Neutral Citation Number: [2024] EWCA Civ 547

Case No: CA-2022-002068

IN THE COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
COMMERCIAL COURT (KBD)
DAVID RAILTON KC (SITTING AS A DEPUTY JUDGE OF THE HIGH COURT)
[2022] EWHC 1995 (Comm)

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 22 May 2024

Before:

LORD JUSTICE ARNOLD
LORD JUSTICE PHILLIPS
and
LADY JUSTICE FALK

- -

Between:

(1) ROYAL & SUN ALLIANCE INSURANCE PLC
(2) INTERNATIONAL GENERAL INSURANCE CO (UK) LIMITED
(3) HDI GLOBAL (formerly HDI Gerling Verzekeringen NV)
(4) TT MUTUAL INSURANCE LTD

Claimants/Appellants

- and -

(1) TEXTAINER GROUP HOLDINGS LIMITED
(2) TEXTAINER LIMITED
(3) TEXTAINER EQUIPMENT MANAGEMENT LIMITED
(4) TEXTAINER EQUIPMENT MANAGEMENT (US) LIMITED
(5) TEXTAINER EQUIPMENT MANAGEMENT (UK) LIMITED
(6) TEXTAINER MARINE CONTAINERS LIMITED
(7) TEXTAINER MARINE CONTAINERS II LIMITED
(8) TEXTAINER MARINE CONTAINERS III LIMITED
(9) TEXTAINER MARINE CONTAINERS IV LIMITED
(10) TEXTAINER EQUIPMENT MANAGEMENT (S) PTE LTD
(11) TEXTAINER EQUIPMENT MANAGEMENT (US) II LLC

Defendants/Respondents

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Peter MacDonald Eggers KC (instructed by **Kennedys LLP**) for the **Appellants**
Christopher Smith KC (instructed by **BDM Law LLP**) for the **Respondents**

Hearing dates: 22 & 23 November 2023

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Approved Judgment

This judgment was handed down remotely at 10.30am on Wednesday 22 May 2024
by circulation to the parties or their representatives by e-mail
and by release to the National Archives

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Lord Justice Phillips:

1. The principal issue on this appeal is whether insurers, who have paid out under excess of loss policies, are entitled to a proportionate share of relevant recoveries subsequently made by the insured, or whether those recoveries are to be applied first to uninsured losses, applying the "top down" approach adopted by the House of Lords in *Lord Napier and Ettrick v Hunter* [1993] AC 713.

The essential facts

2. The respondents ("Textainer") are companies in the Textainer group, one of the largest intermodal container lessors in the world. For the year commencing 1 October 2015 Textainer benefited from a container lessee default insurance programme, consisting of a US$5m retention, a primary policy of US$5m (in excess the US$5m retention) and five excess of loss policies providing cover up to US$80m in excess of the US$5m retention ("the Policies"). The respondents are, or represent, most of the insurers subscribing to the primary policy and the first to third excess policies ("the Insurers").

3. On 31 August 2016 one of Textainer's lessees, Hanjin Shipping Co. Ltd ("Hanjin"), applied to the Seoul Central District Court for receivership, an event entitling Textainer to an indemnity under the Policies against the loss of containers on-hire to Hanjin and not recovered within 183 days, uncollected rental during that period, and the costs of retrieving and/or repairing recovered containers. At that date Hanjin was in possession of about 113,000 of Textainer's containers, held on a mixture of operating leases and finance leases. Hanjin was adjudged to be bankrupt on 17 February 2017, at which date Textainer's losses were assessed as being about US$117.7m. That figure changed over time as all but 8,820 containers were recovered, counterbalanced by increasing costs and lost rental. For the purposes of this appeal, Textainer's total losses are agreed to have been US$101,856,624, of which the net sum of US$478,265 was received from Hanjin Bankruptcy Trustee in early 2019 in respect of container rentals, paid in order to release a vessel arrested by Textainer.

4. The primary policy and the first to fourth excess policies paid out in full and, on 31 December 2018, the claim under the fifth excess policy was settled for US$25.1m (the limit under that policy being US$30m) so that the total sum paid to Textainer was US$75.1m, leaving uninsured losses in the region of US$21m (in addition to the retention of US$5m). As part of the settlement, the rights of subrogation under the fifth excess policy were transferred to Textainer. The rights of subrogation of insurers under the fourth excess policy (providing cover for US$10m) were also transferred to Textainer pursuant to a settlement agreement dated 26 June 2019.

5. In May 2019, at the invitation of Hanjin's Bankruptcy Trustee, Textainer made a claim against Hanjin. By a settlement agreement dated 28 October 2019 Hanjin agreed to pay US$25,886,647.60 to Textainer in respect of its claim relating to operating leases only ("the Hanjin Settlement"). Between November and December 2019 Hanjin's Bankruptcy Trustee paid Textainer US$14,706,880.84 of that agreed sum.

The proceedings

6. In these proceedings the Insurers claimed to be entitled to 39.3% of the sums received or to be received by Textainer pursuant to the Hanjin Settlement (having insured US$40m of Textainer's total loss of US$101,856,624). Textainer resisted the claim, maintaining that it was entitled to retain all recoveries up to a total of US$56,378,359 (being its net loss of US$101,378,359 less the US$40m covered by the Insurers and the US$5m retention).

