MIB Members' consultation

Terrorism Liabilities

07 February 2018

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1 Introduction/Purpose of this consultation

The purpose of this consultation is to obtain views from MIB members about how the motor insurance market wishes to deal with claims arising from terrorist attacks involving the use of motor vehicles and, in particular, whether any change to the current arrangements should be made. Recent terrorist attacks involving the use of a vehicle have given rise to consideration as to whether such random, unpredictable acts of violence should be borne by the market as a whole (i.e. by the MIB central fund) or by an individual insurer who happens to have insured the vehicle involved, but clearly not for terrorist purposes.

As explained below, where the vehicle used in a terrorist attack is insured, the insurer who has issued a policy of insurance in respect of the use of the vehicle can be liable for the handling and payment of the claims that result. This is due to the wording of the MIB Articles of Association ("the Articles"), specifically Article 75.

The Articles can be altered if a sufficient proportion of members wish a change to be made. A change to the Articles could be made so that individual members are no longer obligated by Article 75 to deal with third party claims arising from the use of a vehicle as part of an act of terrorism, any such claims thereby being dealt with by MIB and funded by the MIB levy.

There is no legal obligation to change the Articles to address this issue but we invite members' views on whether they think a change should be made to tackle the issue in a different way. Once Members' views have been collated, the MIB Board will consider the matter, summarise for Members the conclusions of this consultation, and decide what further steps to take, if any**.**

2 Background

This section explains why Members are currently obliged to deal with and pay third party claims arising from terrorist attacks where death, injury and/or damage to property is caused by the use of a motor vehicle in respect of which there is a policy in place.

2.1 The law and MIB Articles

It is only where third party claims arise from the use of a motor vehicle that current UK law imposes a requirement for there to be insurance to deal with such claims. In the absence of insurance they would fall to be dealt with by MIB as far as the victim is concerned.

Where it can be said that a vehicle has been used as part of a terrorist attack and third party claims arise, it must be ascertained if there was an insurer who provided insurance in respect of the vehicle. Where there is an insurer associated with the vehicle, it is necessary to consider firstly any

obligations on the insurer under the policy, secondly its obligations under the Road Traffic Act 1988 ("the RTA") and then finally its liability under the Articles, principally Article 75.

Starting with policy considerations, although wordings vary by insurer, a common theme is to exclude claims arising from acts of terrorism, but to stipulate that this exclusion does not apply where the RTA requires the insurer to 'cover' the claim. This leads to a consideration of any legal requirements imposed by the RTA on insurers to compensate victims. After all, the insurer will almost inevitably have no contractual liability under the policy to indemnify the terrorist even if, on the face of it, the terrorist was the insured under the policy. It is a fundamental principle of insurance law that a person is not entitled to indemnity under a contract of insurance in respect of his own intentional acts (***Beresford v Royal Insurance (1938) AC 586*** and ***Gray v Barr (1971) 2 QB 554***). This principle has been followed in the authorities concerning motor insurance policies (***Charlton v Fisher (2002) QB 578*** and ***Keeley v Pashen (2004) EWCA Civ 1491***).

So, with no contractual cover, the question then is whether the RTA requires the insurer to deal with the victims' claims.

The RTA sets out 3 key preconditions to an insurer having a liability to meet such third party claims, namely: that-

(1) *"a judgment to which this subsection applies is obtained*" (section 151 (1))

(2) the judgment relates *"to a liability with respect to any matter where liability with respect to that matter is required to be covered by a policy of insurance under section 145"* (section 151 (2)), and

(3) the liability *"is covered by the terms of the policy…to which the certificate relates"* (section 151 (2) (a)).

Precondition 1 is satisfied as soon as the victim obtains judgment against the offender or his estate. This is therefore no barrier to the insurer being liable.

If the judgment relates to a compulsory insurance risk, i.e. is caused by or arises out of the use of a vehicle on a road or other public place (see Appendix A), precondition 2 also provides no barrier to the insurer's liability.

