

**The Concept of Insurable Interest  
and the Insurance Law Reform Act 1985**

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**I: INTRODUCTION**

The concept of “insurable interest” lies at the heart of insurance law. It is the principal element which distinguishes insurance contracts from mere wagers. However, while it has been recognised as a significant component of insurance law since at least the mid-18th century, its meaning remains uncertain. As recently as 1987, for example, Canadian jurisprudence altered its approach by embracing the “factual expectations” doctrine, rather than the established “strict interest” approach. Both of these views are canvassed in depth later in this article, as is the significance of the Canadian development.

**The Insurance Law Reform Act 1985**

The enactment of the Insurance Law Reform Act 1985<sup>1</sup> (“ILRA”) has the potential to effect a similar change in New Zealand through the operation of ss 6, 7 and 8:

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<sup>1</sup> The Act came into force on 9 August 1985.

**6. Need for insurable interest in life policy abolished** – A contract for assurance on the life of a person is not void or illegal by reason only of the fact that the insured under the contract does not have, or did not have when the contract was entered into, any interest in the life of that person.

**7. Need for insurable interest restricted** – (1) Except as provided in the Marine Insurance Act 1908, no person for whose use or benefit or on whose account a policy of insurance is made is required to have any interest in any event for the purposes of –

- (a) Any contract of indemnity against loss; or
- (b) Any contract of assurance on the life of a person.

(2) Notwithstanding anything in Part IX of the Gaming and Lotteries Act 1977, but subject to subsection (1) of this section, no insurance shall be made by any person –

- (a) On any event whatsoever wherein the person for whose use or benefit or on whose account the policy is made has no interest; or

(b) By way of gaming or wagering.

(3) Every insurance made contrary to subsection (2) of this section is void.

(4) Nothing in this section limits the provisions of the Marine Insurance Act 1908.

**8. Repeal of Life Assurance Act 1774** – As from the commencement of this Act, the Life Assurance Act 1774 (14 Geo. III, c. 48) shall cease to have effect as the law of New Zealand.

To understand the potential change effected, it is useful to examine the concept of insurable interest, the reasons for its requirement in insurance law, and the specific elements which constitute an “insurable interest”. Further assistance may be drawn from a comparative analysis of the concept, including an examination of both the common law and statutory approaches adopted in other jurisdictions.

Finally, the practical effect of the New Zealand reforms will be canvassed. Attention will be focused on *Wijeyaratne v Medical Assurance Society NZ Ltd*,<sup>2</sup> a recent decision of Hillyer J in the High Court at Auckland. This is the only decision dealing with the relevant provisions of the Act, and it may be taken to provide some indication as to the future direction of the concept of insurable interest. The case appears to adopt the factual expectations approach. However, it also introduces a previously overlooked statutory element which may render the requirement worthless in any event: the Contractual Mistakes Act 1977.

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<sup>2</sup> [1991] 2 NZLR 332.

## II: THE REQUIREMENT OF INSURABLE INTEREST

At common law there is no requirement for an interest in any contract. Parties to a contract, be it of insurance or otherwise, are generally permitted to bargain as they like, provided the contract is not immoral, illegal, or contrary to public policy.<sup>3</sup> Indeed, in the absence of gaming and wagering statutes, wagers and bets were enforceable and were enforced by the common law courts.

The requirement of an insurable interest arises from two distinct sources. First, there has traditionally been a statutory requirement for an interest. Second, insurable interest is an inherent feature of indemnity insurance,<sup>4</sup> for it is said that an insured with no interest can suffer no loss. Rather than stemming from any statute, this requirement turns on, and arises out of, the policy concerned. These two sources of the requirement, and the principles that underlie them, will be discussed in turn.

### 1. Traditional Statutory Requirement for Insurable Interest

#### *Insurance law statutes*

A statutory requirement of interest has existed in English law since the enactment of the first Marine Insurance Act in 1745. The policy was extended from marine insurance to other forms of insurance by the deceptively titled Life Assurance Act in 1774. Sections 6, 7 and 8 of the ILRA have repealed the latter Act, and hence removed its significance in relation to a range of insurance policies. The legacy of the Marine Insurance Act 1745 and its statutory interest requirement survives to this day in the Marine Insurance Act 1908, and is a prime example of the statutory requirement of insurable interest.

Marine insurances are clearly contracts of indemnity.<sup>5</sup> Without the requirements of the Marine Insurance Act, the interest requirement would arise from the policy, as it does with other indemnity contracts. The position of the Marine Insurance Act is arguably not affected by the ILRA, as s 7 preserves the separate statutory regime for contracts covered by the Marine Insurance Act.

#### *General statutes*<sup>6</sup>

Wagers were enforceable at common law until 1845, when the Gaming Act

<sup>3</sup> *Fender v St John-Mildmay* [1938] AC 1, 36 (HL) per Lord Wright. See also comments of Roche J in *Williams v Baltic Insurance Association of London Ltd* [1924] 2 KB 282, 288.

<sup>4</sup> See generally *MacGillivray and Parkington on Insurance Law* (8th ed 1988) para 9 and following.

<sup>5</sup> Hardy Ivamy, *Marine Insurance* (3rd ed 1980) 5; *Rickards v Forestal Land, Timber and Railways Co Ltd* [1942] AC 50, 79 (HL) per Lord Wright.

<sup>6</sup> See Merkin, "Gambling by Insurance – A Study of the Life Assurance Act 1774" (1980) 9 AALR 331, 333-337; also *Chitty on Contracts* (26th ed 1989) para 4085 and following.

was introduced in England. Its modern New Zealand equivalent is the Gaming and Lotteries Act 1977. Section 128 of this Act provides that wagering contracts are illegal and void. So strong is the policy against wagering contracts that even relief under the Illegal Contracts Act 1970 is unavailable.<sup>7</sup>

In determining whether a “wagering” contract exists, it is important to remember that the absence of an insurable interest is only one feature.<sup>8</sup> Other elements, such as the mutual intention to wager, are also significant. The mere absence of an interest will not render an insurance policy, or indeed any contract, a wager.<sup>9</sup> The leading dictum is that of Hawkins J in *Carlill v The Carbolic Smoke Ball Co* where he stated:<sup>10</sup>

[A] wagering contract is one by which two persons, professing to hold opposite views touching the issue of a future uncertain 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 [that sum] .... It is essential to a wagering contract that each party under it may either win or lose, whether he will win or lose being dependent on the issue of the event, and, therefore, remaining uncertain until that issue is known.

Consequently, unless the insurance contract is complete speculation on the part of both parties, it will not offend the Gaming and Lotteries Act.<sup>11</sup> That Act is irrelevant in the context of insurance contracts, whether or not they are covered by the ILRA.

## 2. Indemnity Requirement for Insurable Interest

It is a fundamental principle in indemnity insurance that no more than an indemnity is given by the policy. Even when wagering by insurance was possible at common law, judges would frequently try to read these “policies” as ones of mere indemnity and so limit recovery to actual loss suffered.<sup>12</sup>

The common law concept of “indemnity” and the statutory concept of “insurable interest” have been linked. In *Truran Earthmovers Pty Ltd v Norwich Union Fire Insurance Society Ltd*, for example, Bright J of the South Australian Supreme Court stated:<sup>13</sup>

[A]n indemnity policy is one importing the concept of insurable interest as that phrase has been interpreted in the cases.