7. The Insurers' claim was dismissed on 5 October 2022 by David Railton KC, sitting as a deputy High Court judge ("the Judge"), following a trial. In his reserved judgment dated 27 July 2022, the Judge held, in so far as relevant to this appeal, that:

   (i) as a matter of principle, any recoveries made pursuant to the Hanjin Settlement were to be applied on a top down basis, and not on a proportionate basis;

   (ii) in any event, the Insurers had failed to prove, as a matter of fact, that the recoveries made in respect of losses relating to operating leases had been indemnified proportionately or at all by the primary policy and/or the first three excess policies; and

   (iii) this was not a case of under-insurance within section 81 of the Marine Insurance Act, 1906 ("the 1906 Act"), so recoveries were not to be shared *pro rata*, the principle of "averaging" not being applicable.

8. The Insurers were granted permission to appeal that decision, challenging each of the Judge's findings set out above. Textainer opposed the appeal and further contended, by its Respondent's Notice, that even if the principle of averaging applied between the insured tranches of loss and the uninsured, the recoveries should nevertheless be applied "top-down" as between the layers of insurance. As the rights of subrogation in respect of the top two layers had been transferred to Textainer, Textainer submitted that the Judge had in any event been right to dismiss the claim.

The Policies

9. The Judge explained that the detailed structure of the insurance was as follows:

> "22 …. a Primary Policy of US$5m excess a US$5m retention, followed by five excess layers providing cover up to US$85m. The Excess Policies comprised the 1st Excess Policy of US$5m excess US$10m; the 2nd Excess Policy of US$5m excess US$15m; the 3rd Excess Policy of US$25m excess US$20m; the 4th Excess Policy of US$10m excess US$45m and the 5th Excess Policy of US$30m excess US$55m. Losses over US$85m were uninsured"

10. The Policies were governed by English law. Each of the excess policies incorporated the terms of the primary policy, save that the fifth excess policy excluded loss of earnings, a factor in the level of settlement of Textainer's claim in respect of that layer. Each of the excess policies also included a "no drop down" clause, providing that the policy would only ever provide cover for the identified tranche of excess loss, and would not provide cover for the layers below in any circumstances.

11. The primary policy included the following provisions:

> **"SECTION 1 - PHYSICAL DAMAGE & EQUIPMENT RECOVERY**
>
> The Insurers will indemnify the Assured to the extent provided by this policy if Equipment is lost, destroyed or damaged whilst being moved delivered or repositioned or whilst located in Depots or otherwise in store anywhere in the World during the Period of Insurance …
>
> **SECTION 1 – PHYSICAL DAMAGE & EQUIPMENT RECOVERY (continued)**
>
> **EXTENSIONS APPLICABLE TO ON- HIRE EQUIPMENT**
>
> In respect of On-hire Equipment the Insurers will indemnify the Assured to the extent provided by this policy for:
>
> **1. LOST EQUIPMENT AND REPAIR AND ASSOCIATED COSTS**
>
> costs incurred in retrieving and/or repairing Equipment abandoned by the Lessee and outstanding repair costs and/or service charges incurred by the Lessee relating to Equipment incurred or arising from the failure of any Lessee to fulfil their obligations to the Assured for such Equipment and not recovered within 183 days of the Date of Occurrence.
>
> **2. SURVEY, DAMAGE REPAIR AND RE-MARKING COSTS**
>
> repair and re-marking costs including survey and/or inspection charges incurred by the Assured in assessing the extent of damage insured under 1. above …
>
> **3. OUTSTANDING REPAIR COSTS AND SERVICE CHARGES**
>
> repair and/or service charges relating to the Equipment raised by the Assured to the Lessee after the Date of Occurrence which the Assured are unable to collect …
>
> **4. RECOVERY, HANDLING AND DROP-OFF COSTS**
>
> 1. costs and expenses reasonably incurred to recover Equipment to a Specified Location or other premises for repair and/or storage and/or releasing as appropriate and
>
> 2. Equipment handling charges incurred by the Assured or the Lessee which the Assured are unable to collect …

caused by or arising from the failure of any Lessee to fulfil their obligations to the Assured with respect to such Equipment…

SECTION 2 - LOSS OF EARNINGS

The Insurers will indemnify the Assured for uncollected rental and other charges as specified in the lease or conditional sale agreement which:

a) relate specifically to leased Equipment which has not been returned to a Specified Location prior to any Lessee's contractual default, bankruptcy (de factor or de jure), insolvency … during the Period of Insurance and

b) are not received as a direct result of such Lessee's contractual default, bankruptcy (de factor or de jure) … or incurred by the Assured following the Assured serving a Notice of Default upon the Lessee … …

Provided that

…

3) the maximum liability of the Insurers under this Section shall be the lesser of 183 days equivalent charges per unit of Equipment subsequent to the Date of Occurrence or any other Limit specified herein.

GENERAL CONDITIONS

…

POLICY LIMITS

Irrespective of the number of parties claiming under this Policy the total amount payable by the Insurers in respect of all claims arising out of any one Occurrence shall not exceed any applicable Limit of Liability or maximum amount payable specified in the policy or in the whole the Total Sum Insured.

