Judgment 3/2011

Woodbourne Trustees Ltd v Generali Worldwide Insurance Company Limited
- Royal Court (Civil Action File 993)
- 20th January, 2011

Annuity and life assurance policies – personal placement market - action alleging excess fees charged by insurer – exercise of 'contractual discretion' – whether terms to be implied – judgment in favour of the Plaintiff in respect of monies retained from surrender proceeds – case preparation and need for proper organisation of files.

IN THE ROYAL COURT OF THE ISLAND OF GUERNSEY

The 20th day of January 2011 before Lieutenant Bailiff Richard Southwell QC and Susan Mowbray, Claire Helen Le Pelley and Terrence George Snell, Jurats

WOODBOURNE TRUSTEES LTD

Plaintiff

and

GENERALI WORLDWIDE INSURANCE COMPANY LIMITED

Defendant

Whereas on the 1st, 2nd, 3rd, 4th, 5th, 8th, 9th November 2010 the Court heard the action of the Plaintiff against the Defendant all in accordance with the cause attached hereto and heard thereon Advocates A M Ozanne and J M Wessels counsel for the Plaintiff and Defendant respectively and whereas on 6th December 2010 the Court handed down its decision and whereas on 17th January 2011 the Court considered various ancillary matters including costs, THE COURT this day handed down judgment in the terms attached hereto and ORDERED Judgment in the sum of US$809,102.00

And in respect of the ancillary matters the Court also handed down a supplementary judgment also appended hereto and;

1. ORDERED that the Plaintiff's costs be assessed on an indemnity basis as referred to in paragraphs 11, 19 and 22 of the said supplementary judgment.
2. HELD that Post-Judgment Interest will have to be paid by Generali at the statutory rate of 8% on the costs and disbursements of the Plaintiff as either agreed or ordered by the Court.

3. ORDERED that the £5,000 paid into Court by the Plaintiff as security for Generali's costs together with accrued interest is to be paid out to the Plaintiff's Advocates A O Hall.
4. ORDERED that Generali shall pay 50% of the Plaintiff's costs of and occasioned by the hearing on 17 January 2011.

S M D ROSS
H M Deputy Greffier

Amended Approved Text
20.01.2011

IN THE ROYAL COURT OF THE ISLAND OF GUERNSEY

ORDINARY DIVISION

BETWEEN **WOODBOURNE TRUSTEES LTD** **Plaintiff**

-and-

GENERALI WORLDWIDE INSURANCE COMPANY LIMITED Defendant

Judgment handed down: 6th December 2010

Before Lieutenant Bailiff Richard Southwell QC and
Jurats: E I J S M Mowbray, C H Le Pelley and T G Snell

Advocate for Plaintiff: **A M Ozanne**
Advocate for Defendant: **J M Wessels**

Cases & texts referred to:

Socimer International Bank Ltd (in Liquidation) v Standard Bank London Ltd [2008] EWCA Civ 116; [2008] 1 Lloyd's Rep 558; [2008] Bus. LR 1304; [2008] All ER (D) 331;
Abu Dhabi National Tanker Co v Product Star Shipping Ltd (No. 2) [1993] 1 Lloyd's Rep 397
Ludgate Insurance Co Ltd v Citibank NA [1998] 1 Lloyd's Rep 221
Gan Insurance Co Ltd v Tai Ping Insurance Co Ltd (No. 2) [2001] EWCA Civ 1047; [2001] 2 All ER (Comm) 299
Paragon Finance plc v Nash [2001] EWCA Civ 1466; [2002] 1 WLR 685
Lymington Marina Ltd v Macnamara [2007] EWCA Civ 151; [2007] 2 All ER (Comm) 825
Attorney-General of Belize v Belize Telecom Ltd [2009] UKPC 10; [2009] 1 WLR 1988:
Trollope & Colls Ltd v NW Metropolitan Regional Hospital Board [1973] 1 WLR 601 HL
Investors Compensation Scheme Ltd v West Bromwich Building Society [1998] 1 WLR 896
Reigate v Union Manufacturing Co (Ramsbottom) Ltd et al [1918] 1 KB 592 CA at p.605
The Moorcock (1889) 14 PD 64 CA
BP Refinery (Westernport) Pty Ltd v Shire of Hastings (1977) 180 CLR 266 PC at 282-283
Halsbury's Laws of England, Damages volume
Trans Trust SPRL v Danubian Trading Co Ltd [1952] 2 QB 297; [1952] 1 All ER 970 CA McNair J [1952] 1 KB 285; [1952] 1 All ER 89
Pirito v Curth (2003) CA Judgment 23/2003
Sohail Masood et al v. Mohammad Zahoor et al Royal Court, unreported, 3 November 2006
McGregor on Damages

JUDGMENT

Relevant History

1. A successful and wealthy businessman, Mr Fergus McCann, and his wife Elspeth, were intending to take up residence in the United States of America at the end of 1999. The trustee of their family trusts was The Regent Trust Company Limited of Jersey ("Regent"), which was owned by the partners of the accountancy firm, Ernst and Young ("E&Y"). They also had a financial adviser, Mr Kerr of Kerr Financial Corporation.

2. Through E&Y, Mr McCann was introduced to the Defendant in this action, Generali Worldwide Insurance Company Limited ("Generali"), a Guernsey company which was and is a subsidiary in the large Generali group of companies under the ultimate parent based in Trieste.

3. By 1999, Generali had, with the benefit of major input from E&Y, developed for use in the private placement market for high-worth individuals (especially those moving to the USA to live and work, but intending later to leave the USA and settle elsewhere) a form of single premium deferred variable annuity policy for which Generali expected the market to be limited to no more than 99 individuals. The essential features of such an annuity policy included:

    (i) an individual annuitant whose life would be used to determine the duration of annuity payments involving life contingencies;

    (ii) a single large premium paid to Generali up-front;

    (iii) an account in which the premium (subject to charges) was placed for investment purposes, being held as a separate and segregated account by Generali, but subject to the terms of the contract between Generali and the custodian trustee which held the segregated investments;

    (iv) sub-accounts through which all or part or parts of the account would be invested in funds managed by investment managers, in the choice of which the policyholder would have an involvement (in this aspect there is a contrast with the mass market annuities where the investments are selected solely by the insurance company);

    (v) fees to compensate Generali for (a) mortality and expense risks and distribution and administrative expenses ("Mortality and Expense fees") at an annual rate of 1.25% of the value of each sub-account, and (b) fees for the fund managers (other than Generali) in respect of each sub-account at an annual rate of 0.35% of the value, as well as operating expenses estimated at 0.03% of the value, all such fees being deducted monthly from each sub-account.

4. This form of annuity policy was intended to be an offshore policy with certain potential advantages in relation to US federal and state taxes. If the value of the investments in the sub-accounts increased, as was anticipated, this form of annuity policy was intended to provide an effective means of securing successful long term investment for the policy holder and the annuitant. The policy was described at length in a Private Placement Memorandum prepared by Generali with the help of E&Y as a descriptive offering. In this Memorandum it was stated that E&Y would receive a "formulary fee" in return for E&Y's services in the design and structure of the form of the policy (though the amount was not stated). This formulary fee in fact amounted to 50% of the substantial profit margin Generali derived from the policies.

5. Generali also developed a form of variable life assurance policy which would be available to (amongst others) those entering into the annuity policies. Under these life policies, substantial premiums would be paid over a relatively short period, and the premiums would be invested similarly in sub-accounts. The charges under these life policies would consist of: (a) an annual Mortality and Expense Risk charge of 1% of the sub-accounts values, deducted

monthly; (b) Management Fees at a maximum annual rate of 0.5% of the sub-account values, also deducted monthly; (c) other smaller fees and charges including distribution and administration fees and bank charges; and (d) substantial Cost of Life Assurance Charges based on the 1980 CSO Mortality Rates Table, which were rates based on aggregate mortality records for the US population or part of it, and which, significantly for the present action, did not distinguish between smokers and non-smokers.

6. It was necessary for Regent to enter into an annuity policy before the end of 1999 since Mr and Mrs McCann were moving then to the USA. On 29th December 1999, Regent, as trustee of the Winter Trust, entered into such a single premium variable annuity policy with Generali. This policy is referred to as the "Winter Policy". The Winter Policy provided (inter alia) that:

    (i) the policy owner was the Winter Trust;

    (ii) the annuitant was Mrs Elspeth McCann;

    (iii) the single premium was US$38 million;

    (iv) 100% of the premium was placed in a single sub-account in Generali US$ Reserve (this was subsequently changed, with other sub-accounts being established, including sub-accounts within US Trust which also held investments of the McCann family trusts);

    (v) the maturity date was 10 January 2047;

    (vi) as set out in paragraph 3 above.

