all of their professional knowledge and experience, their data, tools of probability and risk management, are well able to prevent profiteering. Finally, the principle of indemnity is also a legal barrier to prevent it, because in order to receive compensation the insureds are required to prove their actual loss. If they cannot prove the loss, the insurers' obligation to indemnify does not arise.

3. ISSUES FOR THE FUTURE RESEARCH

This thesis, like any other research, cannot solve all of the problems related to its topic. The principle of indemnity is the most important principle of insurance laws, its content is very broad, and it is a solid foundation for the formulation of several other principles. In this thesis, only two principles (subrogation and insurable interest) derived from the principle of indemnity are studied in depth. In the insurance laws of Vietnam, there are many more issues relating to the principle of indemnity which need to be clarified and dealt with in the future. These may be topics of intensive research, for example:

- The measure of indemnity: this topic is very interesting and very practical, especially in the context of Vietnam. In Vietnam, the disputing parties and the courts often face many difficulties in calculating the amount of compensation from insurance companies. A study of these difficulties and their underlying causes, as well as the provision of solutions to the difficulties is needed for Vietnam. However, it is a broad topic because it is related not only to insurance laws, but also to laws involving damages in civil law.

- There are other principles stemming from the principle of indemnity and their application in practice. They include the principle of double insurance and contribution, the principle of

abandonment, and the principle of reinstatement. Research on these principles is needed in order to investigate whether their application is consistent with the purposes of the principle of indemnity.

The principle of indemnity is the spine of property insurance law. Therefore, ensuring that other principles comply with the indemnity principle is an essential task. Adherence to this principle will create the backbone for establishing a legal framework for the sustainable development of Vietnam's property insurance market in which a balance of the rights and interests of insurers and insureds can be achieved.

APPENDIX

EXCERPT OF THE RELEVANT PROVISIONS FROM VIETNAM'S LAW ON INSURANCE BUSINESS 2000, MARITIME CODE 2005 AND CIVIL CODE 2005

I. LAW ON INSURANCE BUSINESS 2000

Article 3 *Definitions*

6. Purchaser of insurance means an organization or individual entering into a contract of insurance with an insurer and paying an insurance premium. The purchaser of insurance may at the same time be the insured person or the beneficiary.

7. Insured person means an organization or individual having their property, civil liability or life insured in accordance with an insurance contract. The insured person may at the same time be the beneficiary.

9. Insurable interest means a right of ownership, right of possession, right of use, or property right; maintenance rights and obligations to the person insured against...

Article 12 *Insurance contracts*

1. An insurance contract means an agreement between a purchaser of insurance and an insurer, pursuant to which the purchaser of insurance must pay an insurance premium and the insurer must pay insurance proceeds to the beneficiary or indemnify the insured person upon occurrence of the insured event.

2. Types of insurance contracts shall comprise:

- (a) Contracts of personal insurance;
- (b) Contracts of property insurance;
- (c) Contracts of civil liability insurance.

3. Contracts of marine insurance shall be governed by the provisions of the Maritime Code; with respect to issues not covered by the Maritime Code, the provisions of this Law shall apply.

4. Issues relating to insurance contracts which are not covered by this Chapter shall be governed by the provisions of the Civil Code and the provisions of other relevant laws.”

Article 14 *Forms of insurance contracts*

1. An insurance contract must be made in writing.

2. Proof of entering into an insurance contract shall be a certificate of insurance, an insurance policy, a telegram, a telex, a facsimile and other forms stipulated by law.”

Article 17 *Rights and obligations of insurers*

1. An insurer shall have the rights:

- (a) To collect the insurance premium in accordance with the agreement in the insurance contract;
- (b) To require the purchaser of insurance to provide complete and truthful information relating to entering into and implementing the insurance contract;
- (c) To suspend unilaterally the implementation of the insurance contract in accordance with the provisions of article 19.2, article 20.2, article 35.2 and article 50.3 of this Law;
- (d) To refuse to pay insurance proceeds to the beneficiary or to refuse to indemnify the insured person in circumstances outside the scope of the insurance liability or in circumstances where liability is excluded as agreed in the insurance contract;
- (dd) To require the purchaser of insurance to implement measures to prevent and minimize loss in accordance with the provisions of this Law and the provisions of other relevant laws;
- (e) To require a third party to reimburse the insured sum which the insurer has paid to indemnify the insured person as a result of the third party in the cases of property and civil liability³⁸;
- (g) Other rights as stipulated by law.