Although these concepts are separate (and in principle, one need not encompass the other), it is said that unless an insured has an insurable interest, no loss can be suffered. A factual loss can of course be suffered by an insured with no technical

<sup>7</sup> Section 128(3).

<sup>8</sup> Kelly & Ball, *Principles of Insurance Law in Australia and New Zealand* (1991) para 2.33.

<sup>9</sup> *Jackson Securities Ltd v Cheesman* (1986) 4 NSWLR 484.

<sup>10</sup> [1892] 2 QB 484, 490.

<sup>11</sup> See supra at note 8; also *In re London County Commercial Reinsurance Office Ltd* [1922] 2 Ch 67, 78-79.

<sup>12</sup> Supra at note 4, at para 15.

<sup>13</sup> (1976) 17 SASR 1, 9.

insurable interest. The law, however, recognises no loss without an insurable interest.

The difficulties experienced with the rule arise from both the linking of indemnity and insurable interest, and the nature of “insurable interest”. Historically, there was nothing to prevent the policy-based requirement of insurable interest embodying a different meaning to that arising from statute.<sup>14</sup> Practically, however, courts have failed to distinguish between them. As a result, a statutory type of insurable interest has effectively been required.

#### *Reasons for the requirement*

The requirement of an insurable interest is commonly said to be founded on three policy considerations.<sup>15</sup> These are:

- (i) the prevention of insurance in the form of gaming or wagering;
- (ii) the preservation of the indemnity principle; and
- (iii) discouraging the incentive to destroy the property insured.

However, on close examination there is only one principle that lies at the heart of all insurable interest requirements. This principle is identical, whether referred to in the context of the statutory, or the policy requirement of insurable interest. Indeed, it is central to many other concepts and peculiarities of insurance law – it relates to the underlying role of insurance in modern society. Insurance is concerned with protection from risks, and is a form of “hedging” against uncertain events by risk distribution. The requirement that there shall be no profiteering from insurance is fundamental to this role. Many cases illustrate this principle, and it is also essential to related concepts such as contribution, subrogation, and double insurance.<sup>16</sup>

From a more modern perspective, the nature of insurance reflects a restitutionary bias against unjust enrichment in this area of the law.<sup>17</sup> It may even

<sup>14</sup> Supra at note 8, at para 2.31.

<sup>15</sup> See for example Harnett & Thornton, “Insurable Interest in Property: A Socio-Economic Re-evaluation of a Legal Concept” (1948) 48 Col L Rev 1162, 1178-1183; *Kosmopoulos v Constitution Insurance Co* [1987] 1 SCR 2.

<sup>16</sup> See for example the locus classicus of insurance cases, *Castellain v Preston* (1883) 11 QBD 380, 386 (CA) per Brett LJ.

<sup>17</sup> There appears to be a current trend amongst commentators and judges to recognise this principle, or cause of action, and to give restitutionary relief from it. See Goff & Jones, *Law of Restitution* (3rd ed 1987); Birks, *Introduction to the Law of Restitution* (1985); and from a New Zealand perspective, Kos & Watts, *Unjust Enrichment – The New Cause of Action* (New Zealand Law Society Seminar, February 1990). Other concepts in insurance law may be related to this action as well. For example, subrogation (both in insurance and other areas of the law) has been reasoned as a remedy to prevent an unjust enrichment: *Orakpo v Manson Investments Ltd* [1978] AC 95, 104 (HL) per Lord Diplock; *In re TH Knitwear Wholesale Ltd* [1988] Ch 275, 285 (CA) per Slade LJ. Similar comments could be levelled at contribution for double insurance.

show yet another area of the law where the principle of an unjust enrichment is fundamental. Consequently, while insurance law is concerned with reducing risks and spreading loss throughout the community, it is also concerned with restitution – putting people back in the position they would have been in had a loss not occurred.<sup>18</sup>

The requirement that there shall be no profiteering from insurance is fundamental to this role. The strict requirements of the common law are more than adequate to prevent an unjust enrichment being gained from insurers. It is this realization that ultimately underlies the reforms that have occurred.<sup>19</sup>

### *Extent of interest and third parties*

It is not proposed to canvas the full impact of the former Life Assurance Act 1774 on insurance of third party interests. At common law, where a person had a limited interest in the property concerned, but took cover for a third party who also had an interest, the extent and enforceability of the policy depended on the policy itself and the intentions of the parties to it.<sup>20</sup>

The issue frequently arises with goods policies. The leading case is *Tomlinson v Hepburn*.<sup>21</sup> Here a policy on “goods in transit” was held to extend cover to customer-owned consignments, rather than just the plaintiff’s personal liability for goods. It is a question of construction in each case.<sup>22</sup> Borrowdale<sup>23</sup> has suggested that *Tomlinson* is no longer good law in New Zealand. He reaches this conclusion by a literal reading of s 7 of the ILRA. He contends instead that s 4 of the Contracts (Privity) Act 1984 now covers the situation. With respect, it is contended that both these arguments are untenable.

First, Borrowdale’s conclusion depends on an interpretation of the ILRA that cannot be sustained. Section 7 of the Act does nothing to alter the concept of a loss that exists in New Zealand law. A loss for which insurance money can be recovered involves a meaning of indemnity that is historically dependent on insurable interests founded in both factual loss and a legal or equitable relationship to the property concerned. Despite the apparent meaning of s 7 of the ILRA, insurable interest (and *Tomlinson*) is still a relevant concept through the inherent common law meaning of an indemnity.

Second, the application and coverage of s 4 of the Contracts (Privity) Act turns on two elements:

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<sup>18</sup> Supra at note 16.

<sup>19</sup> For comments of Australian Law Reform Commission, see text, infra at pp91-92.

<sup>20</sup> *Chambers v Phoenix Assurance Co Ltd* (1915) 34 NZLR 435.

<sup>21</sup> [1966] AC 451 (HL).

<sup>22</sup> For example, see the recent case of *Guardian Royal Exchange Assurance of New Zealand Ltd v Roberts* [1991] 2 NZLR 106.

<sup>23</sup> Borrowdale, “Insurance Law Reform Acts In Practice (II)” [1987] NZLJ 68, 72; “Insurance Law Reform In New Zealand A Decade On” (1988) 1 ILJ 261.

- (i) the intent of the parties concerned; and
- (ii) the appropriate designation of the third party.

It is suggested that in most insurance cases, with *Tomlinson* being a good example, it is the goods, and not the third party beneficiary, that will be designated. In other words, the requirements of s 4 cannot be made out. Since the Contracts (Privity) Act is expansive of the previous common law, *Tomlinson* and the common law test of intent remain.<sup>24</sup>

#### *Practicalities and the presumption of interest*

The claim of “no insurable interest” by an insurer has never been viewed by the courts as particularly meritorious. Often the insurer has for some time been only too willing to accept the premium on the risk. An insurer proffering the premiums back to the insured and denying liability has never been favourably received by the courts.<sup>25</sup> In *Stock v Inglis*, Brett MR stated:<sup>26</sup>

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. Of course we must not assume facts which do not exist, nor stretch the law beyond its proper limits, but we ought ... to consider the question with a mind ... to find in favour of an insurable interest.