7. On 14th March 2000, Regent, as trustee of the Spring Trust, entered into a life policy with Generali. This policy is referred to as the Spring Policy. The Spring Policy provided (inter alia) that:

    (i) the policy owner was Regent as trustee of the Spring Trust;

    (ii) the life assured was that of Mrs McCann (who was a smoker and then 38 years old);

    (iii) there were to be six annual payments of premium, each of US$1,104,433;

    (iv) the sum assured was US$28,903,775;

    (v) the first premium was placed in a sub-account in Generali US$ Reserve, but there were subsequent changes including to US Trust;

    (vi) the beneficiary was the policy owner;

    (vii) the Cost of Life Assurance Charge rates were based on the 1980 CSO Mortality Rates Table already referred to in paragraph 4 above.

    (viii) as set out in paragraph 4 above.

8. On the same day (14th March 2000) Regent, as trustee of the Summer Trust, entered into a life policy with Generali. This policy is referred to as the Summer Policy. The Summer Policy provided (inter alia) that:

    (i) the policy owner was Regent as trustee of the Summer Trust;

    (ii) the life assured was that of Mr McCann (who was a non-smoker and then 59 years old);

    (iii) there were to be six annual payments of premiums, each of US$2,584,083;

(iv) the sum assured was US$29,682,284;

(v) the first premium was placed in a sub-account in Generali US$ Reserve, but there were subsequent changes including to US Trust;

(vi) the beneficiary was the policy owner;

(vii) the Cost of Life Assurance Charge rates were once again based on the 1980 CSO Mortality Rates Table (with the consequence that Mr McCann as a non-smoker was rated according to a table which aggregated both smokers and non-smokers);

(viii) a mortality loading (apparently based by Generali Re on the medical examination of Mr McCann) of O.0025 was added to the table rates to result in the rates actually charged as the Cost of Life Assurance Charge;

(ix) as set out in paragraph 4 above.

9. Having regard to the large sums assured, it was necessary for Generali to obtain substantial reinsurance for the Spring and Summer Policies. The reinsurance was placed with two reinsurers: Generali Re (a company in the same group) and Munich Re. In respect of the Summer Policy covering Mr McCann's life, the charge for reinsurance by Generali Re was 0.0161716 (including the loading which Generali Re had required), and by Munich Re only 0.008262 (and Munich Re imposed no medical loading). In May 2002, Generali were charging Regent for the Cost of Life Assurance 0.01721, representing a large mark-up or profit margin of up to about 40%, out of which E&Y also benefited substantially.

10. The position of E&Y and its trustee company Regent was unusual. E&Y was deriving a 50% profit share by way of formulary fee from the policy placing with Regent, and E&Y's interests were best served by Generali imposing on Regent the highest charges it could persuade Regent to pay. Regent's duty to the McCanns was to secure the policies at the lowest charges it could persuade Generali to accept, and Regent (and E&Y through their ownership of Regent) were remunerated presumably by fees paid by the trusts of which Regent was the trustee. This was a situation of conflict of duty and interest, which (even if fully disclosed, which it appears not to have been) should not have been allowed to exist. Disclosure of E&Y's interest in the profit-sharing with Generali was made on page 20 of the Private Placement Memorandum in the second paragraph of a section headed "Financial Statements". Being placed on page 20 of a long document in relatively small print, and without a proper heading to draw attention to this paragraph, that was inadequate disclosure having regard to the clear conflict of interest and duty of which E&Y and Regent must have been aware. It needs also to be added that another E&Y Jersey company, Ernst & Young Tax Consultants Limited, was much involved in advising Regent, Mr McCann and Mr Kerr in 1999 and 2000 that the Generali policies were appropriate for Regent and Mr McCann, his wife and his family, and indeed selling the policies to Mr McCann and Mr Kerr, making the conflicts in which E&Y were involved the more inappropriate.

11. At some stage apparently in early 2000, Royal Bank of Canada bought the Jersey E&Y companies.

12. By May 2000, Mr McCann and Mr Kerr were asking for a substantial improvement in the level of charges in the three policies, noting that Generali were "*earning over $1 million per annum on this client*" (Mr Kerr's e-mail of 1 June 2000 to Mr Higgins of Regent and his letter of 7th November 2000 to Mr Colton the Manager of Generali). Following further negotiations, Endorsements No. 1 were made for each of the three policies on 12th February 2001. Endorsement No. 1 to the Winter Policy, the annuity, read as follows:

> "*Notwithstanding anything to the contrary contained therein, it is hereby noted that a 35% reduction in the Mortality, Expense and Administration Charge will take effect from 01 January 2001.*

This endorsement is subject to the condition that funds will remain invested for a five year period from 29th December 1999, the inception of the policy. In the event of a full surrender within the five year period, the total reduction will be refundable; a proportionate figure will apply on part surrender.*

**This condition will no longer apply in the event of the occurrence of any of the following:*

- *Reduction in Generali's financial stability, as judged by the relevant credit rating and the Generali Worldwide balance sheet.*
- *Significant changes in tax regulations or commercial law making the annuity programme less attractive to the trustees.*
- *Deterioration in operational service levels of Generali Worldwide, as judged by the trustees.*
- *Fee levels do not remain substantially competitive with market competition, as judged by the trustees.*

All other terms and conditions remain unchanged."

13. The effect of the endorsement was to reduce the Mortality and Expense and Administration charge from 1.25% to 0.8125%. The Endorsements No.1 to the Spring and Summer Policies were in similar terms. The issues as to the meaning of these endorsements, and their application in the events which subsequently occurred, are at the heart of the dispute in this action.

14. In January 2002, concerns of Mr McCann as to the level of Generali's fees and charges were still continuing and had been made known to Regent and to Generali. Mr McCann had sought the advice of Deloittes to assist Regent as trustee. On 8th January 2002 Mr Higgins of Regent (after a change of name called Royal Bank of Canada Trust Company (International) Limited but referred to herein still as Regent), sent an e-mail to Mr Ian Robinson, Manager of Operations at Generali, in these terms:

"Following recent developments, I think we need to give some thought to the existing client base and the pricing issues within the clients dealt with under the "old" agreement. We now know that the pricing is somewhat higher than the market is charging. For example, Crown's fees are a maximum 75 basis points down to 40 basis points. Whilst we do not need to be the cheapest provider, I feel we do need to be reasonably competitive. As trustees, we do have a responsibility to ensure that the overall pricing is within the "reasonable" ballpark.

We know that McCann is a particular issue and we have reduced our standard charges on his cases already. The other material cases are Donohoe and Palmer (Rosevear) where we are charging standard 1.25%. In addition JP Morgan and Mercury take 35% where funds are invested with them.

If we do not move the rates now I fear that this business will disappear in the next few years. I think it would be prudent to reduce the fees now to hold onto the business long term.

As an initial discussion document I have attached a spreadsheet showing where I believe we need to take the overall fee charges. The basic fee level is reduced to 70 basis points (105 points for the JPM / Mercury funds). This is still relatively high compared to the competition, but is reasonable given the quality of service.

The overall cut in our fee share is substantial. Whereas current arrangements would produce around $950k of net fee revenue (after your $125k admin charge), the

> *revised figures would produce around $540k. However, if this is the price of doing this business we have to remain competitive.*
>
> *Could you take a look at the figures and have a chat with Mark C about them?*
>
> *Give me a call when you have a chance to chat and we can decide what needs to be done."*

As this e-mail shows, Regent and Generali were well aware of the need for Generali to be competitive in the fees it charged.

15. On 4th February 2002 (the letter was incorrectly dated 2001) Mr Cann wrote to Regent calling for (inter alia) substantial reductions in the Cost of Life Assurance charge under the Summer Policy and the Mortality and Expense charges under all three policies, enclosing a copy of the First Deloitte Report referred to below.

16. By this time the Plaintiff had appeared on the scene (then called R&H Trust Co (Bermuda) Limited and subsequently Woodbourne Trustees Limited, a company belonging to the accountancy firm Deloittes and a partner firm, Rawlinson & Hunter). Deloittes in the persons of Mr G Lee, their director of insurance consulting services, and Mr Craig Wilkey who worked in their private wealth group, had been asked to advise Mr McCann (and through him the trustees) on the three policies and the level of cost of similar policies in the market place. The Plaintiff was from this time kept informed, and subsequently became the trustee of the Winter, Spring and Summer Trusts, and so owner of the three policies, in place of Regent. The persons involved in the Plaintiff were Mr James Watlington, a director who dealt with the day to day affairs of the trusts of which the Plaintiff was the trustee, and Mr Paul Hubbard, a director and chairman of the Plaintiff to whom Mr Watlington looked for the making of decisions on behalf of the Plaintiff as trustee.

