Disconnected Sprinkler Highlights the Argument for Reform of the Law on Breach of Warranty:

Qayyum Ansari v New India Assurance Ltd.

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A recent case in the Court of Appeal has reignited discussion about the reforms proposed to the law on breach of warranties by the Law Commission of England and Wales. Although the case does not directly address warranties, it touches on issues often raised in the context of criticism of the draconian nature of the remedy for breach of warranty.

In *Qayyum Ansari v New India Assurance Ltd [2009] EWCA Civ 93* the Court of Appeal considered Qayyum Ansari's appeal against the decision at first instance that Ansari's claim under his insurance policy with New India Assurance (NIA) should be dismissed.

On 4 May 2005 Ansari had entered into a 12 month commercial property insurance policy with NIA. The proposal form for the policy stated that the premises were protected by an automatic sprinkler system. The policy itself contained a term which stated:

"This insurance shall cease to be in force if there is any material alteration to the Premises or Business or any material change in the facts stated in the Proposal Form…"

The policy also contained an extension which stated that cover would not be invalidated by act of neglect of which the owner was not aware.
On 7 September 2005 a fire broke out at Ansari's premises, causing considerable damage. At the time the premises were leased to a Mr Asim, who was using them for the purposes of his business. Ansari subsequently made a claim on his insurance, which was rejected by NIA when it became apparent that the automatic sprinkler system installed at the property had not been connected to the mains water supply at the time of the fire.

The Court of Appeal upheld the decision of the court below. The principal issue to be determined was whether the fact stated in the proposal form (that there was a sprinkler system) had changed, and, more importantly, whether this change was a "material change". The Court of Appeal held that the reference in the proposal form to protection by a sprinkler system meant that there had to be a properly functioning sprinkler system, not merely one that was capable of functioning. As Lord Justice Moore-Bick commented:

"to construe the completed form as meaning no more than that they [the premises] were fitted with an automatic sprinkler system which might or might not be functioning would be contrary to common sense."

Although it was conceded that temporarily switching off the sprinkler system would not necessarily mean that the statement in the proposal form ceased to be accurate, in the present case, where the system had been permanently switched off and a filing cabinet had been placed in front of the isolation valve connecting it to the mains supply, there clearly was a change in facts as stated in the proposal form.

Lord Justice Moore-Bick went on to consider whether this change was a material change. In so doing, he stated that in the present circumstances, materiality did not have the same meaning as pre-contractual materiality in the context of non-disclosure or misrepresentation. Rather it had the meaning as set out in the Court of Appeal case of Kauser v Eagle Star

[2000] Lloyd's Rep IR 154. In that case it was held that in order to be material, a change must be such that it altered the nature of the risk insured. Moore-Bick LJ went on to hold that in the present case the change was indeed material, as "turning off the sprinkler system did more than merely increase the risk of damage by fire and constituted a material alteration of the nature of the subject matter of the insurance." As such, the absence of a sprinkler system took the risk "outside that which was in the reasonable contemplation of the parties at the time the policy was issued."

Finally, the Court of Appeal held that on the facts, Ansari had been aware that the sprinkler system was not in operation, and as such could not rely on the extension to cover relating to acts done without the knowledge of the owner of the property.

Relevance to Warranties

The law on warranties as it stands states that a warranty must be complied with exactly, whether or not it is material to the risk or to the loss actually suffered. Upon breach of a warranty, the insurer is automatically discharged from liability from the time of the breach. As such, had there been a warranty as to the existence (and continuing existence) of a sprinkler system in the Ansari case, there would have been no need to discuss, as the Court of Appeal did at some length, whether the change in the proposal form had been a "material change". Indeed, even if the breach of warranty had no bearing on the risk at all, and the claim had been, for example, in respect of losses arising from a burglary, or for losses in respect of a fire which had occurred after the sprinkler had been switched back on, it may have been possible for the insurers to refuse cover for breach of warranty.

In the view of many commentators, the English law position on warranties is draconian, and unduly harsh on policyholders. As a result of these criticisms, the Law Commission commenced a review of the law on warranties (as well as various other aspects of insurance law) and published a consultation paper in June 2007. Responses have been received by the Law Commission and it continues to produce Issues Papers on its findings. A draft bill in respect of business insurance contracts is expected sometime in 2010 or 2011.

In relation to warranties found in business insurance contracts, two key changes have been proposed. The first proposal is that a new default rule should apply (although the default position can be contracted out of by the parties) such that a business would be entitled to be paid a claim even if there had been a breach of warranty, "if it could prove, on the balance of probabilities, that the breach in question had not contributed to the loss". The second proposal suggests that the remedy for a breach of warranty should be altered so that upon a breach of warranty an insurer will have the option to terminate the contract, but only if the breach has "sufficiently serious consequences to justify termination". It is unclear at this stage exactly how the proposed changes to the law would be interpreted by the courts. However, it would appear that the new rules could very well produce a test very similar to the test for materiality as set out by the Court of Appeal in the Ansari case.