2. An insurer shall have the obligations:

- (a) To explain to the purchaser of insurance the insurance terms and conditions and the rights and obligations of the purchaser of insurance;
- (b) To issue to the purchaser of insurance a certificate of insurance or an insurance policy after entering into the insurance contract;
- (c) To pay insurance proceeds in a timely manner to the beneficiary or to indemnify the insured person upon occurrence of the insured event;
- (d) To provide a written explanation of the reasons for refusal to pay insurance proceeds or indemnity;
- (dd) To co-ordinate with the purchaser of insurance to resolve the claims of a third party for compensation for damage under the insurance liability upon occurrence of the insured event;
- (e) Other obligations as stipulated by law.

Article 19 *Responsibility to provide information*

1. When entering into an insurance contract, an insurer shall be responsible to provide complete information relating to the insurance contract and to explain to the purchaser of insurance the insurance terms and conditions; and the purchaser of insurance shall be responsible to provide to the insurer complete information relating to the subject matter insured. Both parties shall be responsible for the accuracy and truthfulness of such information. An insurer shall be responsible to keep confidential the information provided by a purchaser of insurance.

2. An insurer shall have the right to suspend unilaterally the implementation of an insurance contract and to collect the insurance premium up until the time of suspension of implementation of the insurance contract, upon one of the following acts being committed by the purchaser of insurance:

- (a) Intentionally providing false information with the aim of entering into an insurance contract in order to be paid insurance proceeds or indemnity;
- (b) Failing to fulfil obligations to provide information to the insurer in accordance with article 18.2(c) of this Law.

3. In the case where an insurer intentionally provides false information with the aim of entering into an insurance contract, the purchaser of insurance shall have the right to suspend unilaterally the implementation of the insurance contract; and the insurer must indemnify the purchaser of insurance for any damage arising from the provision of false information.

Article 21 *Interpretation of contracts of insurance*

If an insurance contract contains provisions which are unclear, those provisions shall be interpreted in favour of the purchaser of insurance.”

Article 22 *Void insurance contracts*

1. An insurance contract shall be void in the following circumstances:

- (a) The purchaser of insurance does not have an insurable interest;
- (b) At the time of entering into the insurance contract, the subject matter insured did not exist;
- (c) At the time of entering into the insurance contract, the purchaser of insurance knew that the insured event had already occurred;
- (d) The purchaser of insurance or the insurer was guilty of fraud when entering into the contract of insurance;
- (dd) Other circumstances as stipulated by law.

2. Void contracts of insurance shall be dealt with in accordance with the provisions of the *Civil Code* and the provisions of other relevant laws.

Article 23 *Termination⁴³ of insurance contracts*

In addition to the circumstances for termination of contracts pursuant to the provisions of the *Civil Code*, an insurance contract shall also terminate in the following circumstances:

- 1. The purchaser of insurance no longer has an insurable interest;
- 2. The purchaser of insurance does not pay the insurance premium in full or on time as agreed in the insurance contract, unless otherwise agreed by the parties;

3. The purchaser of insurance does not pay the insurance premium in full within the grace period⁴⁴ as agreed in the insurance contract.

Article 24 *Legal consequences of termination of insurance contracts*

1. In the case of termination of an insurance contract pursuant to the provisions in article 23.1 of this Law, an insurer must refund to the purchaser of insurance that part of the paid insurance premium which corresponds to the remaining duration of the insurance contract, after deducting legitimate expenses relating to the insurance contract;

2. In the case of termination of an insurance contract pursuant to the provisions in article 23.2 of this Law, the purchaser of insurance must continue to pay the full amount of the insurance premium up until the date of termination of the insurance contract. This provision shall not apply to contracts of personal insurance.

3. In the case of termination of an insurance contract pursuant to the provisions in article 23.3 of this Law, an insurer shall remain liable to indemnify the insured person upon occurrence of the insured event during the grace period; and the purchaser of insurance must continue to pay the full amount of the insurance premium up until the end of the grace period as agreed in the insurance contract. This provision shall not apply to contracts of personal insurance.