17. On 1st February 2002, Mr Lee and Mr Wilkey for Deloittes delivered a report (the First Deloitte Report) on the three policies. They referred to the sub-account fund management fees, which, they said, "*vary by account selected"*. It suffices to quote their summary of their conclusions:

> "*Based on our analysis, it appears the policy is overcharged $260,000 in the first policy year for the insurance on your life assuming you are a non-smoker and a standard risk. It is likely this overcharge will continue as long as the policy is in force. This disparity should be resolved with Generali Worldwide. If you are unable to resolve this matter, we can obtain other quotes so you may explore other options available to you.*
>
> *Based on our analysis, it also appears you are overpaying mortality and expense charges. In 2001, it is estimated that you will pay $355,000 in mortality and expense charges. Based on quotes we received we believe these expenses could be reduced by at least $150,000. These savings would be even greater over time assuming assets grew."*

18. Their conclusion, therefore, was that Regent as trustee was being seriously overcharged on all three policies by Generali, even after the reductions effected by the Endorsements No. 1. The First Deloitte Report reached the Plaintiff (Mr Watlington), Regent, and Generali (Mr Colton and others) shortly after. Mr Colton wrote on 15th February 2002 to Regent rejecting the First Deloitte Report entirely, and referring to the fact that a medical loading had been imposed in respect of the Summer Policy on Mr McCann's life, a fact which Mr McCann stated in his response of the same day (15th February 2002) he had then learned for the first time, though apparently both Regent and his adviser Mr Kerr had known of this fact. In March 2002, Generali informed Mr Wilkey that the medical loading had been imposed by only one of the two reinsurers, without disclosing that the reinsurer concerned was an associated Generali company.

19. In the same month, Mr Francis Kehoe who was acting appointed actuary for Generali began to communicate with Mr Wilkey. From their exchanges of e-mails, it appears that Mr Wilkey was addressing to Generali a series of relevant questions concerning the policies and the fee levels and cost of insurance, and from Generali's internal documents it can be seen that Mr Kehoe was seeking to avoid answering several of the questions. This led to what Mr Wilkey in his e-mail of 19th April 2002 described as "*an impasse"* with Generali. However, the result of Mr Wilkey's questioning was that:

    (i) Generali sought non-smoker and smoker specific rates from reinsurers (see for example the 1980 CSO Male Preferred Non-Smoker Mortality Rates Table, a table which was available to Generali and its reinsurers in 1999-2000);

    (ii) Generali sought to remove the medical loading in the Summer Policy;

    (iii) Munich Re agreed without any apparent demur to use such rates, resulting in an immediate reduction in its rates from 0.008262 to 0.0047678 for Mr McCann as a non-smoker – a nearly 50% reduction;

    (iv) Generali Re was replaced as reinsurer by RGA which imposed no medical loading, and there was an immediate reduction from Generali Re's rate of 0.0161716 for Mr McCann to RGA's rate of 0.0035281 – a reduction of over 75%.

    It does not appear that such rates could not have been achieved by Regent and Generali at the inception of the Summer Policy on 8th March 2000, only two years before. The 1980 CSO Preferred Non-Smoker Mortality Rates Table was then readily available; and it is clear that Munich Re and RGA found no difficulty in adopting that Table, and charging considerably lower rates in the reinsurance.

20. In May 2002, Royal Bank of Canada, the successor to E&Y in respect of receipt of the formulary fee, agreed not to receive such fee in respect of the Winter Policy. Generali decided to use "*select"* rates instead of "*ultimate"* rates, which again was for the benefit of Regent as the policy owner. There followed agreement between Regent and Generali on Endorsements No. 2 to each of the three policies dated 1st July 2002, by which it was agreed that from this date the M & E Charge would be halved (from that agreed in the Endorsements No. 1) to 0.40625%. Further, the Cost of Life Assurance Charge in the Summer Policy was reduced from the then current rate of 0.01721 per mille per annum from July 2002 to 0.00500 per mille per annum, resulting in a reduction of this charge from the then current level of US$397,109 to US$115,345, which was a significantly large reduction.

21. At that time (May 2002), the protector of the Winter, Spring and Summer Trusts started the process of replacing Regent with the Plaintiff as trustee of those trusts. In 2003 (as will appear below) Regent assigned all rights in the Winter, Spring and Summer Policies to the Plaintiff, and in relation to each of the three Policies by Endorsements No. 3 dated 21st October 2003 Generali agreed to amend the Schedule to each policy to substitute the Plaintiff as policy owner. However, as a matter of practicality, the Plaintiff effectively took over all dealings with Generali in connection with the three policies from November 2002.

22. On 20th November 2002, Mr Watlington sent a memorandum to Mr Hubbard in which he referred to the First Deloitte Report, to a report of October 2002 from Mr David Carroll of Financial Architects (which included comparisons of charges of six onshore domestic US insurers), and to correspondence with Generali, and stated (inter alia):

    > *"We are now the Trustees of these Trusts. Accordingly, it is our responsibility to remedy the disparity with Generali Worldwide, the insurer that issued these policies, or arrange for the assets behind the policies to be transferred to support new policies written with another firm."*

23. By letters dated 22nd November 2002 and 7th January 2003 to Mr Colton of Generali (with copies to Mr Watlington), Mr McCann drew attention to what he considered overcharging by Generali from the inception of the policies, to the need for Generali to refund from inception the account of the overcharge, and to the fact that the Plaintiff as the new trustee would want "*to examine the current position as to competitiveness on all three contracts"*.

24. There followed a long period during which the Plaintiff by Mr Watlington, Deloittes by Mr Wilkey, and Mr McCann examined the market place for similar private placement annuities and life policies so to ascertain whether, in terms of the Endorsement No. 1, Generali's *"fee levels"* remained "*substantially competitive with market competition"*. The details of their examination of the market competition will be considered later in this judgment when the Court considers the issues between the parties in this action. They concluded that Generali's fees were not competitive.

25. On 28th February 2003 by deeds of assignment of that date, Regent assigned the Spring and Summer Policies to the Plaintiff with all benefits and rights in connection with them.

26. On 12th March 2003, Mr McCann wrote to Mr Colton of Generali to tell him that the insurance advisers were recommending that the three policies should be transferred to another insurer, and to ask for *"cost-free and helpful transfer of assets"*. Mr Colton replied by letter of 21st March 2003 drawing attention to the Endorsements No. 1 and their effect. Both letters were copied to Mr Watlington of the Plaintiff. Though Mr Robinson of Generali in his oral evidence indicated that the later decision to transfer by the Plaintiff came as a surprise, he accepted that he had seen this letter from Mr Colton at the time. Mr McCann replied by letter of 2nd April 2003, in which he stated, in relation to the claw back provisions in Endorsements No. 1 that:

> *"I remain fairly confident that the Trustees will judge these fee levels to be uncompetitive with those charged by a new, reputable company."*

27. On 18th March 2003 Mr Wilkey of Deloitte wrote to Mr McCann (with copies to Mr Watlington for the Plaintiff, Mr Lee of Deloitte, and to Mr Robert Dumont of Deloitte who was a tax expert advising on the policies and any replacements) what will be referred to as the Second Deloitte Report. In this report Mr Wilkey considered the Spring and Summer Life Policies (and indirectly the Winter Annuity Policy) and possible replacement policies offered by Pacific Annuity and Life ("Pacific"- a company on-shore in the USA) and Scottish Annuity and Life International ("SALIC") – a smaller but offshore company). In Mr Wilkey's summary the last paragraph read as follows:

> *"It should be noted that either product is a vast improvement over where we started. Your original insurance was provided with a 1.00% Mortality and Expense Charge. This charge was reduced to 0.65% in January, 2001 and reduced again to 0.40625% in July 2002. The products you are currently considering have Mortality and Expense charges of less than 0.30%. Equally as dramatic has been the reduction in cost of insurance charges. Generali had you listed as a substandard risk and in 2001 you paid approximately $408,000 in cost of insurance charges. After entering a new reinsurance arrangement and recognizing a preferred class, your annual costs of insurance charges were reduced to $120,000. Based on the products currently offered, your insurance charges are below $50,000. Elspeth's insurance charges have been reduced from $54,000 to less than $25,000. The Trusts will realize similar savings with the annuity purchase. Generali's Mortality and Expense charge was 1.25% at issue. In January, 2001 this charge was lowered to 0.8125%. In July, 2002, this rate was further lowered to 0.40625%. This rate is 25% higher than the offers currently on the table."*

This second Deloitte Report was not shown to Generali.

28. The Court notes that, during this period when the Plaintiff as trustee, Mr McCann and Deloitte were examining the competitiveness of Generali's fees and the possibility of moving the policies away from Generali:

    (i) Generali was not kept informed of the progress of this examination or of the possible alternatives being found in the marketplace;

    but

    (ii) Generali, despite knowing that such examination was taking place, refrained from asking about the progress of the examination, from putting forward any offers of better terms, and from seeking to show that Generali was competitive with its potential competitors.