However, the important precondition is precondition 3, namely whether the liability is covered by the terms of the policy. Many policies contain express deliberate act exclusions (excluding the deliberate causing of injury or damage) but, even where the policy wording is silent, it will inevitably only provide cover for liability arising from certain uses of the vehicle specified by the certificate.

In ***EUI v Bristol Alliance (2012) EWCA Civ 1267***, the Court of Appeal accepted that it was lawful for an insurer to limit the permissible uses of a vehicle under the policy and to exclude other types of use. The Court of Appeal considered that such limitations did not contravene section 151. Accordingly, the insurer had no obligation under the RTA to pay the claims.

The EUI decision was subsequently upheld by the Court of Appeal in ***Sahin v Havard (2017) 4 All ER 157***, this being important because it post-dated the European Court's decision in ***Vnuk*** (see Appendix A), the Court of Appeal rejecting an argument that the requirement from ***Vnuk*** to insure all uses consistent with the normal functioning of the vehicle did not mean that the insurer could not seek to limit the insurance to the uses for which the insured sought cover. This is the current law in the UK.

However, the matter does not end there. One then needs to consider the Articles.

All motor insurers are required by law to be a Member of MIB and, as Members, insurers are bound by the Articles. Article 75 requires insurers to deal with, and pay from their own funds, certain 'uninsured' cases provided specific circumstances are fulfilled. These are still uninsured cases (i.e. MIB claims as far as the third party claimant victim is concerned) and are dealt with under the terms of the Uninsured Drivers Agreement.

One of the circumstances where an insurer is Article 75 insurer is where "*the use of the vehicle is other than that permitted by the policy"* (Art 75(2)(a)(1)(iii)). As such, the insurer of the vehicle would be required to handle and pay all the resulting qualifying claims (see Appendix A) in accordance with the Uninsured Drivers Agreement, even though it would have no such liability under its policy or the RTA.

It has long been established in law that a liability arising from criminal use of a vehicle is one which MIB is obliged to satisfy under the Agreements. This is because it is one which is required to be covered by the RTA and is therefore a 'relevant liability' for the purposes of the MIB Agreements (Hardy ***v MIB (1964) 2 QB 745*** and ***Gardner v Moore (1984) AC 548***).

2.2 The MIB Agreements

With specific regard to claims arising out of acts of terrorism, the Untraced Drivers Agreement first introduced an exclusion in 2003 on the understanding that victims would be fully compensated by the State in such cases. The Uninsured Drivers Agreement which came into force in July 2015 then introduced a similar exclusion.

The legitimacy of these blanket, unqualified exclusions was then reviewed in the light of the Judicial Review proceedings brought by RoadPeace against the Secretary of State for Transport in late 2015. As a result of that review, it was then established that, whilst there was State funded compensation available to victims of terror attacks through the Criminal Injuries Compensation Authority (CICA), this scheme was limited in that damages are paid on a tariff basis and are capped, meaning that they can fall short of the damages which could be recovered at common law. This offended the EU law principle of equivalence and the 2009 Consolidated Motor Insurance Directive (2009/103/EC) makes no explicit provision for the Guarantee Fund (MIB) to exclude claims arising from acts of terrorism. Moreover, it was noted that the RTA had never sought expressly to exclude claims arising from terrorist acts. As a result, changes were made to both Agreements removing the terrorism exclusions. These changes came into effect for accidents on or after 1 March 2017.

2.3 Conclusion on legal / Articles position

On the basis of current UK law, an insurer is not liable for qualifying claims arising from acts of terrorism either contractually or under the RTA, but is liable to handle and meet such claims as Article 75 insurer within the framework of the Uninsured Drivers Agreement. These claims trigger a liability upon MIB under the Uninsured Drivers Agreement, a liability which the Articles require the relevant insurer, acting as Article 75 insurer, to meet under the Agreement.

The Articles could be changed if a sufficient proportion of the MIB membership wish to take this step. The change can be made by not less than 75% of the votes cast by the MIB membership in favour of such a change at a General Meeting of members (AGM or EGM) or by a written resolution passed by the MIB members holding not less than 75% of the total voting rights.