4. The legal consequences of the termination of an insurance contract in other cases shall be implemented in accordance with the provisions of the *Civil Code* and the provisions of other relevant laws.

Article 42 *Contract of property insurance above value*

1. A contract of property insurance above value means a contract in which the sum insured is greater than the market value of the insured property at the time of entering into the contract. An insurer and a purchaser of insurance may not enter into a contract of property insurance above value.

2. In the case where a contract of property insurance above value is entered into due to the unintentional wrongful act or omission of the purchaser of insurance, the insurer must refund to the purchaser of insurance the amount of paid insurance premium corresponding to the insured sum which exceeds the market value of the insured property, after deducting legitimate related expenses. Upon occurrence of the insured event, the insurer shall only be responsible to indemnify for damage not exceeding the market value of the insured property.

Article 43 *Contract of property insurance below value*

1. A contract of property insurance below value means a contract in which the sum insured is less than the market value of the insured property at the time of entering into the contract.

2. In the case where a contract of property insurance below value is entered into, the insurer shall only be responsible to indemnify in accordance with the ratio of the sum insured to the market value of the insured property at the date of entering into the contract.

Article 46 *Basis of indemnity*

1. The amount of indemnity which an insurer must pay to the insured person shall be determined on the basis of the market price of the insured property at the point of time when

and place where the loss is suffered and on the basis of the actual level of damage, unless otherwise provided in the insurance contract. The cost of determining the market value and the level of damage shall be borne by the insurer.

2. The amount of indemnity which an insurer shall pay to the insured person shall not exceed the amount of the sum insured, unless otherwise provided in the insurance contract.

3. In addition to the amount of indemnity, an insurer must also pay to the insured person the necessary and legitimate expenses of measures for prevention and minimization of loss and the costs arising which the insured person must bear in order to implement instructions of the insurer.

Article 47 *Forms of indemnity*

1. The purchaser of insurance and the insurer may agree on one of the following forms of indemnity: (a) Repair of the damaged property; (b) Replacement of the damaged property with other property; (c) Payment of monetary compensation.

2. If the purchaser of insurance and the insurer fail to agree on the form of indemnity, monetary compensation shall be paid.

3. In the case of indemnity under clauses 1(b) and (c) of this article, the insurer shall have the right to repossess the damaged property after it has been replaced or after full payment of indemnity in accordance with the market price of the property.”

Article 49 *Right of subrogation*

1. Where the wrongful act or omission of a third party causes damage to an insured and the insurer has already indemnified the insured, the insured must pass to the insurer the right to claim recovery of such sum of indemnity from the third party.

2. If the insured person refuses to pass such right to the insurer or does not reserve or abandons the right to make a claim against the third party, then the insurer shall have the right to deduct an amount of indemnity depending on the level of fault of the insured

3. An insurer may not make a claim against a parent, spouse, child or sibling of an insured person to reimburse the sum paid to the insured person, unless such person intentionally caused the loss.”

II. MARITIME CODE 2005

Article 225 *Subject-matter of marine insurance*

A subject-matter of marine insurance may be any pecuniary interest related to maritime adventures, which can be valued in terms of money, including seagoing vessel, seagoing vessel in course of building, cargo, freight, passage money for the carriage of passengers, charter-hire, hire and purchase money, expected profit on cargo, commission, general average costs, obligations arising under civil liability and sums of money secured by vessel, cargo or freight.

Article 226 *Identification of insurable interests*

1. A person with an insurable interest is a person who is interested in a subject-matter of insurance in a sea voyage.
2. A person is interested in a sea voyage when he/she has grounds to prove that he/she has any relation to the voyage or to any subject-matter of insurance at risk in it, in consequence of which such person may benefit by the safety and due arrival of the subject of insurance, or may not benefit by its loss or by damage to it or by the detention of it, or may incur liability in respect of it.
3. The assured must have interest in the subject of insurance at the time of occurrence of the loss though the assured need not be interested in the subject of insurance when the insurance is effected. When the subject of insurance is insured under the “lost or not lost” condition, the assured may recover although the assured may not have acquired that interest until after the loss occurred, unless the assured was aware of the loss and the insurer was not.