29. On Monday 26th May 2003, there was a three way telephone conversation between Mr Hubbard (who was travelling and in Zurich that day), Mr Watlington (who was at home in Bermuda, that day being a holiday), and Mr McCann, at 3.45 pm Bermuda time. The conversation was noted in a memorandum of the next day (27th May 2003) by Mr Watlington. The conversation was directed to the question whether AIG Life of Bermuda Ltd or SALIC should be chosen as the provider of life policies to the Plaintiff as trustee on the lives of Mr and Mrs McCann. Mr McCann was recorded as saying that:

    "*it was a personal issue in which he was emotionally involved. He was relying on the Trustees to take a dispassionate view and make an independent decision based on overall considerations."*

30. By that time the Plaintiff with the help of Mr Wilkey of Deloittes had established that the fees and charges of AIG Life and SALIC would be cheaper than and competitive with those of Generali, despite the substantial reductions which Generali had already made in the Spring and Summer Policies charges by the Endorsements.

31. The evidence of Mr Hubbard and Mr Watlington was that they left investment management fees out of account, because the Plaintiff would in any event be able to change investment managers to ones they chose, and to choose ones which charged levels of fees which the Plaintiff would be prepared to accept. Also US Trust managed by Mr Richard Bayles was already used for sub-accounts of the Spring and Summer Policies, and they anticipated continuing to use US Trust. Their expectation was of investment management fees at about 0.35% of the value of assets managed, which were the same as or similar to the fees charged for the purposes of the Spring and Summer Policies.

32. No decision was reached during the three way phone conversation. After it Mr Hubbard had an engagement, and he phoned Mr Watlington later that evening for about 20-30 minutes. In the end Mr Hubbard and Mr Watlington decided that Generali's fees were not competitive, and that Generali should be replaced by AIG Life with new life policies on Mr and Mrs McCann's lives.

33. On 28th May 2003, Mr Watlington wrote a letter which was sent by fax to Mr Colton of Generali to inform him of the Plaintiff's decision to buy new life insurance with AIG Life in place of the Spring and Summer Policies. On the same day Mr Watlington sent a fax to AIG Life (Mr Trent Davis and Mr Robert Chesner) to similar effect.

34. Steps were taken to transfer the relevant funds from Generali to AIG Life, without any demur by Generali. It was initially thought that this would be achieved by transfers in specie. But in the event the investments with Generali were liquidated and the proceeds transferred to AIG.

35. On 20th October 2003 Regent by deed of assignment assigned the Winter Policy and all rights under it to the Plaintiff. The process had by then begun for considering whether Generali's annuity fees were competitive, and whether the Winter Policy annuity should be transferred, and if so to which life company. The Plaintiff established that lower rates could be obtained

in the market place than those charged under the Winter Policy by Generali. The Plaintiff looked both to AIG and to SALIC, and on 12th December 2003 received from Mr Mercer of SALIC their quotation for Mortality and Expense and other Charges of:

"DAC Tax	*15 bps*
Premium load 0	
Years 1 – 10	*32.5 bps*
Years 11 – 20	*25 bps*
Years 21+	*15 bps.*"

36. This was sent by Mr Watlington to Mr Wilkey and Mr McCann. Thereafter there was continued investigation of the market by (among others) Mr Wilkey. Lower rates were offered by an American onshore insurer. Mr Watlington continued to press SALIC for a more competitive offer. On 19th January 2004, Mr Mercer of SALIC sent to Mr Watlington an e-mail in which (so far as relevant) he stated:

> *"We generally do not get into "race to the bottom" type pricing for our products. For this case, we have reconsidered the pricing for a number of reasons: 1.) the original quoted pricing was determined along with the pricing for the 2 life transactions – which now are not part of the equation. 2.) the transaction looks much cleaner than when we first looked at it last year. 3.) we have spent considerable time and effort on this case and feel we are close to finalizing it, albeit for the pricing.*
>
> *After considerable review, we would be willing to offer the following pricing on the annuity:*
>
> *DAC Charge: 10 bps*
>
> *For Account Values < $50 MM:*
>
> | | |
> |---|---|
> | *Years 1–10* | *22.5 bps* |
> | *Years 11–20* | *20.0 bps* |
> | *Years 20+* | *15.0 bps."* |

37. Mr Mercer also explained that though based in Bermuda SALIC had elected under section 953(d) of the US Federal Tax Code to be treated as a US domestic corporation, and accordingly to pay such tax under sub-chapter L on income earned under the annuity contract.

38. Mr Watlington sent this offer on to Mr Wilkey on 20th January 2004 stating (inter alia):

> "*Based on our conversation and the due diligence and work done previously on this matter, the Trustees believe that this quotation is acceptable, but wish to have you see it before we commit to it."*

39. Mr Wilkey replied on 22nd January 2004 stating (inter alia):

> "*Based on the offer it seems to meet or exceed the offer made by AGL [an affiliate of AIG]. It seems all you could ask for."*

40. Mr Watlington on 23rd January 2004 sent the chain of e-mails on to Mr Hubbard stating that having received Mr Wilkey's confirmation:

> *"I believe the Trustees have done sufficient due diligence and are in a position to commit to purchase the annuity with [SALIC]. Please confirm that you wish to proceed."*

Mr Hubbard replied simply: "*Please proceed"*.

41. On 27th January 2004, Mr Watlington informed Generali of the Plaintiff's decision concerning the Winter Policy and its intended replacement by a new policy written by SALIC.

42. On 3rd February 2004, Mr Watlington confirmed to Mr McCann that SALIC's annuity offer had bettered the quotation given by AGL, and that the Plaintiff was satisfied that this was a competitive offer by SALIC, and would accept it.

43. In relation to the Winter Policy the Court repeats paragraph 28 above, mutatis mutandis.

44. The investments underlying the Winter Policy had in the event to be sold, and the proceeds of sale were transferred by Generali to SALIC.

45. On 6th February 2004 Mr Robinson sent an e-mail to Mr McCann indicating that the Chief Executive Officer of Generali, Mr Gavin Tradelius, would be in the USA on 26/27th February 2004 and could meet Mr McCann. Mr McCann replied that:

> *"The change of insurers for these policies is a matter for the Trustees; I understand that they have already obtained another provider for the Life policies, and have identified more competitive arrangements for the Annuity."*

He indicated his willingness to meet Mr Tradelius.

46. On 11th February 2004, Mr Tradelius sent an e-mail to Mr Robinson, stating:

> *"Let's set this meeting up ASAP to see if we can reverse the decision – let's talk this morning to prepare a game plan and I will confirm best dates/times to schedule the meeting. I assume you did not mention to him/the Trustees yet the substantial penalties that would apply in the event that they surrender the policies now?"*

47. The reference to "*penalties"* was directed to the terms of Endorsement No. 1 to each of the policies, and to what has been called the "*clawback"* provision in those endorsements. Mr Robinson confirmed in his evidence that he briefed Mr Tradelius.

48. On 12th February 2004 Mr Watlington sent a fax to Mr Robinson, in response to Mr Tradelius' e-mail to Mr McCann, stating (inter alia):

> *"As you know, the Trusteeship of the [Winter, Spring and Summer] Trusts was transferred to us during 2003 and the Policies underlying those Trusts assigned to this Company.*
>
> *While Mr McCann is the Settlor of all three Trusts and a Beneficiary of two of them, we would be grateful if issues relating to their servicing could be referred to us as owners."*

49. A short meeting attended by Mr McCann, Mr Hubbard and Mr Tradelius took place at Mr McCann's house near Boston on 26th February 2004. The evidence of Mr Tradelius and Mr Hubbard was that the meeting involved for the most part complaints by Mr McCann about the conduct of Generali, and the indication by Mr Hubbard that Generali's charges were not competitive. Mr Tradelius put forward no proposals from Generali, and following the meeting, Generali made no proposals, did not ask to be told the terms offered by AIG or SALIC, and did not offer to seek to meet the terms offered by AIG and SALIC.