This “presumption of interest”<sup>27</sup> has been cited in a variety of cases where courts faced difficult problems. It has never, however, been taken to its fullest extent so as to allow the lessening of the strict interest requirement.<sup>28</sup>

#### *Absence of insurable interest*

The consequence of a policy with no insurable interest depends largely on the source of the requirement in each case. A policy by way of gaming and wagering, which offends general wagering statutes, is void and illegal.<sup>29</sup> Because of the illegality, the premiums paid cannot generally be recovered by the insured.

By way of contrast, policies which offended the Life Assurance Act 1774, or its modern equivalent (s 7(2) of the ILRA), were and are merely void.<sup>30</sup> Premiums paid can be recovered in an action for money had and received, or in more modern parlance, payment on failed conditions.

<sup>24</sup> For a contemporary example see *Hams Holdings Pty Ltd v Sun Alliance Insurance Pty Ltd* [1986] VR 348.

<sup>25</sup> See *Norwich Union Fire Insurance Society Ltd v Traynor* [1972] NZLR 504, 505.

<sup>26</sup> (1884) 12 QBD 564, 571.

<sup>27</sup> Sutton, *Insurance Law in Australia* (2nd ed 1991) para 6.24.

<sup>28</sup> *Kosmopoulos*, supra at note 15; see also *In re London County Commercial Reinsurance Office Ltd* [1922] 2 Ch 67, 80 per Lawrence J.

<sup>29</sup> Gaming and Lotteries Act 1977, s 128(3).

<sup>30</sup> Life Assurance Act 1774, s 1; ILRA, s 7(3); and Marine Insurance Act 1908, s 5(1).

### III: THE NATURE OF INSURABLE INTEREST

The development of insurable interest requirements stems from English jurisprudence. However, the United States and, more recently, Canada, have subsequently trodden their own path. This has resulted in related, but importantly distinct views as to the elements comprising an insurable interest. Ironically, both views emerged in one of the earliest insurable interest cases, *Lucena v Craufurd*.<sup>31</sup>

#### 1. *Lucena v Craufurd*

*Lucena* concerned insurance taken out by Royal Commissioners on eight Dutch trading ships and their cargoes. The Commissioners' powers, as limited by statute, entitled them to "provide for the disposal of ... ships and effects detained or brought into the ports of [England]".<sup>32</sup> Before the policy was taken out, and while the ships were en route from Asia and Africa to the United Provinces, they were seized in the exercise of the King's prerogative and redirected to England. At this point, Craufurd and the other Commissioners effected insurance over them. The ships were lost on their way to England. It was necessary to determine whether the Commissioners had any insurable interest in the ships. If not, were they insuring them for the benefit of the Crown?

The opinions of the House of Lords in respect of the first count are extremely significant, and have been influential ever since, providing the "substratum of subsequent debate over the nature of an insurable interest".<sup>33</sup>

Lawrence J adopted a broad approach to the concept of insurable interest. As he saw it, anyone with a "moral certainty of benefit" from the continued existence of a thing could insure,<sup>34</sup> irrespective of property considerations.<sup>35</sup> Consequently, in his view:<sup>36</sup>

[W]here a man is so circumstanced ... 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.

Lord Eldon clearly felt uneasy with the concept of a "moral certainty" of benefit or detriment when he stated:<sup>37</sup>

I have in vain endeavoured 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 ...

Effectively, Lord Eldon feared a flood of insurance resulting from an ill-defined

<sup>31</sup> (1806) 2 Bos & Pul (NR) 269; 127 ER 630.

<sup>32</sup> See facts set out in initial hearing (1802) 3 Bos & Pul 75; 127 ER 42.

<sup>33</sup> *Kosmopoulos*, supra at note 15, at 13.

<sup>34</sup> Conversely, a moral certainty of loss from the damage or destruction of the thing.

<sup>35</sup> On the facts, Lawrence J, although differing in the test, agreed on the result: "I know not how to conceive an interest dependant on a thing, with which thing the persons supposed to be interested have nothing to do": supra at note 31, at 306; 644.

<sup>36</sup> Ibid.

<sup>37</sup> Ibid, 321; 650.



concept of “moral certainty”:<sup>38</sup>

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.

These two dicta have formed the basis of insurable interest definitions ever since. It is surprising, however, that Lawrence J’s dicta have received such support, given that his opinion was clearly overruled by Lord Eldon. Indeed, the primacy of Lord Eldon’s view actually took another 120 years to become firmly established in English jurisprudence, for it was not until *Macaura v Northern Assurance Co Ltd*<sup>39</sup> that the “strict interest” requirement<sup>40</sup> was firmly restated by the House of Lords.

## 2. The Strict, Traditional Approach – *Macaura’s Case*

Mr Macaura owned some land on an estate in Ireland. He sold the timber, both felled and standing, to a Canadian company. He also granted a licence to the company to fell timber for one year. In consideration for this, the only shares issued by the company were allotted to Macaura or his nominees. The only assets of the company were the trees and the licence.

After the timber was felled, Macaura contracted for fire insurance with the respondents and four other insurance companies. The timber on the estate was destroyed by fire and Macaura claimed on the policies. At arbitration, and upheld by the Divisional Court, it was decided that the appellant had no insurable interest. On this ground Macaura appealed, first to the Court of Appeal, and then to the House of Lords. Macaura based his ability to insure on two heads – as both creditor and shareholder. The first ground was rejected outright. Their Lordships gave more detailed consideration to the second.

Both Lord Buckmaster<sup>41</sup> and Lord Sumner<sup>42</sup> upheld the strict interest requirement for insurable interest. Macaura was denied recovery. The House of Lords viewed his claim as too uncertain. He should have ensured that the company insured the goods. Alternatively he should have insured the shares, the very property to which he stood in a legal or equitable relationship.

This strict interest rule has also been applied in New Zealand, the leading case being *United Insurance Co Ltd v Black*.<sup>43</sup> That case also concerned a fire policy over goods. The goods were actually sold, while insured by the respondent, to a third party. The property in, and possession of the chattels had passed from the

<sup>38</sup> Ibid, 324-325; 652.

<sup>39</sup> [1925] AC 619.

<sup>40</sup> *Patterson v Harris* (1861) 1 B & S 336; 30 LJ (QB) 354; *Wilson v Jones* (1866) LR 1 Ex 193. Both were distinguished in *Macaura*.

<sup>41</sup> Supra at note 39, at 626-627.

<sup>42</sup> Ibid, 630.

<sup>43</sup> [1940] NZLR 377 (CA).

insured, yet the insurance remained in the name of the respondent. The Court of Appeal held that the insurer was not liable.

### **3. Factual Expectation of Loss**

The “factual expectations” doctrine of insurable interest has developed from the comments of Lawrence J set out above. Under this doctrine, a factual pecuniary loss is viewed as sufficient to support insurance, regardless of the proprietary relationship to the subject matter. It is a view that has generally found favour with the commentators, and one that is set to assume greater importance, due to recent common law and statutory changes in a number of jurisdictions.

