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India: Trends & Developments

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Trends and Developments

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Developments in Indian Insurance Litigation

Focus of the article

This article deals with an important facet of insurance disputes in India, which is their arbitrability under the existing insurance policies. This has come into focus even more in recent times, given the overall emphasis on using arbitration as a method of resolving commercial disputes in India.

Arbitration is being encouraged to reduce the already overburdened justice delivery system in India. However, the resolution of insurance disputes through arbitration stands out as an exception, given the restricted arbitration clauses in most insurance policies issued in India.

The culprit clause

This issue will be analysed in detail through the lens of the following arbitration clause.

"If any dispute or difference shall arise as to the quantum to be paid under this policy (liability being otherwise admitted) such difference shall independently of all questions be referred to the decision of a sole arbitrator to be appointed in writing by the parties to or if they cannot agree upon a single arbitrator within 30 days of any party invoking arbitration, the same shall be referred to a panel of three arbitrator, comprising of two arbitrators, one to be appointed by each of the parties to the dispute/difference and the third arbitrator to be appointed by such two arbitrators and arbitration shall be conducted under and in accordance with the provisions of the Arbitration and Conciliation Act, 1996.

It is clearly agreed and understood that no difference or dispute shall be referable to arbitration as hereinbefore provided, if the Company has disputed or not accepted liability under or in respect of this policy.

It is hereby expressly stipulated and declared that it shall be a condition precedent to any right of action or suit upon this policy that the award by such arbitrator/arbitrators of the amount of the loss or damage shall be first obtained."

This type of arbitration clause is commonly found in the traditional insurance policies such as fire/material damage, all risks and business interruption. It has also found its way into some of the newer kinds of policies such as liability covers (commercial general liability (CGL), D&O, errors and omissions (E&O), etc). The extent to which this clause has permeated into various kinds of insurance policies means that there is an increasing, albeit mistaken, belief among those buying and selling such policies that issues of liability are not capable of being arbitrated.

Contrast this clause with those found in almost any other commercial agreement where "any dispute" concerning it is capable of being arbitrated. This type of all-encompassing arbitration clause is now the norm across the world, in all types of insurance policies. An indicator of the sensibility of such a wide arbitration clause is that the model arbitration clauses of all leading arbitral institutions (such as the ICC, LCIA, the Singapore International Arbitration Centre (SIAC), the China International Economic and Trade Arbitration Commission (CIETAC), the

Mumbai Centre for Arbitration (MCIA), the Hong Kong International Arbitration Centre (HKIAC) and the American Arbitration Association (AAA)) assume that parties would not want to restrict the kinds of disputes concerning their contracts from being referred to arbitration.

Analysis of the clause

On a plain reading, the clause extracted above is problematic. Its overall significance is that only "quantum" disputes are arbitrable.

The first paragraph of the clause requires that, to be able to arbitrate, the insurer must have "otherwise admitted" its liability for the claim.

The second paragraph inserts two more yardsticks and says that a dispute is not arbitrable if the insurer has "disputed" or "not accepted" its liability. It suggests that even if the insurer is quiet on the issue of its liability (ie, it has neither accepted nor rejected liability), the dispute would not be arbitrable under the clause.

Where an insurer resists arbitration on the basis that the clause is not triggered, the insured has the option to approach the court under Section 11 of the Arbitration Act to seek the appointment of an arbitrator. The scope of the court's enquiry in such cases is limited to considering the existence of an arbitration clause (see Vidya Drolia v Durga Trading Corporation 2021; Supreme Court). However, courts have consistently upheld the validity of the restriction in the arbitration clause covering only quantum-related disputes.

Accordingly, where an insurer has rejected liability, courts will not refer parties to arbitrate under such clauses despite the scope of enquiry being limited to the existence of an arbitration clause. This is because in such cases the courts do not consider that the arbitration clause is triggered in the first place (see Oriental Insurance Company Limited v Narbheram Power and Steel Private Limited 2018; Supreme Court).