50. On 1st March 2004, in response to a request by Mr Watlington, Mr S Le Page of Generali sent an e-mail stating (inter alia):

> "*I can confirm that having received notice of surrender, the policies for the [Spring, Summer and Winter] Trusts effectively terminated on the last day of February, after which no further policy charges will accrue."*

51. On 9th March 2004, Mr Hubbard wrote to Mr Le Page of Generali in response to an e-mail of 5th March 2004 in which Mr Le Page had indicated that deductions would be made in accordance with the Endorsements Nos. 1 and 3 to the policies, as follows:

> *"We do not accept that Generali is entitled to deduct a "refund of charges" or any other charges, set-offs, fees or other compensation whatsoever, and we expect that the full proceeds resulting from the policy redemptions will be transferred intact by you to the control of the new insurers. In the Trustees judgment, based on the wording of the policy endorsement no refund is called for. This matter is for the trustees' judgement, and not the discretion of Generali.*
>
> *AIG Life of Bermuda Ltd charges 35 basis points for Mortality and Expense with no monthly administration charge. Scottish Annuity & Life International Insurance Company (Bermuda) Ltd. charges 22.5 basis points. These rates are significantly lower than what the trustees were paying Generali, even with the reduction you now purport to reclaim.*
>
> *You stated that Generali will honor its contractual obligations. If Generali does deduct the "refund of the reduction in fees", it will be in breach of contract.*
>
> *I trust the above is satisfactory and we look forward to receipt of the full amount of the policy proceeds in the hands of the new insurers without further deduction."*

52. Relying on the Endorsements to the three policies Generali, when transmitting the policy funds to SALIC and AIG, deducted the following sums:

Winter Policy	US$ 695,677
Spring Policy	US$ 36,224
Summer Policy	US$ 77,201
Total	**US$ 809,102**

53. In this action the Plaintiff claims against the Defendant (i) payment of this sum, (ii) payment in respect of additional work done by the Plaintiff and charged to the three Trusts in consequence of the Defendant's alleged wrongful breaches of the three policies, (iii) interest, and (iv) costs.

54. It is to be regretted that this action has taken so long a period of time to reach the stage of this trial.

Witnesses of Fact

55. It is convenient here to set out briefly the views reached by the court concerning the oral evidence addressed by the parties. The Plaintiff, represented by Advocate Alison Ozanne, called three witnesses, Mr Hubbard, Mr Watlington and Mr Wilkey. In the Court's judgment, all three of these witnesses did their best to tell the Court accurately what had occurred, despite the long passage of time, and their evidence was reasonably confirmed by the large number of faxes, e-mails, letters and other documents placed before the Court.

56. Generali, represented by Advocate Jeremy Wessels, also called three witnesses, Mr Tradelius, Mr Robinson and Mr Kehoe.

57. As regards Mr Tradelius, he had little involvement except for the meeting with Mr McCann and Mr Hubbard on 26th February 2004. It is noteworthy that, though the evidence of Mr Robinson was that Mr Tradelius had been briefed before going to this meeting (Day 4, pages 104-105), Mr Tradelius was recorded in Mr Hubbard's note of this meeting (not prepared contemporaneously and not until 15th June 2004), as stating that Mr Tradelius:

> "*Was aware that there were some problems but was not aware of the scope of the problems or the question of fees as he was effectively making a courtesy call. He was therefore unaware nor had his office apparently made him aware of the earlier negotiations between Fergus [McCann] and the previous Trustees and Generali".*

58. In the Court's judgment, what Mr Tradelius then said (as recorded by Mr Hubbard) did not represent the correct position as to his state of knowledge, as shown by Mr Tradelius' own e-mails to Mr Robinson. Since the limited scope of his evidence was peripheral to the issues in this action, the Court finds it unnecessary to consider his evidence in more detail. But if this were necessary, the Court would not have accepted his evidence except in so far as consistent with the documentary record at the time.

59. Mr Robinson was for the most part a careful witness whose evidence was consistent with the contemporary documents. However, on Day 4, pages 100-102, Mr Robinson gave evidence that when Generali was informed by the Plaintiff of its intended surrender of the Spring and Summer Life Policies (see paragraph 33 above) this came as a "*surprise"* to Mr Robinson. But in answer to questions from the Court Mr Robinson agreed that he had seen and discussed with Mr Colton the response dated 21st March 2003 to Mr McCann's letter of 12th March 2003 (see paragraph 26 above). The Court notes also Mr McCann's letters of 22nd November 2002 and 7th January 2003 to Mr Colton (paragraph 23 above) and of 2nd April 2003 (paragraph 26 above). The Court considered that in view of the long period between that time and the trial, Mr Robinson's evidence had to be checked for its correctness or otherwise, against the contemporary documentary record.

60. Mr Kehoe was in the Court's judgment not a witness whose oral evidence could be accepted except in so far as confirmed by the contemporary documents. It was apparent that in his case the long passage of time meant that he did not have an independent recollection of anything not appearing in the documents.

Expert Witnesses

61. It was a regrettable feature of this action that the expert witnesses (Mr Cottingham called by the Plaintiff and Mr Le Boeuf called by Generali) were asked to express expert opinions on different questions.

62. The Court concluded that Mr Cottingham was a careful witness who did not allow his opinions in so far as relevant (his views on the interpretation of the Endorsements No. 1 were inadmissible) to stray either from the scope of his expertise or into advocacy for the Plaintiff's case, and where Mr Cottingham's evidence was different from that of Mr Le Boeuf the Court has preferred the evidence of Mr Cottingham.

63. Mr Le Boeuf's evidence suffered from two factors: first, his prime experience has been in the American domestic market, and not so much in the offshore personal placement market; and secondly, too much of his evidence, as read on paper and particularly as delivered orally, gave the Court the strong impression of being further advocacy for Generali's case. As stated above, the evidence of Mr Cottingham is preferred where there are differences.

The Issues

64. The Court now turns to the issues as defined by the Advocates. It is a pity that, though time was given for a further refinement of the issues, these remained at the time of final submissions a work-in-progress. Accordingly, the Court has to some extent re-drafted the issues to accord with the way in which they were presented by the Advocates.

65. The Court wishes here to make clear that after careful and detailed consideration and discussion, all the members of the Court are agreed on all of this judgment, in the context of the determination of the factual matters by the three Jurats, guided by the determination of matters of law by the Lieutenant Bailiff.

Issue No. 1

How are the Endorsements no. 1 to be construed?

66. The wording of Endorsement no. 1 to the Winter Policy has been set out above in paragraph 12. Three questions have to be answered in interpreting this wording in the fourth bullet point:

    (i) What is the meaning of "*fee levels"*;

    (ii) What is the meaning of *"remain substantially competitive with market competition"*;

    (iii) What is meant by, and what are the implications of, "*as judged by the trustees"*.

(i) Fee Levels

67. Miss Ozanne submitted that the words "*fee levels*" related solely to the fees charged by Generali itself, which consisted of the Mortality and Expense charges. Mr Wessels, on the other hand, submitted that these words must include all fees charged under the umbrella of each of the policies, including the fees charged by each of the managers of the funds in which the sub-accounts were invested. If Mr Wessels' submission is right, then the Plaintiff in investigating the "*market competition"* would have to look to not only what other insurance companies were charging for their services, but also the fees charged by the particular investment managers for each of the sub-accounts, and then consider in each case the combined package of insurers' fees and investment managers' fees.

68. Miss Ozanne's submissions were these, in summary:

    (i) The subject matter of the Endorsements no. 1 (and of the Endorsements no. 2 which followed) was reductions in the Mortality and Expense fees – the fees charged by Generali itself. Fees charged by investment managers were not part of the subject matter of these endorsements.

    (ii) The "*claw-back*" provision related to these reductions which, in the event of surrender within the five year period, were to be "*refundable"*. The claw-back position did not in any way relate to the fees of investment managers.

    (iii) Given that (i) and (ii) above were limited to the fees of Generali itself, the words "*fee levels"* in the fourth bullet point could and should not be applied to fees of investment managers which formed no part of the subject matter of the Endorsements or the claw-back provision.

    (iv) In any event, in which investment fund or funds the premiums were to be placed was subject to the wishes of the Plaintiff as the policy owner. The investment fund or funds used could be changed from time to time as the Plaintiff's wishes changed. Investment fund managers might charge the same fees, or the level of their fees might differ. So the words of the fourth bullet point could not realistically be implemented by the Plaintiff if "*fee levels"* included fund managers' fees, because the Plaintiff could not reach a judgment on overall fee levels including fund managers' fees which might change at any time, and the Plaintiff would not have known exactly which fund managers charging what level of fees would need to be compared.

(v) The wording should be construed in favour of the Plaintiff's interpretation, as Generali had produced the wording.

69. Mr Wessels' submissions were these, in summary:

(i) With annuity and life policies it is the totality of fees which is relevant: these include both the insurers' own fees and the fees charged by the investment fund managers used for the purposes of investing the policy premiums.

(ii) In assessing competition in the market for private placement annuity and life policies for the benefit of high-worth individuals, there would be no sense in singling out only the insurers' fees. The market is concerned with the package of all the fees charged for the purposes of each policy.

(iii) Mr Wessels relied on Mr Le Boeuf's evidence in which he sought to emphasise the relevance of this complete package of all the charges.