Where the assured has no interest in the subject of insurance at the time of occurrence of the loss, he cannot acquire interest by any act or selection after he is aware of the loss.

4 Where the buyer of goods has insured them, the buyer shall have an insurable interest, even though the buyer might have rejected the goods or have treated them as at the seller’s risk, by reason of the latter’s delay in making delivery or otherwise.

Article 233 *The insured sum*

1. Upon concluding a contract of marine insurance, the insured must declare the sum for which the subject of insurance is insured (hereinafter referred to as the insured sum).
2. Where the insured sum as specified in the contract is lower than the insurable value, the insurer shall be liable for losses in such proportions as the insured amount bears to the insurable value, including other expenses under the insurance.
3. Where the insured sum as specified in the contract exceeds the insurable value, the amount in excess of the insurable value shall not be accepted.”

Article 243 *The insurer’s liability to refund*

The insurer shall have to refund to the assured all reasonable and necessary expenses incurred for the purpose of averting the loss or lessening its extent; expenses incurred in the implementation of the instructions of the insurer as provided for in Article 242 of this Code, or expenses incurred for identifying the cause and extent of the loss within the scope of liability of the insurer, and expenses contributed to the general average. These expenses shall be refunded in such proportion as the insured sum bears to the insurable value.

Article 247 *Transfer of the right to recourse*

After having indemnified the insured, the insurer shall have the right to recourse against the person who is responsible for such loss (hereinafter referred to as the third party) within the amount paid. The insurer shall exercise this right in accordance with the provisions applicable to the insured.

Article 248 *The insured's obligations in the recourse against the third party*

1. The assured shall be obliged to provide the insurer with all information, documentation as well as proof and to take necessary measures to enable the insurer to exercise the right to recourse against the third party.
2. Where the assured fails to perform the obligations specified in Clause 1 of this Article or he/she is at fault that makes the insurer's right to recourse unexercisable, the insurer shall be exempt from the payment of the whole indemnity or enjoy a reasonable reduction of the payable indemnity.
3. If the assured has received the indemnity for losses from the third party, the insurer shall be obliged to pay only the difference between the indemnity amount according to the contract of insurance and the amount of money the assured received from the third party.

III. CIVIL CODE 2005

Article 4 *Principle of free and voluntary undertaking and agreement*

The law guarantees the freedom to undertake and agree on the establishment of civil rights and obligations if such undertakings and agreements do not breach matters prohibited by law and are not contrary to social ethics.

In civil relations, parties shall be entirely voluntary and no party may force upon, prohibit, coerce, intimidate or hinder any other party.

All lawful undertakings and agreements shall bind the parties and must be respected by individuals, legal entities and other subjects.

Article 137 *Legal effect of invalidity of a civil transaction*

1. An invalid civil transaction shall not give rise to civil rights and obligations of the parties, or to changes and termination of such rights and obligations as from the time the transaction is entered into.
2. Where a civil transaction is valid, the parties shall restore everything to its original state and shall return to each other what they have received. If restitution cannot be made in kind, it may be paid in money, except where the transacted property, benefits and income which had been received are confiscated in accordance with law. The party at fault must pay compensation for any loss.

Article 138 *Protection of interests of bona fide third parties with respect to invalid civil transactions*

1. Where a civil transaction is invalid but the transacted property is moveable property ownership of which is not required to be registered and such property has already been transferred to a bona fide third party through another transaction, then the transaction with respect to the third party is still valid, except for the case stipulated in article 257 of this Code.

2. Where the transacted property is immovable property, or moveable property ownership of which is required to be registered, and the transacted property has been transferred to a bona fide third party through another transaction, then the transaction in relation to that third party is invalid, except where the bona fide third party received the property via an auction or via a transaction with another party pursuant to a verdict or decision of an authorized State body being the owner of such property but thereafter such person is not the owner of the property as a result of the verdict or decision being amended or rescinded.

Article 181 *Property rights*

Property rights are rights which can be valued in terms of money and may be transferred in civil transactions, including intellectual property rights.