3 Actions if change is preferred by a sufficient proportion of Members

In order to change the current situation so that claims arising from the use of a vehicle as part of an act of terrorism are dealt with directly by MIB and funded through the levy, it will be necessary to amend the Articles, specifically the ambit of where an insurer is the Article 75 insurer.

The amendment would be to exclude these cases from the definition of Article 75 insurer. This could be done by excluding liability for claims arising out of an act of terrorism. The Terrorism Act 2000 contains a definition of an act of terrorism which could be adopted by the Articles. If it is decided to proceed with making the necessary changes, the precise wording proposed will be circulated to members in the usual way, but it may be similar to the exclusion which previously appeared in the 2003 Untraced Drivers Agreement and the 2015 Uninsured Drivers Agreement, namely that there would be no liability upon the Article 75 insurer where the claim was caused by or in the course of an act of terrorism within the meaning of section 1 of the Terrorism Act 2000.

The effect of this would be that, notwithstanding the fact that there may be an insurer for a vehicle used to carry out a terrorist attack, the resulting claims (assuming they were judged to be 'arising from the use of the vehicle' – see Appendix A) would be dealt with by MIB and funded by the MIB levy in the same way that all other MIB claims are funded. Therefore there would be an increase in the MIB levy in implementing such a change to the Articles compared to what the MIB levy would be without such a change. (see Section 3.1 below).

Members are asked for their views on whether they would support a change to the Articles to exclude from the liability of the Article 75 insurer claims arising from the use of a vehicle as part of an act of terrorism for events on or after 01 January 2019.

3.1 The Levy

In order to better understand the financial impact on MIB of potential terrorism claims our external actuaries Willis Towers Watson (WTW) have constructed a model simulating insurance losses arising from UK terrorist ramming events and expected payments over a 10 year time horizon.

The scenarios considered were:

1. Event frequency equal to one in each of the ten years
2. Event frequency equal to three in each of the ten years
3. Event frequency equal to one in year one rising to five in year ten

Model Summary

- Events have been split into two categories Type I and Type II.
    - Type I incidents represent standard ramming events for example London Bridge.
    - Type II incidents are much bigger events for example the Nice attack, but would also include hypothetical events such as a vehicle ramming a train.

- For each model run they have simulated the number of Type I and Type II events arising in each year over a 10 year period (assuming the number of events is from a Poisson distribution). The event frequency is perhaps the most important and most judgemental assumption and as such they have presented the results under 3 different scenarios which should provide a useful idea of the range of potential outcomes.

- The model allows for the scenario where there is a surge of terrorist activity over a prolonged period (or conversely, actions taken by the government to reduce the activity over several years).

- For each event they first simulate the number of deaths and total injuries arising from the event. These are simulated reflecting the observed link between the number of deaths and injuries within the historical data.

- Each injury is then deterministically allocated as either minor or catastrophic based on historical data.

- While they have selected a single severity for minor injuries and deaths based on historical MIB data, for catastrophic injuries they further split into size-of-loss bands as a proxy to reflect severity using 3 bands based on MIB data. They make a further adjustment as they expect these events to give rise to a greater proportion of higher severity claims due to the nature of the attack.