(iv) Mr Le Boeuf went further in his evidence. He indicated that often the fees of the insurers and the fees of the fund managers are linked. Insurers seek (for competitive purposes) to charge what on their face appear to be low Mortality and Expense fees, and to improve their profits by arranging with their selected fund managers to share in the fund managers' fees, which are increased in order to enable this profit-sharing to be achieved for the benefit of both the insurers and the fund managers. Mr Le Boeuf indicated that this system of profit-sharing is kept confidential to the insurers and the fund managers, and it is generally not disclosed to prospective or actual policyholders.

(v) The wording of the clawback was produced by Regent, and there was no basis for construing it adversely to Generali.

70. The Court's conclusion on the meaning of "*fee levels"* is that Miss Ozanne's main submissions are correct. The Endorsements were related to a reduction only in Generali's own fees – the Mortality and Expense charges, and the refund to Generali in the event of an early surrender of the policies (or any of them) was a refund only of such reduction in Generali's fees. The fees of investment managers were not involved, because there was no agreed reduction in such fees, and no refund related to such fees. The suggestion that the words "*fee levels"* could be expanded so as to encompass whatever fees might be charged by the different investment managers chosen from time to time by the Plaintiff as the policy holder is, in the Court's judgment, not correct. But the Court does not consider that Miss Ozanne's submission in paragraph 68(v) above is needed to reach the correct conclusion (and may not be well founded in fact).

71. At this point it is necessary for the Court to reach a conclusion concerning the evidence of Mr Le Boeuf on which Mr Wessels relied. Mr Le Boeuf's emphasis on the complete package of all charges was, in the Court's judgment, primarily based on policies designed and used for what was described as the "*mass market"*. Under these policies the insurer would present the policyholder with a list of approved investment funds, and the policyholder would have no right to require a change of funds and fund managers. The personal placement market is different: high net worth individuals, or their trustees, as policy holders are able to choose to move the sub-accounts to funds different from those selected by the insurers, and the fees charged by such different fund managers may be the same as, or may be higher or lower than, the fees charged by the fund managers selected by the insurers. In this regard Mr Le Boeuf's evidence is, in the Court's judgment, directed to the wrong types of policy.

72. As regards the practice of insurers sharing the fund managers' fees, it was again clear to the Court that this system is primarily one adopted in the US domestic insurance market, and in the mass market (in which fund managers are selected by the insurers and not able to be

changed by the policyholders), and it is not a system which has any real application in relation to offshore one-off private placements. Mr Le Boeuf indicated that the American regulators treat such fee-sharing as normal and acceptable: but that also related to the US onshore mass market, and not to the offshore private placement market.

73. Mr Cottingham questioned the ethics of such undisclosed fee sharing in which the fees of insurers are made to appear competitively low while in reality being boosted by the secret sharing in the artificially higher fees of the fund managers. He made clear that his experience involved a complete rejection of any attempt by insurers to negotiate such fee-sharing. He also indicated that round the world the regulatory authorities have begun to regulate against such fee-sharing.

74. In the Court's judgment Mr Wessels' reliance on Mr Le Boeuf's evidence for the purposes of construing the wording of the Endorsements no. 1 was not well founded.

(ii) "*Remain substantially competitive with market competition*"

75. The construction of these words in the Endorsements no. 1 raises a question which was not addressed in any detail by the Advocates. Mr Wessels submitted that the assessment by the Plaintiff of the competitiveness of the fee levels required the Plaintiff to examine the whole package of fees charged by Generali, and then to compare that package with the packages of fees charged for reasonably similar annuities and life policies in the offshore private placement market. As the Court has already held, what are to be compared are the fees charged by the insurers alone, without reference to fund managers' fees which will change from time to time as the sub-account investments are moved from one or more investment funds to another or to others.

76. A point which the Court raised related to the extent of the research into other insurers' fee levels which the Plaintiff could be expected to undertake for the purposes of judging whether General's fees remained "*substantially competitive with market competition"*. In this regard the nature of the offshore private placement market has to be kept in mind. Though the insurers seeking to persuade high net worth individuals to enter into their annuity and life policies may set out standard fee terms in the offers made by their private placement memoranda, those standard fees may, or may not, in practice be adhered to when negotiating with particular high net worth individuals whose bargaining power, derived from the size of the sums they are prepared to invest in annuity and life policy premiums, may be considerable. This is illustrated by the large reductions in fees which Generali agreed when pressure was applied indirectly by Mr McCann, and directly by Regent as the policyholders. It is also illustrated by the response of SALIC when pressed to reduce their fees for the annuity: see paragraphs 35 and 36 above. So what may be quoted in private placement memoranda may differ markedly from what insurers are prepared to agree to gain or to retain the premiums of high worth individuals.

77. Further, the nature of the offshore private placement market is inevitably rather opaque. Finding out what a range of insurers engaged in this market are charging under their existing policies (or are offering for new policies, though as indicated above initial offers may be at higher rates than the policies ultimately agreed) may in itself present considerable difficulties (quite apart from probable discrepancies between what is publicly offered and what is privately agreed, as referred to in the last paragraph). The Court concludes that research undertaken to assess whether an insurer's fees actually charged in this market were *"substantially competitive with market competition"* was likely to have to be based for the most part on:

    (i) Any information which could be obtained (if any) as to fees actually being charged by other insurers;

    (ii) Actual offers of fees to the Plaintiff by other insurers (as opposed to what other insurers may disclose in private placement memoranda);

(iii) The level of standard fees offered by insurers in the onshore market, because these standard fees, which are available to any person who wishes to enter into a policy and in some instances perhaps reduced to take advantage of the fee sharing mentioned above, are likely to be higher than those available to high net worth individuals negotiating private placements of large premiums with insurers operating offshore.

78. Whether the research undertaken by the Plaintiff with the assistance of Mr McCann and Deloitte (and others who became involved – Mr Nowotny, and Mr David Carroll of Financial Architects who appears to have been connected with AIG Life of Bermuda Ltd – "AIG") met the requirements of Endorsements no. 1 will be considered by the Court below.

(iv) ***"as judged by the trustees"***

79. The fourth bullet point in the Endorsements no. 1 gives to the Plaintiff the contractual right to judge the continuing competitiveness of the fees charged by Generali. It is agreed by the parties that the right to judge is subject to the implication that the Plaintiff would not exercise its judgment:

> "*unreasonably, perversely or in bad faith".*

Though this is agreed, it is necessary to spell out by reference to some of the relevant authorities what is meant by these words.

80. Though Generali has pleaded that the Plaintiff made its judgment "*in bad faith"*, a phrase which in civil disputes not involving governmental bodies always involves a charge of dishonesty, Mr Wessels has made it clear that no such charge is made against the Plaintiff, and in his final submissions to the Court has withdrawn the allegation.

81. The Court therefore needs to examine the words "*unreasonably"* and "*perversely*" in the context of a right and power of one party to a contract to form its own judgment which is to be binding on both parties to the contract.

82. A large number of authorities was cited, but it is necessary only to refer to a few of them. The first is Socimer International Bank Ltd (in Liquidation) v Standard Bank London Ltd [2008] EWCA Civ 116; [2008] 1 Lloyd's Rep 558; [2008] Bus. LR 1304; [2008] All ER (D) 331; a decision of the English Court of Appeal. In the main judgment of Rix LJ reference was made in paragraphs 60 – 64 to four earlier decisions of the English Court of Appeal concerning the exercise of discretionary contractual powers by a contracting party. In the first, Abu Dhabi National Tanker Co v Product Star Shipping Ltd (No. 2) [1993] 1 Lloyd's Rep 397 Leggatt LJ said:

> *"For purposes of judicial review the Court is concerned to judge whether a decision-making body has exceeded its powers, and in this context whether a particular decision is so perverse that no reasonable body, properly directing itself to the applicable law, could have reached such a decision. But the exercise of judicial control of administrative action is an analogy which must be applied with caution to the assessment of whether a contractual discretion has been properly exercised. The essential question always is whether the relevant power has been abused. Where A and B contract with one another to confer a discretion on A, that does not render B subject to A's uninhibited whim. In my judgment, the authorities show that not only must the discretion be exercised honestly and in good faith, but, having regard to the provisions of the contract by which it must be conferred, it must not be exercised arbitrarily, capriciously, or unreasonably. That entails a proper consideration of the matter after making any necessary enquiries. To these principles, little is added by the concept of fairness: it does no more than describe the result achieved by their application."*

83. In the second case Ludgate Insurance Co Ltd v Citibank NA [1998] 1 Lloyd's Rep 221 Brooke LJ said:

> *"35. It is very well established that the circumstances in which a court will interfere with the exercise by a party to a contract of a contractual discretion given to it by another party are extremely limited. We were referred to Weinberger v Inglis [1919] AC 606; Dundee General Hospitals Board of Management v Walker [1952] 1 All ER 896, Docker v Hyams [1969] 1 Lloyd's Rep 487, and Abu Dhabi National Tanker Company v Product Star Shipping Company Limited [1993] 1 Lloyd's Rep 397 ("The Product Star"). These cases show that provided that the discretion is exercised honestly and in good faith for the purposes for which it was conferred, and provided also that it was a true exercise of discretion in the sense that it was not capricious or arbitrary or so outrageous in its defiance of reason that it can properly be categorised as perverse, the courts will not intervene."*