Perhaps the classic expression of the doctrine is that of Harnett and Thornton.<sup>44</sup> The authors conclude that this “factual expectation” doctrine is the only basis on which to rest the concept of insurable interest. Their reasons are thoroughly convincing.

### **4. Comparing the Approaches**

In order to maintain the “factual expectation” insurable interest, it is essential to prove that the insured has suffered a factual loss.

The strict interest approach requires the insured to further demonstrate a legally or equitably enforceable right or liability in relation to the property concerned. It is only if this second step is made out that it can be said that an insured has suffered a legally recognisable loss, and hence has an insurable interest.<sup>45</sup>

The factual expectations doctrine undoubtedly provides the modern insurance industry with a better idea of what is, or is not, valid insurance. The strict requirement’s “back-door” manner of avoiding policy liability should be allowed to wane. The reasons commonly advanced in favour of the strict interest requirement are dated, and were perhaps never fully reasoned in any event. The “factual expectation” basis of interest more than adequately serves the policy against recovering more than an indemnity. As will be demonstrated, this view is becoming more widely accepted throughout the common law world.

## **IV: COMPARATIVE APPROACHES TO INSURABLE INTEREST**

The dichotomy of views relating to the nature of insurable interest is reflected to some degree in most common law countries. However, statutory reform and common law developments mean that the “factual expectation” approach is becoming accepted as the correct basis of insurable interest. This change can be best illustrated by examining Canadian and Australian developments.

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<sup>44</sup> Supra at note 15.

<sup>45</sup> See the approach of Clark, *The Law of Insurance Contracts* (1989) para 4-3.

## 1. Common Law – Canadian Winds of Change

The movement away from a strict interest approach can be seen most dramatically in Canada. In 1987 the Supreme Court in *Kosmopolous v Constitution Insurance* overruled the *Macaura* view of insurable interest, and instead embraced the factual expectation doctrine.<sup>46</sup> *Kosmopolous* abruptly altered the entire foundation of Canadian insurance law.

### *Kosmopolous v Constitution Insurance Company*

The Supreme Court of Canada held that it was sufficient to give rise to an insurable interest if a person had a moral certainty of advantage from the survival of the subject matter insured, or a similar chance of detriment from the damage or destruction of the insured property. Hence, the Supreme Court finally embraced the factual expectations doctrine. They attacked the strict rule on five grounds.

First, they held that the rule requiring a “right derivable from property” was inherently uncertain. They consequently favoured Lawrence J’s view of a factual expectation of loss.<sup>47</sup>

The Court also attacked the traditional “floodgates” argument supporting a “strict interest” approach. The Court saw no reason why the insurance industry could not, especially today, calculate such risks and properly insure them without regard to a proprietary interest.

The “factual expectation” view has also been criticised because it causes difficulties in measuring loss. The Supreme Court recognised that in the case of insurable interests:<sup>48</sup>

[the] difficulty of measuring the loss suffered by an individual shareholder should not ... prevent a broadening of the definition of insurable interest.

Moreover, the authority of *Macaura* was questioned. The Supreme Court adopted Keeton’s suggestion that the decision was mainly based on inferences of fraud. This suggestion, coupled with the presumption of insurable interest as expounded in *Stock v Inglis*, were further indicia of the arbitrary harshness of *Macaura* and the inappropriateness of the strict test.

Finally, the Court considered the reasons behind the rule and concluded that these policies supported, if anything, a broader rather than a narrower definition of insurable interest.

<sup>46</sup> Supra at note 15. Prior to this decision Canadian law reflected the conventional learning of the House of Lords in *Macaura*; see *Clark v Scottish Imperial Insurance Co* (1879) 4 SCR 192; *Guarantee Co of North America v Aqua-Land Exploration Ltd* [1966] SCR 133; *Wandlyn Motels Ltd v Commerce General Insurance Co* [1970] SCR 992.

<sup>47</sup> The reasoning on this point, of course, does not go any further to explain just how and why a “moral certainty” standard is any more certain than a “legal” property standard. The Supreme Court of Canada’s reasons are unsupported and equally unconvincing on this point. Lord Eldon’s concerns in *Lucena* are every bit as valid as they ever were.

<sup>48</sup> Supra at note 15, at 19.

As far as the Supreme Court of Canada was concerned, the “reasons advanced in ... favour [of the *Macaura* definition] are not persuasive and the policies alleged to underlie it do not appear to require it”.<sup>49</sup> They embraced the factual expectations doctrine as more certain, realistic, socially beneficial, and more in line with the policies behind the rule. *Kosmopoulos* represents the position currently adopted in Canada.<sup>50</sup>

## 2. Statutory Reforms – Australia

The major federal insurance statute in Australia is the Insurance Contracts Act 1984. The reforms introduced arose from a discussion paper and report published by the Australian Law Reform Commission (“ALRC”) during the early 1980s.<sup>51</sup> Accordingly, the ALRC’s comment regarding insurable interest contains interesting and relevant material.

The ALRC was critical of the *Macaura* case and its “technical rule” which “prevented the insured recovering the loss actually suffered by him”.<sup>52</sup> Reference was made to a contemporary Australian application of the rule, *Truran Earthmovers Pty Ltd v Norwich Union Fire Insurance Society Ltd*,<sup>53</sup> a case illustrating the strict interest requirement of the common law.

The plaintiff wanted to buy a bulldozer that was owned by a third party. It was arranged for sums of money lent by the plaintiff to the vendor to be deducted from whatever price was eventually agreed upon. Because the vendor was unable to afford insurance, the purchaser took out insurance in his own name. The bulldozer was damaged by fire. The purchaser’s claim under the policy was refused, due to lack of insurable interest.

The Supreme Court of South Australia held that there was a simple debtor/creditor relationship between plaintiff and vendor which gave the plaintiff no interest in the vendor’s goods. Although the vendor had suffered a loss, the policy was not stated to be for his benefit, but merely for the benefit of the plaintiff. Under the indemnity principle, the plaintiff had suffered no loss for which he might recover.

“Once again” stated the ALRC, “technical rules prevented recovery of an actual loss.”<sup>54</sup> The Committee embraced the factual expectations doctrine, as outlined by Harnett and Thornton, and concluded that legislation should provide that:<sup>55</sup>

... where an insured is economically disadvantaged by damage to or destruction of the insured property, the insurer should not be relieved of liability by reason only that the insured did not have a legal or equitable interest in the property.

<sup>49</sup> Ibid, 30.

<sup>50</sup> See *Scott v Wawanese Mutual Insurance Co* [1989] 1 SCR 1445.

<sup>51</sup> Australian Law Reform Commission, *Insurance Contracts* (1982).

<sup>52</sup> Ibid, 72.

<sup>53</sup> Supra at note 13.

<sup>54</sup> Supra at note 51, at 73.

<sup>55</sup> Ibid.

*Insurance Contracts Act 1984, Part III*

The result of the ALRC recommendations can be found in Part III of the (Australian) Insurance Contracts Act 1984. Section 16 relates to the requirement of insurable interest. It provides:

(1) A contract of general insurance is not void by reason only that the insured did not have at the time that the contract was entered into, an interest in the subject matter of the contract.