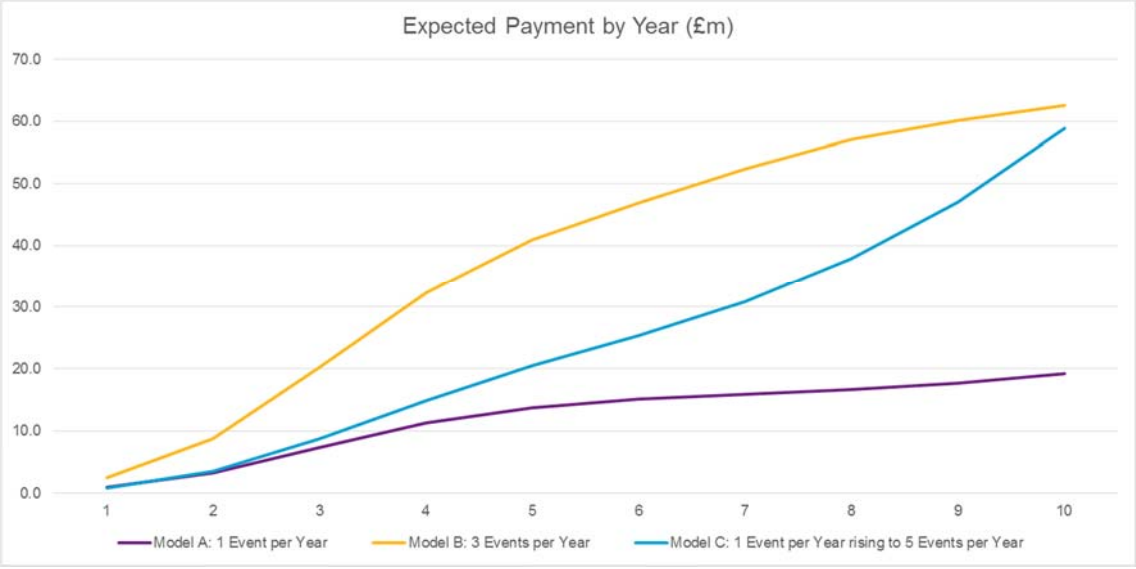
- They also assume a proportion of catastrophic claims will settle as PPOs based on historical MIB proportions. There are factors particular to these type of events that could both increase and decrease PPO propensity and as such it has been left at its actual historic level.

- They then calculate the expected cashflows based on historic expected payment patterns for minor injuries, non-PPO catastrophic claims, fatalities and PPOs and accelerated these payment patterns to allow for factors such as shorter disputes over liability and pressure from claimants / media to make payments more quickly.

- No allowance for reinsurance has been made at this stage.

Model Output

The below graph summarises the key output for these three models in terms of expected amount paid in each of the subsequent 10 years.



The above shows the expected payments for the three models. However, there is an enormous range for each model as is illustrated in the table below in relation to Model B.

Model B – range of payments at various percentiles

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Total
Exp pmt	2.5	8.8	20.2	32.2	41.0	46.9	52.3	57.2	60.2	62.5	383.8
50th	1.6	5.1	11.6	20.4	27.7	32.7	36.6	41.2	43.6	45.8	298.6
80th	3.5	11.9	28.3	45.3	58.3	68.9	75.4	78.8	82.1	86.1	541.6
90th	5.8	19.7	43.3	72.2	85.1	98.8	109.5	114.9	118.2	122.0	714.7
95th	7.9	29.4	65.6	98.6	119.6	128.2	147.3	160.1	153.9	156.4	910.3

Highlighted row is the expected values for Model B as shown in the above graph.

All of the above models are only illustrations. However, it is possible to envisage claims of a type and scale not seen to date that would require funding by the MIB levy as opposed to individual insurers.

In the event that insurers decide to mutualise the terrorism liability, the MIB Board will give further consideration to the mechanism for funding these liabilities in terms of:

- The size of the levy requirement in the first and subsequent years
- The level of any increase in the buffer required to minimise the potential for an additional levy call in any year

3.2 Disputes

If the above change was made to the Articles and a dispute subsequently arises in relation to whether or not a particular incident is to be regarded as an act of terrorism, this would be a dispute "in relation to the interpretation, application or implementation of Article 75" (Art 75(5)) and would, accordingly, fall to be dealt with by the mechanism applicable at the relevant point in time according to the Articles. Currently, that mechanism involves the Technical Committee rules of procedure under Article 75(5) with the limited appeal available to an independent arbitrator under Article 75(6).

The Article 75 Working Group (a sub group of the Technical Committee) has already had preliminary discussions about possible improvements to the dispute resolution process and these discussions will continue during 2018. The scale of the possible claims involved arising from terrorist acts will be factored into the on-going discussions in this area.

Any new proposals in relation to how disputes are dealt with can be put in place by a future change to the Articles if approved by members.

3.3 Competition law considerations

On the basis of legal advice obtained by MIB from our own lawyers and George Peretz QC, we are satisfied that there are no issues relating to competition law or State aid which would result from amending Article 75 in the way described.