However, in a recent judgment in the case of Geo Chem Laboratories v United India Insurance (2020; Delhi High Court), the Court appointed an arbitrator even though the insurer had not admitted liability (but had not rejected it either). The Court did so on the basis that the insurer had "not taken a view on the claim one way or the other" despite having an "ample opportunity to a take a final view on the claim".

Reading the second paragraph of the clause, the Court took the view that, since the insurer had not expressly denied liability, it could not be said that it had "disputed or not accepted liability under or in respect of this policy". The court did not return a finding on whether the insurer's failure to take a view was a "deemed acceptance" of liability and left that issue to be decided by the arbitrator under Section 16 of the Arbitration and Conciliation Act 1996 (Arbitration Act).

Such clauses are therefore more flexible than they may seem on a plain reading. When a court is faced with some doubt on the clause's application in a particular situation, it is likely to favour arbitration given the recent attitude leaning towards encouraging arbitration.

Another facet of the elasticity of such a clause in the other direction is where insurers may contend that even if liability for a part of the claim is denied, a dispute concerning that part would not be arbitrable as a "quantum" dispute. Although the overwhelming majority of cases hold that when liability under the "policy" is admitted, the disputes are arbitrable, NR Industries v New India Assurance (2021; Rajasthan High Court) is

a case in which the court refused the appointment of an arbitrator because the insurer had rejected liability for a portion of the claim. A dispute over that portion was not seen as a mere "quantum" dispute by the court.

The last (third) paragraph of this clause is what is commonly known as a "Scott v Avery" clause, deriving its name from a judgment of the House of Lords delivered in the 1850s. Its aim was to encourage arbitration over court litigation as the primary route to resolve disputes. The clause has filtered into Indian insurance policies and has stayed entrenched there, sitting inconsistently with the first two paragraphs that restrict arbitration to only "quantum" disputes.

This creates an anomalous situation where, on the one hand, the first two paragraphs indicate that an insured cannot arbitrate liability-related disputes, but the third paragraph makes it incumbent to first obtain an arbitral award before approaching the courts. Courts have, unsurprisingly, held that in such cases an insured can directly approach the courts irrespective of the language of the third paragraph of this clause, which would be rendered inoperative in case of a rejection of liability. Some such cases were decided in the early to mid-1900s (see for example Eagle Star & British Dominion Insurance Company v Dina Nath 1922; Bombay High Court, and Chiranjiv Lal v Tropical Insurance Co 1952; Punjab & Haryana High Court).

In any event, a Scott v Avery clause is now unnecessary since the Arbitration Act has provisions for referring parties to an arbitration if they try to skip that process and approach the courts directly. The exception to this is where insureds approach the consumer forums, which is possible in spite of the existence of arbitration clauses in policies.

Problems with the clause

The first and foremost problem with such arbitration clauses is that they become the subject matter of unnecessary and avoidable litigation before courts. Parties spend a fair amount of time, and the consequent costs, in just determining whether their dispute should be referred to arbitration. Such litigation is frequently carried all the way to the Supreme Court of India.

As for the Scott v Avery portion at the third paragraph of the clause, it is not only redundant but also has the potential to create confusion that may lead to unnecessary litigation.

Even if a court appoints an arbitrator in limited cases, invariably the issue of arbitrability is left to the arbitral tribunal to decide. This results in applications being made challenging the arbitrator's jurisdiction to hear the matter (under Section 16 of the Arbitration Act), which again take time and costs.

The time and costs spent by parties in simply trying to resolve the issue of arbitrability would certainly be better spent in resolving the actual dispute over the claim, whether it concerns liability or quantum, or both. It defies logic seeing that in relation to all other commercial disputes, parties do not have to contend with such restricted arbitration clauses and the vagaries of litigation to determine arbitrability.

The rationale for such clauses is yet more inexplicable in the current scenario, where the government, courts and all stakeholders have been pushing to decongest the courts in favour of using arbitration as a mainstay of dispute resolution. The reason for this is the high volume of cases pending before the Indian courts. As of August 2022, there were reportedly about 41 million cases pending before the various district

courts, 6 million cases before 25 High Courts, and 70,000 cases before the Supreme Court. As for consumer courts, where the bulk of the insurance cases (frequently involving complicated issues) are filed, there were reportedly some 630,000 cases still pending as of March 2022. It is apparent that it is not feasible for parties to expect a timely resolution of their disputes by litigating before civil or consumer courts.