Section 17 takes the extra, *necessary* step of redefining the nature of the remaining indemnity interest requirement. It provides:

[W]here the insured under a contract of general insurance has suffered a pecuniary or economic loss by reason that property the subject matter of the contract has been damaged or destroyed, the insurer is not relieved of liability under the contract by reason only that, at the time of loss, the insured did not have an interest at law or in equity in the property.

It is clear from these two provisions that both the requirement of interest (from statute), and the nature of insurable interest (from the nature of indemnity at common law) have been altered.

There has not yet been any judicial consideration of these provisions. However, although the Insurance Contracts Act was not mentioned in *Framar Money Management Pty Ltd v Territory Insurance Office*,<sup>56</sup> O'Leary CJ of the Supreme Court of the Northern Territory clearly adopted the "factual expectation" basis of interest.

### 3. Conclusions

From this brief overview, the evolving nature of insurable interest can be very clearly seen. The changes to the *Macaura* doctrine are derived from two sources: first, the legislature, and second (more innovatively), from the courts. Both show a trend towards the factual expectations doctrine. This doctrine is seen to represent better the interests of certainty, justice and fairness, as well as meeting the policy behind the requirement. It remains to be seen where New Zealand stands in this picture.

## V: NEW ZEALAND LAW – THE INSURANCE LAW REFORM ACT 1985

If one word were required to describe the nature of the ILRA's progress into law, that word (at least in respect of insurable interest) would be "change". From its genesis in the recommendations of a Contract and Commercial Law Reform Committee ("CCLRC") report in 1983, and at every stage of the Bill, the provisions dealing with the concept of insurable interest were constantly revised and altered. This makes it all the more surprising that, in the writer's opinion, the legislature erred in at least three respects.<sup>57</sup>

<sup>56</sup> (1986) 87 FLR 251, 267.

<sup>57</sup> See text, *infra* at pp94-96.

## **1. The Contract and Commercial Law Reform Committee**

The ILRA arose out of recommendations made in a 1983 report entitled "Aspects of Insurance Law (2)". It is important to note that the CCLRC was only concerned with insurable interest requirements for life policies.

## **2. The Parliamentary Progress of the ILRA**

Following its introduction to the House of Representatives in December 1983, the Bill (in the form proposed by the CCLRC) was referred to the Statutes Revision Committee ("SRC"). It would appear that the government was not committed to the CCLRC report or the draft Bill at the time.<sup>58</sup>

The Bill returned to the House in a changed form, after consideration by the SRC. The SRC had extended the abolition of insurable interest to include indemnity policies. This change was drawn from recommendations of the Justice Department, which drew on New South Wales and Australian law reform recommendations. The Department stated in its recommendations:<sup>59</sup>

The argument in favour of this is that under [an indemnity policy] the insured can recover only what he has lost. Therefore there seems little point in also requiring him to have an insurable interest in the property at the time he takes the insurance out. The point would not arise very often, but we do not think insurers should be able to resist claims for losses under indemnity policies simply on the ground that the insured had no interest in the property at the time the contract was made.

Following the 1984 snap election, the Bill lapsed. It was re-introduced by the new Minister of Justice, Geoffrey Palmer, on 6 November 1984. The changes to clause 7 introduced by the SRC were cursorily discussed before the Bill was referred to the Commerce and Energy Committee ("CEC"). On its re-introduction, the Minister simply reiterated the Justice Department recommendations:<sup>60</sup>

[Clause 7] reflects the fact that under an indemnity insurance policy an insured person can recover only the amount he actually loses when property is destroyed or damaged. It is pointless, therefore, to require him also to have an insurable interest in the property when the insurance is taken out.

The comment in the latter sentence is curious indeed. The Minister can only have been referring to the Life Assurance Act requirement of interest, which is necessary at the time the policy is taken out. This is because the common law concept, usually associated with indemnity insurance, is only relevant at the time of loss. Accordingly, it is clear that even at this stage of the reform, the two quite separate requirements were confused.

After six months in Committee, the Bill resurfaced in Parliament on 12 June 1985. In the CEC, only drafting changes were made to clause 7. In particular, the order of the clauses was altered to the form adopted in the current Act. At this

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<sup>58</sup> 455 NZPD 4979 (15 December 1983).

<sup>59</sup> Department of Justice letter to the Chairman of the SRC dated 16 April 1984, at 5 (copy on file with author).

<sup>60</sup> 458 NZPD 1300, 1300-1301 (6 November 1984).

stage, two points are relevant to note.

First, as a result of drafting changes the gaming and wagering mischief was removed in respect of policies covered by s 7(1).

Second, throughout the legislative process, from the Justice Department recommendations to the SRC, to the reintroduction to the House from the CEC, references were made to “contracts of general insurance”.<sup>61</sup> When the report of the CEC was tabled, Mr Jeffries stated that the clause was concerned with the need for insurable interest in “general or non-life insurance”.<sup>62</sup> This clearly illustrates that the ILRA was seen as a comprehensive reform. In truth, there were substantial holes in its coverage.

### 3. The Current ILRA – Problems in Communication?

In submissions to the CEC concerning s 7, the New Zealand Insurance Council commented that the clause would be the subject of speculation which would keep a section of the legal profession happily employed. Whether this has proven to be the case is debatable, but the drafting of s 7 and its coverage leaves much to be desired. There are at least three major criticisms which can be directed at the ILRA.

#### (a) *Simplification or complication?*

The ILRA intended to simplify the law and repeal old and, in the words of one Member of Parliament, “stupid Victorian legislation”.<sup>63</sup> In actual fact, it creates more confusion and complexity than existed previously.

The position with regard to New Zealand insurance law may be summarised as follows:

- (i) An insurable interest is required for marine insurance, and its nature is strictly defined in the Marine Insurance Act 1908. The ambit of the Marine Insurance Act is, however, uncertain in itself. Whereas earlier versions of the Bill clearly indicated that the Marine Insurance Act would apply solely to contracts falling within s 3 of that Act, the ILRA provides that “nothing shall limit” the provisions of the Marine Insurance Act.<sup>64</sup> The precise meaning of this provision and its effect on marine insurance is uncertain. Far from limiting the provisions of the Marine Insurance Act, the ILRA expands the code-like enumeration of interests - that is, if the ILRA is to have the meaning attributed to it by some commentators.<sup>65</sup>

<sup>61</sup> Undoubtedly borrowing from the Australian reforms: see text, *supra* at pp91-92.

<sup>62</sup> 463 NZPD 4765, 4766 (12 June 1985).

<sup>63</sup> GWF Thomson, 455 NZPD 4980-4981 (15 December 1983).

<sup>64</sup> *Supra* at note 8, at para 2.15.

<sup>65</sup> For example, Tarr, “Insurance Law Reform” (1985) 11 NZULR 362; and Borrowdale, *supra* at note 23.