84. The third case, Gan Insurance Co Ltd v Tai Ping Insurance Co Ltd (No. 2) [2001] EWCA Civ 1047; [2001] 2 All ER (Comm) 299; involved a claims cooperation clause in a facultative reinsurance policy which required the prior approval of the reinsurers for any settlement or compromise of an underlying loss. The Court of Appeal held that a term preventing the reinsurers from withholding such approval unless they had reasonable grounds for doing this was not to be implied. Reference was made in Socimer to extracts from the judgment delivered by Mance LJ:

> *"64 I gain some assistance by analogy from these cases. In all of them, it seems to me that what was proscribed was unreasonableness in the sense of conduct or a decision to which no reasonable person having the relevant discretion could have subscribed ….*
>
> *67 ….I would therefore accept as a general qualification, that any withholding of approval by reinsurers should take place in good faith after consideration of and on the basis of the facts giving rise to the particular claim and not with reference to considerations wholly extraneous to the subject-matter of the particular reinsurance ….*
>
> *73 If there is any further implication, it is along the lines that the reinsurer will not withhold approval arbitrarily, or (to use what I see as no more than expanded expression of the same concept) will not do so in circumstances so extreme that no reasonable company in its position could possibly withhold approval. This will not ordinarily add materially to the requirement that the reinsurer should form a genuine view as to the appropriateness of settlement without taking into account considerations extraneous to the subject matter of the reinsurance ……".*

85. The fourth case was Paragon Finance plc v Nash [2001] EWCA Civ 1466; [2002] 1 WLR 685 in which the issue was whether the discretion given to a mortgagee finance company to vary the interest rate paid by the mortgagor was to be exercised "*fairly as between both parties to the contract, and not arbitrarily, capriciously or unreasonably"*. Dyson LJ accepted a limited implication that the discretion was not to be exercised "*unreasonably"* in a sense analogous to the limitation in public administrative law that a discretionary power of a public authority is not to be exercised in a manner in which no reasonable public authority would exercise the power. Dyson LJ said:

> *"41. So here too, [referring to Gan Insurance v Tai Ping Insurance] we find a somewhat reluctant extension of the implied term to include unreasonableness that is analogous to Wednesbury unreasonableness. I entirely accept that the scope of an implied term will depend on the circumstances of the particular contract. But I find the analogy of the Gan*

> *Insurance case and the cases considered in the judgment of Mance LJ helpful. It is one thing to imply a term that a lender will not exercise his discretion in a way that no reasonable lender, acting reasonably, would do. It is unlikely that a lender who was acting in that way would not also be acting either dishonestly, for an improper purpose, capriciously or arbitrarily. It is quite another matter to imply a term that the lender would not impose unreasonable rates ….".*

86. Reference was also made by the Advocates to another decision of the English Court of Appeal in Lymington Marina Ltd v Macnamara [2007] EWCA Civ 151; [2007] 2 All ER (Comm) 825. In this case the licensee of a right to berth a yacht in the marina was permitted by the licence terms to grant a sub-licence provided that the proposed sub-licensee was first approved by the marina company. The judge at first instance held that the relevant test whether the sub-licence could be refused approval was simply whether the identity of the sub-licensee was acceptable or not to the marina company. Because the marina company had misconstrued its powers it had acted unlawfully. The power to object to the identity of a sub-licensee was subject to the implication (on the basis of the Gan Insurance case) that the power was to be exercised in good faith and on relevant grounds, and not arbitrarily. The Court of Appeal disapproved the judge's reliance on a test applicable to public bodies in administrative law, but upheld his decision. The contractual power to refuse to approve a sub-licensee was to be exercised in good faith, on the basis of relevant facts, not with reference to extraneous and irrelevant matters. The court could not substitute its own view of the reasonableness of the decision of the marina company. Arden and Pill LJJ referred to some of the cases already cited above, and followed their guidance.

87. So far as concerns the law of Guernsey, this Court holds that the test is similar to the one established in England. Leaving good faith on one side, the exercise of a contractual discretionary power is to be exercised on the basis of factors which are relevant for the purposes of the contract to the exercise of the power, and not on the basis of extraneous or irrelevant factors. Before it is exercised any necessary and appropriate enquiries are to be made. If the decision is reached on the basis of only relevant factors, after such enquiries have been made, and is therefore a rational, and not an irrational, decision, it will be upheld by the Court. It is no part of the Court's function to second-guess the contracting party and to arrive at the Court's own conclusion on the matter; that would be to usurp the function given by agreement to the contracting party. Though the use of terms such as "*subjective"* and "*objective"* carries the danger of obfuscation and not clarification, it can perhaps be said that the Court does not apply some simple "*objective"* standard, but the Court upholds the "*subjective"* decision of the contracting party, provided that this decision has been arrived at in a rational way on the basis of only relevant factors, and not irrelevant factors.

88. The Court has dealt with Issue no. 1 fully, because in the view of the Court the submissions made for the opposing parties did not fully grapple with all the terms of the fourth bullet point in the Endorsements no. 1, a step which the Court regards as essential before embarking on consideration of the other issues.

Issue No. 2

Whether the policies as amended by the Endorsements should contain an implied term that any exercise of judgment by the Plaintiff should not be made unreasonably, perversely or in bad faith

89. The parties agree that such a term is to be implied. The Court has already considered the ambit of this term above.

Issue No. 3

Whether the policies as amended by the endorsements should contain a further term implied into them that in the exercise of its judgment the Trustee should have regard to the following nine factors?

(i) Pricing of the products including having regard to:

(a) the overall level of charges;

(b) the need for any medical loadings;

(c) the need for an offshore policy;

(d) the degree of input into investment strategy or ability to offer bespoke products;

and

(e) any discretions to increase or alter charges or levy further charges;

(ii) The financial standing/reputation of the insurer, particularly having regard to the long term nature of the products;

(iii) The tax effectiveness of the products including the use of aggregate rates and the need to maintain a safe harbour;

(iv) The specialised nature of the products; and

(v) The specialised nature of the market for the products and the limited number of participants in that market.

("the nine factor term")

90. Mr Wessels relied on these nine factors in two different ways:

(i) as an implied term; or

(ii) as factors which the Plaintiff was bound to take into account as relevant factors.

The Court will consider, first, whether this term is to be implied, and secondly, Mr Wessels' alternative argument which has in fact been omitted from the agreed statement of issues.

91. The requirements to be met before such a term can be implied in a contract, especially a contract such as these complex insurance policies and the Endorsements, have been stated so frequently and so fully by, in particular, the Courts of England and Wales, that a brief reference to the various tests or requirements is all that is necessary in this judgment:

(i) The Court has no power to improve the terms of these policies or to make them fairer or more reasonable (Attorney-General of Belize v Belize Telecom Ltd [2009] UKPC 10; [2009] 1 WLR 1988: Trollope & Colls Ltd v NW Metropolitan Regional Hospital Board [1973] 1 WLR 601 HL).

(ii) The starting point is to ascertain the meaning of these policies (as endorsed) which the words used would convey to a reasonable person having the background knowledge known to the contracting parties at the relevant times (Investors Compensation Scheme Ltd v West Bromwich Building Society [1998] 1 WLR 896; Belize Telecom – above).

(iii) The question whether any further term is to be implied (in addition to the terms expressly stated in the policies as endorsed) can arise only if there is

something missing or not dealt with in the express terms, or if necessary to make sense of the express terms (Belize Telecom- above).

(iv) The requirement of "necessity" is absolutely fundamental. The Court cannot make an implication in order to express what the Court considers would have been reasonable for the parties to have agreed. The implied term must be necessary to fill a lacuna or to make sense of the express terms (Scrutton LJ in Reigate v Union Manufacturing Co (Ramsbottom) Ltd et al [1918] 1 KB 592 CA at p.605: Belize Telecom (above) at para.22).

(v) The necessity for the implication of the term must arise from the construction of the express terms, and must not be considered in isolation from, or in contradiction of, the express terms. The need must be to make real sense, commercially or otherwise, of the express terms, and not merely to add what the parties might reasonably have added if they had so decided and agreed (The Moorcock (1889) 14 PD 64 CA: Reigate (above): Belize Telecom (above) at para.25).

(vi) There is always the danger that the Court may be led to imply a term covering an event or the like, which the parties themselves had specifically discussed and decided not to cover in their agreed express terms – a not infrequent occurrence in relation to highly complex commercial contracts.