The question therefore is the following: why are such clauses forcing parties to litigate liability related claims still prevalent in the insurance sector in India? It is, perhaps, out of sheer inertia that these clauses have not been updated.

A straightforward solution

When a dispute arises, the objective of the parties is to resolve it in the most efficient manner. A court proceeding, or a consumer action, is seldom efficient compared with arbitration. The biggest advantage of arbitration under the Arbitration Act is that it is a time bound exercise (12 months from the date of completion of pleadings per Section 29A of the Arbitration Act).

Arbitration also allows parties to appoint arbitrators of their choice considering their experience and expertise in relation to their dispute.

Furthermore, the grounds of challenge to an arbitral award are extremely narrow, so there is a good chance that the dispute would end with the arbitral tribunal's award.

Lastly, there is no bar in law to parties agreeing that they would arbitrate any and all kinds of disputes arising from the insurance policy. It makes no sense in this day and age to leave issues of liability to be decided by courts and restrict arbitration only to quantum disputes.

Clauses along the following lines would address the problem appropriately.

- Any dispute arising out of or in connection with this insurance policy, including any question regarding its existence, validity or termination, shall be referred to and finally resolved by arbitration under the Arbitration and Conciliation Act, 1996.

Parties can make additions to this base clause to address other issues such as the number of arbitrators; methodology of their appointment, seat of arbitration, and provisions as to bearing of cost. Parties can also choose institutional arbitration instead of ad hoc arbitration considering the growth of many such institutions in India.

Furthermore, parties (mainly the insurer) can also consider adding mediation/conciliation provisions as a step before arbitration.

While permissible under the law, once a dispute has arisen, parties will seldom agree to arbitrate under a fresh arbitration agreement to address issues of liability in addition to quantum. It is therefore imperative to ensure that an all-encompassing arbitration agreement is included in the insurance policy as an efficacious dispute-resolution mechanism.

Insurers and insured would both benefit from a more modern arbitration provision instead of the archaic one frequently used in insurance policies at present. Insurers would not need to unnecessarily carry reserves on disputed claims for a long period of time as is the case when disputes are litigated before courts. Insureds would benefit from a quicker decision on their claims.

Also, the costs regime in arbitrations has recently changed (see Section 31A of the Arbitration

Act) and the winning party can be awarded the costs to be paid by the losing party. This would discourage frivolous claims or defences being pursued by insureds and insurers respectively.

In summary, there are only downsides to a restricted arbitration clause in insurance policies which allows only quantum-related disputes to be arbitrated. Addressing this problem is as simple as changing the arbitration clause in the insurance policies to an all-encompassing one, and there is no reason why this solution should be delayed any further.

Solaris Legal is a boutique Indian law firm focussing on dispute resolution. It was founded in 2021 by three partners: Trinath Tadakamalla, Debarshi Dutta and Mrinal Ojha. With a dedicated and experienced team of lawyers, Solaris offers services to a broad range of clients across the country through its offices in New Delhi and Mumbai and a network of lawyers in various cities. Solaris Legal has an industry-leading practice in the insurance and reinsurance domain, with 14 lawyers working specifically in this practice. Other than insurance and reinsurance, Solaris Legal has a robust practice in the areas of insolvency, oil and gas, construction, infrastructure, and TMT. In the insurance and reinsurance space, Solaris Legal represents some of the largest entities in India and other parts of the world, and often works with overseas firms in advising on domestic and international commercial disputes.

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Trinath Tadakamalla is a partner at Solaris Legal who focuses on insurance and reinsurance, infrastructure, energy, construction and commercial disputes. He is ranked by Chambers as “highly recommended” for insurance and listed in expert guides for “insurance & reinsurance”. He has handled some of the largest insurance disputes in the Indian market. Trinath is also a well-recognised name in the field of commercial arbitrations, and he is experienced in dealing with disputes in various jurisdictions, including the UK, the US and Singapore.

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