This advice was provided to the Directors of MIB in relation to any potential risks to the MIB and its members in pursuing mutualisation. Each individual member may wish to consider whether they want to obtain their own legal advice.

4 Summary of questions

Please provide your views and comments on the following:

1) **Members are asked for their views on whether they would support a change to the Articles to exclude from the liability of the Article 75 insurer, claims arising from the use of a vehicle as part of an act of terrorism for events on or after 01 January 2019.**

2) **If you have answered yes to Question 1, would you prefer the Articles to reflect that MIB would only be responsible for claims over and above a particular level and, if so, the preferred level over and above which MIB would be responsible for paying claims?**

3) **Do you have any further views or comments on the matters discussed in this paper?**

5 How to respond

Please respond to: MIBconsultation@mib.org.uk

All responses to be received no later than 22 March 2018.

6 Appendix A

The concept of the 'use' of a motor vehicle for the purposes of the compulsory insurance requirements of Part VI of the Road Traffic Act 1988 ('the RTA')

Section 145 of the RTA imposes a requirement for a motor insurance policy to insure in respect of death or bodily injury or property damage to a third party *"..caused by, or arising out of, the use of the vehicle on a road or other public place."*

'Use' is inevitably wider than simply driving the vehicle.

There are a number of English authorities concerning the phrase "caused by or arising out of the use…" including ***Dunthorne v Bentley [1999] Lloyds Rep IR 560, Slater v Buckinghamshire County Council [2004] Lloyds Law Reports 432, Axn v Worboys [2012] EWHC 1730, Wastell v Woodward (28th February 2017)*** and ***UK Insurance v R & S Pilling trading as Phoenix Engineering [2017] EWCA Civ 259***. Those cases deal with circumstances in which the activity which was alleged to arise out of the use did not involve the actual driving of the vehicle but was more remotely connected with the use of the vehicle.

The courts have found, for example, that

(a) crossing the road after running out of petrol and causing an accident in the process was use of the fuelless vehicle (***Dunthorne***), and
(b) causing a fire when carrying out repair work on a vehicle in a garage likewise constituted an accident arising from the use of the vehicle being repaired (***Phoenix***).

However, European law is also relevant on the issue of 'use'.

In ***Vnuk v Zararovalnica Triglav (2014) C-162/13,*** the Claimant was stacking bales of hay from a ladder into a barn on a farm in Slovenia when a tractor reversed into the ladder and knocked the claimant from it. The question for the court was whether that liability had to be covered by insurance in circumstances where the accident occurred on private land.

The European Court held that there was no limit to the geographical obligation to insure and that it applied to private land as well as public roads and that the insurance was obliged to cover any use *"…that is consistent with the normal function of that vehicle..".*

More recently, the European Court has held that, whilst the requirement is to insure for any use consistent with the normal function of the vehicle (i.e. following ***Vnuk***), this is only when, at the time of the accident, the principal function of the vehicle was to serve as a means of transport and not, for example, as a machine (***Rodrigues de Andrade v Salvador and others (2017) C514/16***).

In the context of terrorism, it is hard to see how parking a vehicle loaded with a bomb in a street and then remotely detonating the bomb would constitute use consistent with the normal function of the vehicle and accordingly how it could be said that the damage and injury resulting has arisen from the use of a motor vehicle. This is because UK courts, applying ***Marleasing*** principles, will be required to interpret section 145 of the RTA (as far as possible) in a manner consonant with ***Vnuk*** such that the phrase "caused by or arising out of the use of the vehicle" will, where necessary, be construed so as to mean use consistent with the normal function of the vehicle.

On the other hand, where a terrorist drives a vehicle at innocent pedestrians, it may be difficult to argue successfully that this does not involve a use consistent with the normal function of the vehicle (namely the movement of the vehicle), which would fall within the compulsory insurance requirements.

The Westminster Bridge and London Bridge attacks in London in 2017 highlighted how a vehicle might be used by terrorists in a way which fell within the compulsory insurance requirements. They also demonstrated the potential limits to these requirements in that those innocent victims injured or killed after the vehicles had been abandoned but where the terrorists carried on with their attacks on foot might struggle to show that their claims arose from the use of the vehicles.