MARINE INSURANCE ACT 1906

Although not every section of this Policy may relate to a marine adventure, all the terms, conditions and warranties of the Marine Insurance Act 1906 shall apply to the insurance under this policy …

GENERAL DEFINITIONS

…

ANNUAL AGGREGATE LIMIT

The maximum amount the Insurers will pay for any claim or series of claims occurring or with Dates of Occurrence during any one annual Period of Insurance…

ANNUAL AGGREGATE LIMIT – SINGLE LESSEE(S)

The maximum amount the Insurers will pay for all claims attributable to any individual Lessee or group of Lessees owned or controlled by a single entity during any one annual Period of Insurance.

ASSURED'S RETENTION The amount of any loss or series of losses arising out of any one Event the Assured will retain before making a claim under this Policy.

CLAIM The aggregate of all losses and damages including all costs and expenses suffered by the Assured resulting from each Occurrence insured hereunder.

DATE OF FINAL CLAIM The date exactly twelve (12) months after the Date of Occurrence or as otherwise may be agreed between the Insurers and the Assured.

DATE OF OCCURRENCE The date of an event which may give rise to a claim recoverable hereunder…

DATE OF PRELIMINARY CLAIM A date not later than six (6) calendar months after the Date of Occurrence when the Assured having submitted written claims to the Lessee … remains unable to recover Equipment and/or amounts due from the Lessee in respect of the period from the Date of Occurrence…

OCCURRENCE Any one occurrence or all occurrences of a series consequent on or attributable to one source or original cause…

TOTAL SUM INSURED The maximum sum payable in the aggregate for all claims arising out of any one Occurrence….

CLAIMS CONDITIONS

…

RECOVERIES

Following the payment of a claim under this policy and in the absence of an indemnity from any other Policy specified herein any sums recovered from any other source whatsoever as or towards payment of the amount indemnified shall be shared between the Insurers and the Assured as follows:

i) all sums shall be allocated to the Insurers until the amount paid under this policy (including costs) has been recovered and

> ii) all further sums shall inure to the benefit of the Assured.
>
> When sums are received as recoveries in respect of amounts indemnified both under this policy and the other policy(ies) specified herein and the recovered sums cannot be clearly assigned to losses indemnified by any specific policy then the recovered sums shall be allocated to the Insurers and such other insurers in the same proportions as each has borne of the total loss.
>
> Once all the insurers' claims payments (including costs) have been [recovered] any further sums recovered shall [inure] to the benefit of the Assured.
>
> This Condition shall not apply when recovered sums have been assigned to losses sustained and indemnified by a specific policy …"

How the issues arise

12. It was common ground that the doctrine of subrogation allows an insurer who has indemnified an insured to "take advantage of any means available to the insured to extinguish or diminish the loss for which the insurer has indemnified the insured": *MacGillivray on Insurance Law* 15th ed. 2022 para 22-001. By reason of that right, any recoveries received by the insured will inure to the benefit of the insurer with a view to diminishing the loss which the insurer has paid and indemnified: *MacGillivray* paras 22-005, 22-067.

13. In the present case, recoveries from the Hanjin Settlement had the effect of reducing Textainer's total losses, but those losses nevertheless remained well above the upper limit of the cover provided by the Insurers. On the face of matters, those recoveries did not therefore engage the Insurers' undoubted right to be subrogated to recoveries made in respect of insured losses. This mirrors the position as it would have been if the recoveries had been made before Textainer had claimed under the Policies: the recoveries would have reduced Textainer's losses, but however those recoveries were allocated, losses would still have exceeded the cover under the Policies when a claim was made.

14. The above approach also reflects that of the House of Lords in *Napier*. In that case Lloyd's names, including members of the Outhwaite syndicate, held stop loss insurance, covering losses made in a year of account above an excess up to a specified limit. The names sustained underwriting losses for 1982 and their claims were met by insurers. The names subsequently recovered damages from the managing agents of the syndicate in respect of the losses. The issues included whether the names were entitled to be fully indemnified against their losses (including in relation to losses below the excess) before the stop loss insurers were entitled to be reimbursed for the sums paid out to the names under the policy. The House of Lords held that the losses should be applied "top down", illustrated by an example in which it was assumed that for the 1982 year of account a hypothetical name suffered a net underwriting loss of £160,000, that the excess was £25,000, and that the limit was £100,000. After the stop loss insurer had paid £100,000 to the name, damages of £130,000 recovered from the managing agents were attributable to the net loss of £160,000 suffered by the hypothetical name. Lord Templeton explained the approach to be taken as follows at p.730A:

> "The problem must, in my opinion, be solved by assuming that the name insured the first £25,000 of any loss and also insured the excess over £125,000 as well as insuring the £100,000 payable under his policy with the stop loss insurers. There would then be three insurance policies as follows: (1) a policy for the payment of the first £25,000 of any loss; (2) a policy for payment of the next £100,000 of any loss; (3) a policy for payment of any loss in excess of £125,000.
>
> When the name suffered a loss of £160,000 the name received £25,000 under the first policy, £100,000 under the second policy and £35,000 under the third policy. The damages payable by Outhwaite were £130,000. The third insurer is entitled to be the first to be subrogated because he only agreed to pay if the first two insurances did not cover the total loss; accordingly the third insurer must be paid £35,000. The second insurer is entitled to be the second to be subrogated because he only agreed to pay if the first insurance cover proved insufficient; accordingly the second insurer must be paid £95,000. The sum of £35,000 payable by way of subrogation to the third insurer and the sum of £95,000 payable by way of subrogation to the second insurer exhausts the damages of £130,000 received by the name from Outhwaite. There is nothing left to recoup to the second insurer the balance of £5,000 out of the £100,000 he paid under his policy. There is nothing left by way of subrogation for the first insurer in respect of the first £25,000 which he agreed to bear.
>
> Under the stop loss insurance the name agreed to bear the first £25,000 loss and any loss in excess of £125,000. In my opinion the name is not entitled to be in a better position than he would have been if he had taken out the three insurances I have mentioned. The name in fact acts as his own insurer for the first £25,000 loss and acts as his own insurer for any loss in excess of £125,000. So the name must pay £95,000 to the stop loss insurers just as he would have been liable to pay £95,000 to the second insurer if he had taken out three policies. In the result, out of the loss of £160,000, the name will have borne the first £25,000 because he agreed with the stop loss insurers that he would bear that loss. The stop loss insurers having paid £100,000 under the policy will receive back £95,000 by way of subrogation."

15. *Napier* was followed and the top down approach was applied by Langley J in *Kuwait Airways Corporation v Kuwait Insurance Co S.A.K* [2000] 1 Lloyd's Rep 252. The Judge helpfully summarised the facts of that case at [87] as follows:

> "The basic facts were that on 2 August 1990 Iraq had invaded Kuwait, and had taken control of the airport where fifteen Kuwait Airways (KAC) planes were situated. Rix J held that KAC's loss was complete on 2 August 1990. Eight of the fifteen aircraft were subsequently recovered by KAC. The insurers had paid KAC US$300m; the scheduled (insured) value of the fifteen aircraft was US$692m, and the scheduled value of the eight recovered aircraft was US$395m. The issue to be decided was whether the recoveries should be applied on

> the top down basis, or shared proportionately between the parties in the proportion 300/692 to insurers, and 392/692 to KAC."

16. Langley J, at p.261, recorded the arguments as follows:

> "KAC's submission is straightforward. The policy limit of US$300m was an aggregate limit. Insurers in fact paid on an aggregate basis. The analogy, following Lord Templeman, is insurance from the ground up to $300m and self−insurance for US$392m excess of US$300m (the agreed value of all the aircraft covered being US$692m). Thus the top down principle itself requires that recoveries be applied first to the "layer" US$392m excess of $300m because the notional insurer (in fact KAC) is "entitled to be the first to be subrogated because he only agreed to pay if (the US$300m) did not cover the total loss." KIC's submission is that each aircraft loss was a separate loss, exemplified by the fact that each had its own agreed value in the policy, the premium was based on that value and indeed of the 15 aircraft concerned three were the property of the government of Kuwait of which one was included in the eight aircraft eventually recovered. Hence, it is submitted, the payment made of US$300m was in effect a payment of 300/692 of the agreed value of each aircraft."

17. Langley J accepted KAC's submissions, stating at p.261 as follows:

> "In my judgment KAC is plainly right on this issue. I do not think there can be any justification for "disaggregating" recoveries where there is an aggregate limit to the indemnity. Moreover the aggregate limit (in the case of one occurrence) applied regardless of the number of aircraft lost or of whether they were the property of KAC or the government. Whether or not there were a number of losses or only one loss (there was certainly only one occurrence) is in my judgment nothing to the point. Once the top down principle applies, I think it provides the answer as KAC submitted.
>
> Moreover that conclusion accords with commercial good sense. Had KAC lost only the 7 aircraft which were in fact destroyed, insurers would unarguably have had to pay up to the limit of the indemnity without any recovery. It would be remarkable if the policy was to be so construed that because KAC lost those 7 aircraft but also 8 (or any other number of) others which were later recovered intact insurers became entitled to a credit of a proportion of the value of the aircraft recovered.
>
> For the same reason I do not think the basic principle that an assured is entitled to a full indemnity for his loss but no more has any impact on this Question, save that if KAC was not to recover the aggregate limit I do not think it could be said to have received a full indemnity for its losses (or loss). The effect of insurers' submission is that the aggregate limit of £300m only applies in limited circumstances (where there are no recoveries) but otherwise is an unpredictable figure depending on recoveries and their value. That is not what I think the policy says and means. It is also arguably inconsistent with the established principle

> that the cause of action for breach of a contract of indemnity accrues at the time of loss."

18. The Insurers contended that the Policies in the present case were distinguishable from the stop loss policies considered in *Napier*. The stop loss policies, they argued, applied to a single (or "unitary") financial loss for a specified period of underwriting accounting ascertainable on a single date, and covered the excess of that loss above a specified amount. In contrast, the Policies did not insure a unitary loss, but covered the physical loss or damage to individual containers and related costs/loss of earnings as and when those losses were incurred, eroding first the retention, then the layers of cover, one by one. *Kuwait Airways*, they argued, was distinguishable because all the losses occurred simultaneously. Alternatively, it was wrongly decided.