- (ii) Section 7(1)(b) clearly does not require an insurable interest for life insurance. Section 6 further reinforces this policy, although preserving “other reasons” (apart from absence of an interest) for invalidating life insurance policies. Presumably this would include gaming and wagering.<sup>66</sup>
- (iii) Section 7(1)(a) does not require an insurable interest for indemnity insurance. Any “contract of indemnity against loss” will fall under s 7(1)(a), although “indemnity” is not defined by the ILRA. Some contracts can be classified very easily, but can this be said of all contracts? What of valued policies, or those which provide for reinstatement, or replacement, instead of an indemnity measure? In short, the essential question which arises is that of what constitutes a “contract of indemnity against loss”.
- (iv) An insurable interest is required for non-marine, non-life, and non-indemnity policies (including health and personal accident insurances) pursuant to s 7(2). Absence of interest will render the policy void. Problems of insurable interest do not normally arise in the case of such policies. As stated by Hardy Ivamy:<sup>67</sup>

A policy of [such sort] is, in practice, usually effected by the insured in respect of his own bodily safety.

But he continues:<sup>68</sup>

Where ... the insured insures a third person against accident .... the insured must ... have an insurable interest in the safety of the person insured i.e. he must be in such a position that he will suffer pecuniary loss in the event of an accident to the person insured.

At common law, the situations where an insured has a pecuniary interest in a third party are identical for both life and personal accident insurance.<sup>69</sup> By retaining an “insurable interest” requirement in areas such as personal accident insurance, while abolishing it in relation to life insurance, the legislature apparently overlooked the nature of the requirement. Indeed, with the exception of marine insurance – which must be considered in its historic context – there is no valid argument against adopting a common definition for all insurance contracts.

The reform of the ILRA is incomplete and ill-defined. It creates unnecessary categorisation in insurance law which could easily have been avoided.

<sup>66</sup> Quære, however, how this is achieved. Now that the Life Assurance Act is repealed, the only mechanism that makes wagers void and illegal is the Gaming and Lotteries Act, which has problems of its own: see text, supra at pp82-83.

<sup>67</sup> Hardy Ivamy, *Personal Accident, Life, and Other Insurances* (2nd ed. 1984) 4; see also Hardy Ivamy, *General Principles of Insurance Law* (5th ed 1986) 23.

<sup>68</sup> Ibid.

<sup>69</sup> Supra at note 45, at para 3-6; see also supra at note 8, at paras 2.26 and 2.30.



*(b) Gaming and wagering prohibition*

It is questionable whether a policy against wagering is retained by the ILRA. For contracts not covered by s 7(1), the gaming and wagering prohibition in the ILRA applies, and the absence of an insurable interest is sufficient to render a policy void under s 7(3). In addition, the application of the Gaming and Lotteries Act is preserved.

For contracts falling within s 7(1), Part IX of the Gaming and Lotteries Act still applies. It is thus a question of whether the particular insurance policy falls within the ambit of s 128 of the Gaming and Lotteries Act. The difficulties in this area have already been canvassed. The existence of an insurable interest alone is not enough. Other elements are required. The objective question of intention is paramount, as is the requirement that each party must stand to win or lose at the expense of the other.

It is submitted that the requirement of the Gaming and Lotteries Act, when detached from the independent necessity of an interest, loses much of its efficacy.

*(c) Nature of insurable interest for indemnity contracts*

This is, perhaps, the most fundamental criticism of the ILRA. Both Tarr and Borrowdale have stated that the ILRA reforms now open the way for a factual expectation approach to insurable interest in New Zealand law. However, it is submitted that this view cannot be maintained under present law.

First, the ILRA is a statute which impacted on the requirement of insurable interest in a limited number of cases, as set out in s 7(1)(a) and (b). It does nothing to alter the meaning of the terms "insurable loss" or "indemnity". It is illogical to suggest that by abolishing the requirement of insurable interest, one has somehow necessarily effected the nature of an indemnifiable loss.

Second, the requirement of insurable interest arising from the policy is concerned with concepts of indemnity and loss, and is completely different from any statutory requirement of interest. Subsections 7(1) and (2) of the ILRA simply achieve a legislative reversal of the previous Life Assurance Act 1774. The common law, and the concept of indemnification for loss, remain unchanged. In short, the ILRA does nothing to alter the common law position, whereby an insured can suffer no loss without an insurable interest. In order to modify this position, it is preferable to redefine what is meant by "an indemnity" and "an insurable loss", rather than altering the requirement of an insurable interest. Walsh J put the position aptly in *Davjoyda Estates Pty Ltd v National Insurance Co of New Zealand Ltd* when he stated, "[i]t is completely inconsistent with the notion of indemnity that there shall be an absence of [insurable] interest".<sup>70</sup>

The correct approach to reform of this position would be to follow the Australian model. It is clear that only a factual expectation of loss is required in that jurisdiction to enable a recovery.

<sup>70</sup> (1965) 69 SR (NSW) 381, 428.

#### 4. Conclusions

Throughout its lengthy history of reform, the ILRA has achieved its intended objective. It has altered the requirement of insurable interest, and repealed the Life Assurance Act 1774. In its present form it has not altered the concept of an insurable loss, nor the policy-based requirement of insurable interest which arises out of this. It is submitted that *Macaura* is still good law in New Zealand.

Nevertheless, given the uncertain scope of s 7 of the ILRA, and the confusion which must now surround *Macaura* following the Supreme Court of Canada's decision in *Kosmopoulos*, there are clear indications that a New Zealand court might mitigate the harshness of the strict interest requirement where appropriate.

### VI: JUDICIAL CONSIDERATION OF THE INSURANCE LAW REFORM ACT

#### 1. *Wijeyaratne v Medical Assurance Society NZ Ltd*<sup>71</sup>

The plaintiffs, Mr Wijeyaratne (W) and Enayati (E), were young entrepreneurs involved in a pizza delivery venture as partners. To deliver their pizzas they purchased and insured with the defendants two Honda City cars.

W's father, a doctor, was a member of the Medical Assurance Society NZ Ltd, and was consequently entitled to insure with it. Due to the family connection, the defendants accepted and issued policies in the name of the partnership, W alone, and W and E jointly. This case is complicated by the fact that the Society is not a general insurance company, but is only open to its members and their families. Hence, only W was entitled to insure with it. The need for both parties to be named in the insurance policy was, it seems, a factor that weighed strongly with the judge.

At the beginning of 1987, E imported a Corvette sports car from Los Angeles. Import restrictions were such that if he sold the car within two years of its importation, he would be liable to pay additional duty. E did not use the car and garaged it, uninsured, with relatives. W wished to purchase the car, and E and W talked frequently about this possibility. It became "understood" that if E wished to sell the car, W would have the right of first refusal. Furthermore, any further contributions to the partnership by W would be credited to the purchase price.

The Society issued a proposal to insure the car for a value of \$45,000. The policy named W as the insured. The premium of some \$1,400 was paid. Less than a month later, the car was stolen from W's driveway. The insurers denied liability, primarily on the grounds that W had no insurable interest in the car.

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<sup>71</sup> *Supra* at note 2.