Article 257 *Right to reclaim moveable property, ownership of which is not required to be registered, from a bona fide possessor*

The owner shall have the right to reclaim moveable property, ownership of which is not required to be registered, from a bona fide possessor in a case where such possessor obtained the moveable property through a contract without compensation to a person without the right to dispose of such property. In a case where such contract includes compensation, then the owner has the right to reclaim such moveable property if it was stolen, lost or in other circumstances in which possession of it was obtained contrary to the wish of the owner.

Article 258 *Right to reclaim moveable property, ownership of which is required to be registered, or immovable property from a bona fide possessor*

The owner shall have the right to reclaim moveable property, ownership of which is required to be registered, or immovable property except where a third party is a bona fide possessor of such property through an auction or through a transaction pursuant to a verdict or decision of an authorized State body which made such person the owner of the property but at a later date such person was not the owner of the property due to the verdict or decision being amended or rescinded.”

Article 346 *Mortgages of insured property*

1. Where mortgaged property is insured, the insured sum shall also form part of the mortgaged property.
2. The mortgagee must notify the insurer that the insured property is being mortgaged. The insurer shall pay the insured sum directly to the mortgagee on occurrence of an insured event. If the mortgagee failed to notify the insurer that the insured property was mortgaged, the insurer shall pay the insured sum in accordance with the insurance contract and the mortgagor shall be obliged to make payment to the mortgagee.

Article 577 *Transfers of claims for indemnity*

1. Where a third party is at fault for causing damage to the insured, and the insurer has paid insurance benefits to the insured, the insurer has the right to demand the third party indemnify the insurer for the insurance benefits already paid. The insured must provide the insurer with all necessary information, documentation and evidence of which the insured has knowledge in order to enable the insurer to exercise its right to demand the third party [to indemnify].

2. Where an insured has received monetary compensation for damage from a third party which is less than the amount payable by the insurer, the insurer is only required to pay the difference between the [total] insurance benefits [otherwise payable] and the amount paid by the third party, unless otherwise agreed. If the insured has received insurance benefits but the insurance benefits are less than the damage caused by the third party, the insured has the right to demand the third party indemnify [the insured] for the difference between the insurance benefits and the monetary compensation for the damage.

An insurer has the right to demand the third party indemnify fully [the insurer] for the amount it has paid to the insured.

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ABSTRACT

The principle of indemnity is a root of indemnity insurance. The nature of the principle is that when the insured event occurs, the insureds are entitled to receive compensation equal to the actual loss they have suffered. The indemnity principle is the foundation for the formulation of the other principles in insurance laws, such as the principle of insurable interest and the principle of subrogation. This thesis examines the research questions of “if insureds have suffered an actual economic loss caused by an insured risk, to what extent does the current Vietnamese insurance law on subrogation and insurable interest allow them to be compensated for their loss? And what reforms are necessary to protect the insureds’ rights to obtain full compensation?”

This research has critically examined the application of the two principles (the principle of insurable interest and the principle of subrogation) in connection with the indemnity principle, and argues that the rules of insurable interest and subrogation under Vietnam’s insurance laws to some extent depart from the nature of the indemnity principle. In some circumstances, the provisions governing insurable interest may deprive the insureds of the right to be compensated for the actual economic loss, and may put the insurers into an “all to gain, nothing to lose” position. In addition, there is confusion between the principle of subrogation and the principle of assignment in Vietnamese insurance laws. This confusion may harm the insureds’ rights to obtain full compensation for their actual economic loss.

This thesis concludes that, in order to make the rules of insurable interest and subrogation under Vietnamese insurance laws consistent with the nature of the principle of indemnity, their reform is necessary. Adherence to the indemnity principle will create the backbone for establishing a legal framework for the sustainable development of Vietnam’s property insurance market in which a balance of the rights and interests of insurers and insureds can be achieved.

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**THE UNDERMINING OF THE INDEMNITY PRINCIPLE
- A PLEA FOR A RETURN TO BASICS AND THE REDISCOVERY OF
FULL INDEMNITY IN INSURANCE LAW – A CASE STUDY OF
VIETNAM**

**Submitted in accordance with the requirements for the degree of
Doctor of Philosophy**

by

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