19. Therefore, the Insurers submitted, recoveries by Textainer under the Hanjin Settlement were not to be regarded simply as a reduction in the total loss it had sustained (as was necessarily the case in *Napier*), but should be applied to the specific losses suffered by Textainer where it was possible to do so. It was possible to do so in the present case, according to the Insurers, because the Hanjin Settlement was *pro rata* settlement of Textainer's losses in respect of operating leases (being 40% of Textainer's claim in respect of those leases), and it should be inferred that losses in respect of operating leases and finance leases were suffered evenly and regularly over time. The result, the Insurers contend, is that the Hanjin Settlement recoveries should be applied proportionately across the layers, so that 39.3% is payable to them.

20. In order to succeed on that line of argument, the Insurers needed to succeed on both its legal argument that the top down approach was not applicable and its factual argument that the Court should infer that losses under the operating leases and finance leases were suffered evenly and regularly.

21. In the alternative, the Insurers argued that *Napier* could be distinguished because the Policies are marine container insurance, thereby engaging section 81 of the 1906 Act, which provides:

> "Where the assured is insured for an amount less than the insurable value or, in the case of a valued policy, for an amount less than the policy valuation, he is deemed to be his own insurer in respect of the uninsured balance."

22. The Insurers contended that Textainer had underinsured its containers, demonstrated by the fact that its losses exceeded the upper limit of the Policies, with the result that Textainer was deemed to be its own insurer in respect of the uninsured losses. It followed, they said, that the principle of averaging applied, and the losses fell to be shared proportionately between the Insurers and Textainer, as established in *The Commonwealth* [1907] P 216.

The legal issue: whether the top down principle applied

23. The Judge first expressed the view (at [85]) that the differences between the stop loss policies considered in *Napier* and the Policies were not as "sharp" as the Insurers suggested. Whilst it might well be that payments under the Policies could be connected

to a particular loss and a particular recovery, that was also possible in the case of the stop loss policies in *Napier*.

24. But in any event the Judge did not regard such differences as there were in the formulation or ascertainment of the aggregate loss to be indemnified as undermining the rationale for applying the top down approach in *Napier*, pointing out at [86] that the approach:

> "…was firmly based (in both the House of Lords and the Court of Appeal) on the fact that the excess cover was being provided in respect of aggregate losses. Precisely how the aggregate loss was formulated or ascertained is in this context of less importance. The cover was being provided against a particular layer of loss, and it was the nature of the cover which determined the application of the top down approach. There was no suggestion in *Napier* that how recoveries were to be applied under the general law of subrogation should turn on whether or the not the provisions adopted in the relevant policy permitted (in some or all cases) the possibility of identifying and connecting particular losses, payments and recoveries, or whether in particular cases some or all of the losses, payments and recoveries could in fact (on the available evidence) be so identified and connected."

25. At [87]-[94] the Judge considered *Kuwait Airways* and rejected the Insurers' attempts to distinguish that case on the facts. At [94] the Judge concluded that in *Kuwait Airways*:

> "…the cover provided was aggregate cover, and to be fully indemnified for its loss, the insured was entitled to receive the aggregate limit. As Langley J said, it would be remarkable if the policy were to be construed such that the insurers' position would be materially different if they paid for the loss of just seven aircraft, or the loss of fifteen, and then recovered eight. In each case the insured had suffered a loss of seven aircraft in respect of which it was entitled to be indemnified."

26. The Judge further recorded, at [96] and [97], that the effect of the Insurers' primary case (that recoveries should be applied against losses with which they could be connected), was that insurers on higher layers (whether or not they had paid) would not get the benefit of the reduction in the insured's aggregate loss effected by recoveries applied to the lower layers, or to the insured's retention. The result would also be that the effective limit of aggregate cover provided to the insured would be reduced. The Judge went on to say at [98]:

> "As a matter of principle, this does not seem an appropriate way in which recoveries in relation to an excess of loss (or equivalent) policy such as the present should be dealt with. Nor does it seem consistent with the approach adopted in *Napier* and *Kuwait Airways*. I agree with the learned editors of *Arnould* (at paragraph 31–46) that the top down approach applies in respect of stop loss and excess of loss policies because "*it is in the nature of such policies … that any recovery which may enure to the benefit of insurers by subrogation must be applied top*

> *down … because the very cover provided is against a particular layer of loss*". As Staughton LJ stated in Napier (at [1993] 1 Lloyd's Rep 10; 23), "*When an insurance policy provides for an excess, or is arranged in slices or layers or strata, it seems to me that the "loss against which the policy has been made" is the slice or layer or stratum which the insurer has agreed to bear*". If in any particular case the parties to an excess policy or programme consider that a different approach to the distribution of recoveries is warranted, it would of course be open to them to agree on what that approach should be."

27. The Judge supported his conclusion at [99] by referring to the fact that the Insurers' approach would produce a different result depending on whether recoveries were made before or after payment by the insurers:

> "I also agree with Mr Smith's "reality check": the position both before and after the payment of a claim should be the same, and the effective limit of aggregate cover should not depend on the happenstance of when any particular recovery is made, or whether it can be adequately connected (by one or more of the methods proposed by the Claimants) to a particular loss indemnified by an insurer, or retained by the insured. The top down approach achieves this; the Claimants' suggested approach does not."