*Insurable interest in the case*

The nature of the interest which W held in E's Corvette is unclear. Any interest that he did hold could only have arisen out of either their "understanding" (the basis on which the case proceeded) or, alternatively, on W's numerous bailments of the vehicle (an issue seemingly not considered). Hillyer J did not consider just what "thread" connected W to the car (and whether this was sufficient to found an insurable interest in the car). However, it seems reasonably clear that W did not have a legal or equitable interest in the car, as previously required under New Zealand law. His Honour recognised, however, that W "did have some interest in the car and in the possibility of the car being stolen".<sup>72</sup>

Hillyer J considered the need for insurable interest and set out s 7 in full. In his words, the section is "somewhat puzzling".<sup>73</sup> He stated somewhat unusually:<sup>74</sup>

[The defendant] submitted that here subs (2) prevented Mr Wijeyaratne from being covered by insurance because he had no interest in the Corvette motor vehicle. Subsection (2) however is subject to subs (1), and that provides that a person does not have to have any interest where the contract of indemnity is against loss.<sup>[75]</sup> It would seem that the provision that *the insured can recover only if the loss is proved* <sup>[76]</sup> was thought to be a sufficient safeguard against the need to have an interest, in the case of any contract of indemnity. Presumably that is unequivocal and clear. [Emphasis added.]

His Honour overlooked the significance of the "insurable interest" requirement for indemnity insurance. A concept lying at the very heart of indemnity insurance is that cover is only provided where there is a proven loss. An insurable interest arises out of this requirement. The need to prove loss (or to prove an interest) is unaffected by the ILRA, as it was unaffected by any of the previous statutory requirements. This requirement is central to the very function of the indemnity. If the insured can suffer no loss, there is no interest to be insured.

His Honour concluded that W did have "some interest" in the possibility of the car being stolen.<sup>77</sup> He did not comment as to whether this was an insurable interest, but considered that there was sufficient interest to avoid the application of s 7(2)(b). The logical implication is that W's interest was sufficient to found an insurance, and did amount to an insurable interest.

In the end, Hillyer J "rectified" the contract under s 7 of the Contractual Mistakes Act 1977. Strictly speaking, this renders all of his comments on insurable interest obiter.

<sup>72</sup> Ibid, 340.

<sup>73</sup> Ibid, 339.

<sup>74</sup> Ibid, 340.

<sup>75</sup> Quære: when would a contract of indemnity ever be anything other than against loss?

<sup>76</sup> What Hillyer J means by this "provision" is unclear. There is certainly no provision in the ILRA to this effect. He can only be referring to the requirement that arises out of the nature of the policy, as one of indemnity, to prove loss.

<sup>77</sup> Supra at note 2, at 340.

*Contractual Mistakes Act 1977*

Hillyer J concluded that the contract should be “rectified” under the Contractual Mistakes Act to include both plaintiffs (W and E) as the “insured”. He justified his decision on three grounds, covered variously by s 6(1)(a)(ii) and (iii), although he noted that “all [are] different facets of the same mistaken view of the situation”.<sup>78</sup> The importance of this decision lies in the implication that the requirement of insurable interest was modified in 1977, rather than by the ILRA in 1985.

In his judgment, Hillyer J speaks of “rectifying” the contract to include E as one of the insured. However, in this context the use of the term “rectification” is inappropriate as it does not accurately describe the relief awarded. His Honour did not rectify the contract within the true meaning of the term. Rather, he exercised his broad discretion under s 7(3) of the Contractual Mistakes Act. This is a statutory power to make “orders as [the court] think[s] just”. He did not exercise the Court’s equitable jurisdiction to rectify at all.<sup>79</sup>

The application and use of the Contractual Mistakes Act is misguided, because it obscured the real question which needed to be resolved. Did W have an insurable interest in the car sufficient to enable him to insure it? Was W even required to have such an interest? The application of the Contractual Mistakes Act, and its assumed necessity by both counsel and Hillyer J, merely indicates that W did not have an insurable interest. Furthermore, it perhaps indicates that s 7 does require some “interest” element after all. Both the granting of relief under the Contractual Mistakes Act, and the respective mistakes that were identified by the judge, can be viewed as indications that W could not have made a valid claim, or that W could not have had a sufficient interest in the car. If W was in a position to make a valid claim (or if he did have an interest), there would have been no mistake at all. Consequently, the application of the Contractual Mistakes Act would have been unnecessary.

*The Insurance Law Reform Act 1985*

It is important to note that s 7 of the ILRA should form the foundation for any consideration of problems relating to insurable interest. Hillyer J only cites the ILRA as an apparent afterthought.

Section 7(3) provides that any contracts which are made contrary to subsection (2) are void. However, s 7(2) is subject to s 7(1). Consequently, it is submitted that the section imposes a preliminary requirement. It is necessary to determine whether s 7(1) is applicable. In the event that s 7(1) does not apply, s 7(2) cannot operate to render a contract void.

This analysis must preclude any application of the Contractual Mistakes Act. It should be noted that the Contractual Mistakes Act only applies to valid “con-

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<sup>78</sup> Ibid, 338.

<sup>79</sup> It should be noted that s 5(2)(b) of the Contractual Mistakes Act saves the “law relating to the rectification of contracts”.

tracts". Had W's insurance contravened s 7(3), the contract would have been void. Therefore no relief could have been granted under the Contractual Mistakes Act, as there would have been no contract to which it could apply. Section 2(5) of the Contractual Mistakes Act would not have saved matters either, as this section only deems there to be a contract "where there would be one but for the mistake". Here, we are concerned with another statute which voids the contract *ab initio*.

Returning to the issue at hand, it is submitted that, had the correct approach been taken, the Court would have been forced to consider s 7 fully. This would have made it easier to determine the effect of s 7 on New Zealand insurance law.

In *Wijeyaratne*, it would have been clear to both the Court and the parties that the motor vehicle policy was "a contract of indemnity against loss". On this basis, s 7(1)(a) would have been satisfied and, accordingly, it would have been unnecessary to show an insurable interest.

Having determined that s 7(1) is applicable, the next step would be to quantify the indemnity that the insurer ought to pay. It is at this stage that the practical effect of the ILRA could have been established. There were two views open to the Court.

First, the traditional requirement of a strict legal or equitable relationship to the property could have been reasserted. This approach suggests that W could not have suffered a loss, as he had no legal interest in the car. Unless he was contracting as the agent of E, or had a limited interest of his own that could sustain the policy, the contract would have been valid, but simply worthless. This approach would have confirmed the minimal impact of the ILRA. It is submitted that it would also have resulted in a harsh, albeit correct, result. Relief under the Contractual Mistakes Act would only have been necessary if this approach had been accepted.

Alternatively, the Court could have restricted its examination to the factual requirement of loss. Under this enquiry, a more complex calculation of the value of loss is required, but the issue of insurable interest no longer requires consideration. Once it is established that s 7(1) applies to the policy, a factual loss is sufficient for recovery. The result is fair, and accords with judicial developments in other common law jurisdictions. Indeed, it gives true meaning to the ILRA: a statute that, without such judicial interpretation, still surely remains a mystery.

In *Wijeyaratne*, W's loss could be described as either the loss of the use of the car at the time or, alternatively, the loss of the chance to purchase the car later. However the factual loss is approached, W would have been able to insure. Furthermore, depending on both the wording of the policy and the intention of the parties (applying *Tomlinson*), W could have recovered the full value of the car, holding any excess beyond his own loss (which is likely to have been substantial) on trust for E.

The Court did not adopt either of these approaches. Instead, possibly prompted by inadequate pleading on both sides, Hillyer J chose to "rectify" the contract. Thus, the Court chose to relieve the mistake under which both parties to the contract, and E (a non-party), were suffering.

## 2. The Implications of *Wijeyaratne*

It is submitted that ultimately nothing has been achieved. W has not been given an insurable interest, since arguably he never had one. E has merely been included as an insured on the policy. However, W's name has been retained as an "insured". This is not because of any interest he held in the car, but simply because the presence of his name on the policy is necessary (he being the member of the Society). Once again, however, the relief granted indicates that the judge considered W did not have sufficient interest in his own right to sustain the policy. If he had, the question of mistake would never have arisen.

To return to Hillyer J's decision, and the possible application of the Contractual Mistakes Act, two points should be noted. First, the relief granted by Hillyer J under s 7 (to "rectify" and add E to the policy) is discretionary and depends on the circumstances of each case. The facts of *Wijeyaratne* (and *Kosmopoulos*) involve situations where fairness and justice arguably lie in the granting of such relief, and the consequent "validation" of the insurance contract. In other cases where, for instance, insurance is undertaken without the knowledge of the person with the actual interest, this element is not so evident and, it is suggested, relief would not be so readily forthcoming.

Second, the operation of the ILRA is a further factor to consider. The judgment in *Wijeyaratne* fails to make this clear. The ILRA explicitly prohibits insurance contracts taken out as wagers.<sup>80</sup> While this factor is likely to influence the discretion to award relief, s 7(3) of the ILRA renders all contracts void ab initio. Consequently, issues otherwise arising under the Contractual Mistakes Act would not require consideration, since no contract would exist on which s 6 could operate. A consideration of the ILRA and its effect on each contract must be a preliminary step.

The impact of the Contractual Mistakes Act is significant. The exercise of discretion in the manner illustrated by Hillyer J in *Wijeyaratne* practically removes the importance of insurable interest in circumstances where both parties believe that it exists and contract on that basis.

## 3. Summary

Once "rectified", there was a valid insurance contract. E had an insurable interest in the car (by ownership). W's interest was more intangible. Indeed, he had no enforceable contractual right to the car. His right of first refusal was non-contractual. He may have had an interest as bailee, or licensee, although this is not discussed in the case.

On a factual expectation approach, W undoubtedly had an interest in the car.<sup>81</sup>

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<sup>80</sup> Supra at note 2, at 339-340.

<sup>81</sup> *Kosmopoulos*, supra at note 15; *Scott*, supra at note 50.

He benefited from its continued existence (he had a “right” to drive it whenever he wanted) and he would certainly have been prejudiced by its theft (because there would no longer have been a car which he could use, or in respect of which he could exercise the right of first refusal).

However, it is not clear whether the case signifies that the “factual expectations” doctrine will be applied in the future. It is submitted that *Wijeyaratne* does not embrace this approach at all. The decision to “rectify” the contract under the Contractual Mistakes Act and to include E as an insured suggests that W had no insurable interest. This factor provided the basis of the mistake for which relief was required under s 7.

It is submitted that the decision is unfortunate. The waters of insurable interest in New Zealand, already muddied by the wording of the ILRA, have become murkier still. The introduction of the Contractual Mistakes Act further pollutes the stream.

## VII: CONCLUSIONS

### 1. The Requirement of Insurable Interest

Despite the recent developments, insurable interest in New Zealand continues to arise from two distinct sources, namely the remaining statutory requirements,<sup>82</sup> and the nature of a policy of indemnity. The 1985 reform has not altered this position.

However, the ILRA has altered the relationship between these requirements and the need for an insurable interest in respect of different types of policy. This has resulted in a position of some uncertainty. The distinctions made by s 7 clearly lack sophistication or forethought, and do little to clarify or simplify an area of law which is central to insurance contracts. Indeed, following the repeal of the Accident Compensation Act 1982 and the narrowing of accident cover by the Corporation,<sup>83</sup> there is now the potential for increased disputes in the area of personal accident policies, and increased focus on the problems caused by these oversights.

### 2. The Nature of this Requirement

The nature of insurable interest required by common law has proven to be narrow to the point of injustice. This has been abrogated by statute in Australia and various United States jurisdictions, and has been the subject of an innovative and principled re-examination by the Supreme Court of Canada. The intention underlying New Zealand reforms may have been the same, but in practice a different path has been followed.

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<sup>82</sup> Represented by the ILRA, the Gaming and Lotteries Act 1977, and the Marine Insurance Act 1908.

<sup>83</sup> See Legislation Note, *infra* at p190.

It is submitted that despite assumptions to the contrary, the concept of insurable interest has not been altered by the 1985 reform. The ILRA merely amends previous statutory requirements which existed for a variety of policies. It does nothing to alter the elements which must be proven in order to establish a loss.

Any reform should address the nature of the concept, as well as the requirement of an insurable interest. In effect, the nature of an "indemnity" needs to be redefined to include factual pecuniary losses, irrespective of their link to the property concerned.

### **3. Reforming the Reform**

Suggestions of further reform may seem a little premature, following so closely after the enactment of the ILRA in 1985. As yet there has been minimal judicial consideration of the ILRA, and an appellate court has not yet had the opportunity to examine the crucial provisions. However, by necessity, this paper has focused on the major shortcomings of the ILRA in terms of its coverage and effect. There are potentially two ways in which reform could occur.

First, a New Zealand court of appropriate standing could embrace the factual expectations doctrine of insurable interest over the whole sphere of insurance law. In doing so, it would be following the lead of Canadian and various United States jurisdictions. The court would also be abandoning a rule, the strictures of which have become outdated in the complex environment that modern insurance serves.<sup>84</sup> As the Canadian experience illustrates, the common law provides an appropriate avenue for this reform. Arguably, the ILRA reforms have partially completed this task. A New Zealand court could herald the change, either through a redefinition of the common law, or through an interpretation of the ILRA.

Alternatively, the force for reform could come from the legislature, effecting a statutory alteration to the concept of insurable interest.<sup>85</sup> Such an approach would necessitate clarification as to the objectives of the ILRA reforms. Preferably it would involve a complete restatement of the nature of the interest requirement for indemnity policies.

The history of the ILRA, spanning two governments and three committees, produced reform that is complex, incomplete, and imprecise. Any further reform must be preceded by the identification of clear objectives. Furthermore, it is imperative that those objectives be implemented through a rational, systematic process. Without such safeguards, there is little hope that clearly drafted legislation will ensue. Insurable interest, as a concept at the very heart of insurance

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<sup>84</sup> See Harnett & Thornton, *supra* at note 15, at 1163.

<sup>85</sup> This reform could occur in tandem with other insurance law reforms that are arguably overdue in New Zealand. It might even reflect a trend to codification of important insurance law concepts, embracing those consumer protection mechanisms that have been the focus of modern reforms like the Fair Trading Act 1986 and Motor Vehicle Securities Act 1989. See for example the Australian Insurance Contracts Act 1984.



contracts, deserves a more thorough re-examination in light of its nature and function. Its relationship with the traditional and, it is submitted, worthy aim of preventing profits from insurance, requires a thorough reassessment and examination, as does the role of the concept in today's modern insurance industry.