28. At [100] the Judge further pointed out that the Insurers' approach would risk Textainer not receiving a full indemnity, contrary to a fundamental principle of insurance law articulated by Brett LJ in *Castellain v. Preston* (1883) 11 QBD 380 at p.386.

29. On this appeal, the Insurers argued that the Judge had failed to recognise the fundamental distinction between the case of a single or unitary loss (such as the net underwriting loss at 36 months in *Napier*) and the case of multiple losses, such as the present case. In the former case, it was plain that subsequent recoveries would reduce that single loss "top down", but where there were multiple losses of different items of property at different times, recoveries in respect of those specific items not only could but must be allocated to the insurer who had indemnified against their loss.

30. The Insurers gave an example of where 1000 containers ("the A containers") were lost and the insurers under the primary policy paid out in respect of that loss, and subsequently a further 1000 containers ("the B containers") were lost and were indemnified under the first excess policy. If there was a later recovery in respect of the A containers, that recovery must be applied to the primary policy, not the first excess policy, because the insurers under primary policy had indemnified against the relevant loss and, applying the basic principle of subrogation, the recoveries in that regard enure to the benefit of the insurer. The insurers under the first excess policy had not indemnified the relevant losses: to pay the recoveries to them on a "top down" basis would be unjustifiable.

31. The Insurers further contended that the fact that the Policies contained provisions providing the period over which losses were recoverable (for example, rental for 183 days after a Date of Occurrence) and for aggregate limits says nothing about the date on which losses actually occur. Neither do they undermine the fact that losses, as they

occur, erode the retention, then the cover under the primary policy and then each excess layer in turn, each loss above the retention being paid by a specific one of the Policies.

32. In my judgment, however, the Judge was right to identify that the true nature of the cover being provided by the Policies was against particular layers of loss, and that the manner in which losses were determined and aggregated in that context was not an important factor. The nature of the cover required that the Policies "pay up and recover down" (as the approach was summarised by Staughton LJ in the Court of Appeal in *Napier*, p. 24). Otherwise, if recoveries were not applied "top down" but proportionately to the insured layers as well as to the uninsured losses above the limit of cover:

    i) Textainer would not be fully indemnified in the amounts for which it was covered under the Policies, contrary to the fundamental principle referred to by the Judge; and

    ii) Textainer would be in a worse position than if the recoveries had been made before the Policies had paid up, contrary to the observation approved by Dillon LJ in the Court of Appeal in *Napier*, p. 21, that the principle "must be exactly the same whether the underwriters have or have not already paid the amount for which they are liable by the time the recovery is achieved".

33. Far from the stop loss policies in *Napier* being distinguishable from the Policies in the present case, providing excess of loss cover, *Arnould: Law of Marine Insurance and Average* 20th ed. para 31-465 regards the application of the top-down principle to those policies as mirroring the position under excess of loss policies:

> "…It is the nature of [stop loss] policies (like excess of loss policies) that any recovery which may enure to the benefit of insurers by subrogation must be applied from the top down (irrespective of the number of layers in the insurance programme), because the very cover provided is against a particular layer of loss (above the excess point and below the limit). Thus, each successive policy attaches only if the overall loss (usually expressed as the ultimate net loss or net ascertained loss; in the case of the stop loss policies, expressed as the net underwriting loss) has exceeded the excess point specified in the policy. Any recovery reduced, pro tanto, the overall loss. The effect of a reduction in the overall loss therefore manifests itself first on the top layer, and then down through successive layers until the effect of the recovery is exhausted…"

34. That approach was taken by Langley J in *Kuwait Airways*, a decision which was neither distinguishable (for the reasons given by the Judge) nor wrong. Indeed, in my judgment it was plainly right, giving KAC the benefit of the cover for which it had bargained and declining to produce a result which would have been different had the eight recovered aircraft not been taken in the first place.

35. In my view the Insurers' argument is based on an overly formalistic and largely theoretical approach to the allocation of individual losses and the notional connection of recoveries to those losses, when no such process or requirement is apparent from the terms of the Policies themselves, nor from the manner in which Textainer and the

Insurers dealt with the claim. As Textainer pointed out, cover is not really provided in relation to containers, most of which will eventually be recovered (as in the present case), even if they are initially treated as giving rise to a constructive total loss after 183 days. The real subject of the insurance is the multiple strands of lost rental, costs and expenses which will be ongoing and intertwined leading up to the date on which they will be ascertained and aggregated. The simplified example of two sets of 1000 containers given by the Insurers does not represent the reality of the cover or the ascertainment of losses.

36. In my judgment, rather than the rigid (and largely theoretical) analysis suggested by the Insurers, a broader approach is required to conform most closely with the underlying rationale of subrogation, as recognised by Rix J in a preliminary decision in *Kuwait Airways*, reported at [1996] 1 Lloyd's Rep 664, 695. That approach, as recognised in the authorities and the leading textbook, is that in the case of excess of loss policies, recoveries should be applied top down.

37. It follows that, largely for the reasons given by the Judge, I would reject the challenge to the application of the top down principle to the recoveries from the Hanjin Settlement.

The factual issue: whether even and regular losses should have been inferred

38. If I am right that recoveries from the Hanjin Settlement fell to be applied "top down" as a matter of principle, the further factual issue does not require determination. Nevertheless, I will briefly set out my reasons why I consider that the appeal would also fail on this issue.

39. The Judge accepted at [102] the Insurers' contention that (if it were to be a relevant exercise to undertake), each individual loss would contribute to the erosion of the retention and then the limits of the primary and excess policies in the chronological order in which it was suffered. The Judge further accepted that it would be a matter for evidence as to when each particular loss was suffered, and that it might, in appropriate cases, be permissible to draw inferences from the available material as to this.

40. After further recognising at [103] that the recovery pursuant to the Hanjin Settlement was in respect of operating lease losses only, the Judge rejected the Insurers' argument that it should be inferred that those losses, and those in respect of finance leases, were all suffered evenly and regularly throughout the relevant period:

> "104…. there are detailed spreadsheets maintained by Textainer, and available to the [Insurers], which provide extensive details of each loss. The spreadsheets were not however in evidence before me, and no attempt has been made by the [Insurers] to identify which particular loss (or group of losses) occurred when. Instead the [Insurers] pointed to the fact that the Hanjin Settlement was in respect of all operating lease losses, and they sought to rely upon a pragmatic assumption that losses in respect of finance leases would have occurred at the same time as, or at least in proportion to, losses in respect of operating leases, with the result that I should proceed on the basis that all losses (under both types of lease) were suffered evenly between the Date of Occurrence and 9 March 2018 (the last date on the Loss Schedule).

> 105. The assumption proposed is one which could make a very material difference to who would benefit (on the [Insurers'] case) from the recoveries made. For example, if a large number of finance lease losses were suffered early on, and before an equivalent number (or amount) of operating lease losses, the recoveries in respect of the operating lease losses might not be attributed at all to the uninsured retention, or to the Primary or 1st Excess Policy. Similarly, if the bulk or all of the early losses were in respect of operating leases, a substantially greater recovery (on the [Insurers'] case) might be due in respect of Textainer's retention, or the Primary or 1st Excess Policy, than currently proposed by the [Insurers].
>
> 106. On the material before me I do not consider that I have enough information to make the assumption proposed. The Hanjin Receivers and Bankruptcy Trustee (and potentially third parties) may have different interests in finance and operating leases respectively, and I do not know, on the evidence provided, whether it can be said with any confidence that finance lease losses in this case tracked the profile of operating lease losses. As the profile of operating lease losses has not in any event been analysed in evidence, it is not known whether or to what extent significant numbers of such losses in fact occurred at the same time (or at the same time as finance lease losses), and as a result, whether or not it can be determined which policy paid what amount in respect of which type of loss.
>
> 107. I agree with Textainer that it was for the [Insurers] to establish the factual premise on which their claim is based, and in my view they have not done so in this respect. This is not a case where the relevant details and evidence are not available to them. On the contrary, they are available, but have not been relied upon for these purposes. Had I agreed in principle with their approach to the distribution of recoveries, I would accordingly have held that it had not been made good on the facts of the present case."

41. The Insurers criticised the Judge for engaging in what they characterised as speculation, the Judge having postulated that there may have been a significant difference between the timing and pattern of losses under the two types of lease when there was no evidence to suggest that was the case. In order to reach the conclusion that it was possible that none of the recovery in respect of the operating leases should be applied against losses covered by the Insurers, the Judge was envisaging a scenario in which almost all the losses in respect of finance leases occurred before the losses in respect of the operating leases. That was unrealistic and should have been discounted as a practical possibility.

42. Whilst accepting that they bore the burden of proof, the Insurers maintained that the starting point should have been a presumption of equality and regularity, a presumption which was not rebutted. Indeed, the Insurers argued that the Schedule submitted to the claim against Hanjin (showing losses as at 16 February 2017) gave support to that assumption, demonstrating that rental income had been lost month by month from September 2016 to February 2017 in respect of both operating leases (totalling just over US$8m) and finance leases (totalling just over US$11m) and that recovery costs (which could not be broken out by month because most units had multiple expenses such as

storage, transport or handling) were comparable over that period (about US$8.5m for operating leases and about US$9.6m for finance leases). The Insurers also asserted that an examination of the spreadsheets would not have assisted in the exercise because they were concerned with quantum of losses, grouped together, not the date losses occurred, but is unclear how that assertion can be accepted given that the spreadsheets were not in evidence below or on this appeal.

43. Contrary to the Insurers' contention, however, there is no presumption that losses occurred evenly and regularly, it being necessary to infer any such pattern from the evidence. The correct approach was explained in *Arnould* para 33-25 as follows:

> "… if the precise dates and ordering of the losses cannot be determined, it may be necessary to infer from the evidence when they have occurred. Although there is no presumption that losses have occurred in regular and consistent fashion, in practice, an inference to that effect may be drawn, so that if losses have occurred over a period of years, it may be appropriate to allocate them on a time on risk basis. Thus in *Municipal Mutual Insurance Ltd v Sea Insurance Co Ltd* [1998] Lloyd's Rep IR 421 the assured faced pilferage claims over a three year period, and these were allocated by the reinsured on the assumption that the losses had occurred equally across the period of coverage, so that they could be allocated on that basis to insurance and reinsurance years of cover. That approach was upheld by the Court of Appeal."

44. In *Municipal Mutual* there was "sparse" evidence available as to when thefts had occurred during the three year period, so the court accepted that, on the balance of probabilities, they had occurred "on a straight line basis". In the present case, in contrast, there was a wealth of material available as to when losses had occurred in the form of the spreadsheets submitted by Textainer and the underlying data. To the extent that such material would have been insufficient for the Insurers to make their case, it was open to them to seek further disclosure on the issue of the timing of the losses suffered.

45. I consider that, where a party with the burden of proof on an issue elects not to adduce available evidence to support its case, the court is entitled to decline to draw inferences which might otherwise have been drawn from the limited material which is adduced in evidence. That may be analysed, as the Judge did in this case, as a failure of the party to establish the factual premise of its case, or it might be viewed as a strong countervailing factor which makes it inappropriate to draw the inference in question. In any event, allowing a party to prove a case by inference, when it has not adduced available evidence on the issue, would encourage parties to mount inferential cases that they know or suspect the evidence, if adduced, would not support, and would risk injustice. I do not say that a Judge could never be persuaded to draw an inference in the absence of evidence that could have been adduced, but I do not consider that the Judge in this case can be criticised for refusing to do so.

46. In any event, the Judge was also entitled to say that he could not discount the possibility that losses on finance leases largely occurred before those in respect of operating leases. Whether there was any relevant distinction between the two types of lease in this regard was a "known unknown". It is plain that Hanjin's Bankruptcy Trustee made some distinction for an unknown reason, as only the claim in relation to operating leases was

settled. Textainer suggested, by way of example, that Hanjin may have abandoned containers on finance leases first due to the capital element in rental payments. Such matters are not simply speculation, but a demonstration that it is not safe to draw the inference proposed by the Insurers.

Conclusion on the application of the top down approach

47. For the above reasons, the Judge was right to hold (subject to the question of averaging addressed below) that Textainer's recoveries from the Hanjin Settlement fell to be applied top down.

Section 81 of the 1906 Act: whether averaging applies

48. The Judge did not doubt the potential distinction between non-marine insurance (as in *Napier*) and marine insurance (arguably effected by the Policies), but gave short shrift to the argument that the present case represented under-insurance for the purposes of section 81 of the 1906 Act. At [95] the Judge stated that the concept of under-insurance:

> "…was not relevant for present purposes in circumstances where the Policies provide excess insurance in respect of particular layers of loss. As Staughton LJ said in the Court of Appeal in *Napier*, after referring (amongst other things) to s.81, Marine Insurance Act, 1906 and The Commonwealth (at [1993] 1 Lloyd's Rep 10; 23-24): "*None of those points seems to me to touch on an insurance effected on a layer, slice or stratum*".

49. The Insurers argued that the Judge had failed to recognise that, whilst structured as layers, the Policies constituted property insurance, just like insurance of a vessel. If losses were suffered in relation to a vessel in excess of the amount for which it was insured, that would constitute under-insurance and the insurer would only to liable for a *pro rata* share of the loss. The same applies, the Insurers submitted, where losses in respect of the containers insured by the Policies exceeded the upper limit of cover. Staughton LJ's comment cited by the Judge was an *obiter* aside, without any analysis, and should not be followed.

50. In my judgment, however, the concept of undervaluation is simply not engaged in relation to layers of insurance. In the case of the insurance of a ship, for example, where the whole vessel is insured and the insurer is liable for any damage it suffers, insurance at less than the value of the ship can readily be seen to be under-insurance by value, exposing the insurer to the same risk (up to the limit of cover) as if the insurer had insured the full value of the vessel. On the other hand, where cover is in relation to a defined portion of loss, the insurance cover by definition matches precisely the value of that which is insured and the insurer is not exposed to a risk greater than the cover provided. Staughton LJ's dictum in the Court of Appeal in *Napier* seems to be a succinct recognition of the above analysis.

51. Further, and as Textainer pointed out, whereas the insurable value of a ship is readily ascertained by reference to section 16(1) of the 1906 Act, insurance which includes the costs of recovery and repair of containers and loss of rental falls within section 16(4) (insurance on any other subject-matter) and insurable value is "the amount at the risk of the assured". In the present case, typical of excess of loss insurance, Textainer's risk

was undefined and indefinite, demonstrating why the principle of averaging is inapposite for excess of loss insurance.

52. As Textainer further pointed out, if averaging due to undervaluation did apply in relation to the Policies, the Insurers would only have been liable for a proportion of the amount of cover they had underwritten in the first place, but they in fact paid in full. The attempt belatedly to introduce the concept of averaging to obtain a proportionate share of recoveries (rather than to deny full liability) is misconceived and further demonstrates the fallacy of the approach in this context.

53. For those reasons I reject the challenge to the Judge's finding in respect of section 81 of the 1906 Act. In view of that conclusion, the issue raised by the Respondent's Notice does not arise for consideration.

Overall conclusion

54. I would dismiss the appeal.

Lady Justice Falk:

55. I agree.

Lord Justice Arnold:

56. I also agree.