(vii) Some of the relevant tests were summarised in BP Refinery (Westernport) Pty Ltd v Shire of Hastings (1977) 180 CLR 266 PC at 282-283:

> *"… the following conditions (which may overlap) must be satisfied: (1) it must be reasonable and equitable; (2) it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it; (3) it must be so obvious that 'it goes without saying'; (4) it must be capable of clear expression; (5) it must not contradict any express term of the contract".*

(viii) Having cited this passage in Belize Telecom (above) the Privy Council continued with these observations (in para. 27):

> *"The Board considers that this list is best regarded, not as series of independent tests which must each be surmounted, but rather as a collection of different ways in which judges have tried to express the central idea that the proposed implied term must spell out what the contract actually means, or in which they have explained why they did not think that it did so. The Board has already discussed the significance of "necessary to give business efficacy" and "goes without saying". As for the other formulations, the fact that the proposed implied term would be inequitable or unreasonable, or contradict what the parties have expressly said, or is incapable of clear expression, are all good reasons for saying that a reasonable man would not have understood that to be what the instrument meant*."

However, in the view of this Court, the first condition in the BP Refinery case list ("it must be reasonable and equitable") is not entirely consistent with the other cases cited above (including Belize Telecom itself) which make it abundantly clear that the reasonableness and equitableness of a term proposed to be implied go only some way towards meeting the fundamental tests to be satisfied before any implication is to be made. Necessity is the fundamental starting point.

92. The Court now turns to consider whether Mr Wessels' nine factor term is to be implied in these policies as each endorsed by the three endorsements. The Court has reached the firm conclusion that such a term is not to be implied in these policies as endorsed:

    (i) Whatever lacuna there might have been in respect of the process by which the Plaintiff was to reach a judgment as to the competitiveness of General's fee levels (and in view of the Court there was no such lacuna), it has been filled fully by the agreed implied term. There is no necessity to make any further implication.

    (ii) The proposed nine factors as a whole go far beyond anything which could begin to satisfy the tests of necessity or obviousness or the officious bystander test.

    (iii) In so far as the nine factor term includes factors which would be relevant to the Plaintiff's process of forming a judgment under the fourth bullet point in Endorsements no.1, they would be amply catered for by Mr Wessels' alternative argument that they are simply relevant factors for the Plaintiff to consider.

    (iv) Some comments need also to be made on the specific factors which Generali wishes to be inserted by implication. Factor (i)(a) would have to be qualified in any event so that it referred only to the overall level of Generali's own fees, and not the fees of investment managers. As to factor (i)(b) medical loadings had ceased to be relevant as a result of Endorsement no. 2 of the Summer Policy, and no one is now suggesting that such loadings remain relevant. The policies are offshore policies, and there is no need for this to be spelled out again through factor (i)(c). Factor (i)(d) is irrelevant, since one of the main purposes of policies such as these is to give the policy holder the ability to select different investment funds from time to time. As to factor (i)(e), it is no part of either party's case that there was any discretion to increase the fee burden (and it is noteworthy that reductions in the fee burden are ignored in the formulation of this factor). As to factor (ii) the financial strengths of any competitive insurers was an obvious factor to be taken into account in conjunction with the security of the premium funds, and is covered amply by Mr Wessels' alternative argument. The "reputation" of any insurer would be of limited relevance, since experience in recent years has shown that reputation may not be the best guide to reality. The tax effectiveness of any policies was a matter for the Plaintiff as trustee and for their beneficiaries, and factor (iii) would be of limited relevance to the Plaintiff's judgment in respect of Generali's fees. The specialised nature of offshore annuity and life policies such as these three policies is built into any judgment of the competitiveness of those policies in the offshore market, and the implication of factor (iv) would add nothing to the judgment process. The same point applies to the specialised nature of the market (part of factor (v)). The limited number of participants (the other part of factor (v)) is relevant to the judgment process only in so far as it might prevent the Plaintiff from obtaining more than a limited number of directly competitive quotations, and therefore lead the Plaintiff to look for comparisons with quotations outside the immediate offshore market.

93. Miss Ozanne relied on the "*entire contract*" clauses in the policies as excluding this alleged implied term. Such clauses are included in contracts to prevent parties seeking to rely on collateral representations, warranties or contracts, which such clauses may be effective to exclude. But such clauses do not prevent the implication of terms, since the essential point of implied terms is that the Court holds that such terms form part of the contract at the moment when the contract is entered into. It is noted that if the "*entire contract*" clauses had the effect

for which Miss Ozanne contends (which they do not) they would have excluded the implication of the term which the parties have agreed is implied in these policies.

94. In the judgment of the Court the nine factor term is not to be implied in these three policies.

95. As already indicated in paragraph 92(iv) above, some of the factors were factors which the Plaintiff would need to take into account; most would not be. To that limited extent the Court accepts Mr Wessels' alternative argument concerning such factors.

Issue 4

Whether the Court should draw a negative inference against Generali by not calling Mark Colton as a witness of fact.

96. Mr Colton was clearly much involved in all the matters set out in the history above and could, if he had been called as a witness by either side, have given relevant evidence of fact. The negative inference which Miss Ozanne submitted that the Court should draw is "*that Mr Colton would agree with Woodbourne's understanding of the meaning of "fee levels" in the endorsement which Mr Colton drafted*" (Day 7, page 136, lines 19-22). Such an inference is not one which the Court could properly draw, not least because it would be both inadmissible and irrelevant. The view of Mr Colton as to the construction of the words "*fee levels*" would be just as inadmissible and irrelevant as the views of any of the witnesses of fact (or Mr Cottingham) on that aspect.

Issue 5

Whether the Plaintiff made any judgment at all for each of the three policies.

97. Miss Ozanne correctly submitted that the only decision or judgment of the Plaintiff which is relevant in this action is its decision that the fee levels of Generali were uncompetitive. Once that decision had been made, and the premium fund had been withdrawn from Generali, what the Plaintiff chose to do with the funds (whether to enter into replacement policies, or to invest in some other form of investment, or to deposit the funds with a bank or banks) was irrelevant.

98. The question which Mr Wessels raised under this issue was whether the Plaintiff had in truth formed any judgment as to the uncompetitiveness of Generali's fee levels. He put this in two ways: either (i) that Mr McCann had decided that the fee levels were uncompetitive, and the Plaintiff had simply gone along with this decision and looked for the cheapest rival insurers to replace Generali; or (ii) that the Plaintiff had assumed (along with Mr McCann) that Generali's fees were uncompetitive, and had done no more than to try to find any rival insurer which would offer a lower fee, even though what the rival insurer was offering was not in its terms, or in the rival insurer's financial security and reputation, truly competitive with what Generali had agreed to provide by the three policies with their fees greatly reduced as a result of the Endorsements nos.1 and 2.

    This issue has to be considered separately in relation to the Spring and Summer Policies and to the Winter Policy, since these were dealt with separately.

99. Much of Mr Wessels' submissions and his cross-examination of the Plaintiff's fact witnesses was based on the premise that there needed to be a meeting of the directors of the Plaintiff who reached a specific decision on a particular day at a particular time, clearly recorded in a contemporaneous minute, and reported to Generali straightaway. He drew the Court's attention to the various ways in which the Plaintiff's lawyers, both those before Miss Ozanne and Miss Ozanne herself, had tried to set out in pleadings the answer as to exactly when and how the decision or decisions had been reached by the Plaintiff. The Court notes, however, that in this action the pleadings on both sides failed to set out clear statements of the parties' contentions and the parties' cases appearing from the evidence and submissions at trial have departed in a number of respects from the pleaded cases. In an ideal world, Mr Wessels'

conception of the required decision might be met. But the Court for the reasons set out below considers that, though the decision-making process did not meet Mr Wessels' ideal, there were valid decisions made by the Plaintiff in relation to each of the three policies. In the Court's view there needed to be a "*decision*" by the Plaintiff in relation to each of the policies; but as so often in practice, as opposed to theory, the decision did not have to be arrived at in so precise and clear-cut a manner as Mr Wessels submitted.

The Spring and Summer Policies

100. In the period before the Plaintiff took over the dealings with the policies and with Generali in November 2002 (paragraph 21 above), those concerned with the policies had been Mr McCann, Regent, and Mr Wilkey of Deloitte. Mr McCann had throughout shown his concerns about the conduct of Generali, E&Y and Regent, especially in relation to the medical loading by Generali Re as reinsurer (which Generali had accepted after some improvement in Generali Re's rates) that had resulted, when added to the high Mortality and Expense fees and Cost of Insurance charges, in what Mr McCann justifiably regarded as serious overcharging. The challenges to Generali had resulted in the reductions in fees and Cost of Insurance Charges agreed by the Endorsements no. 1 and 2, but subject to the claw-back provision if the policies were surrendered within five years from inception, and without any refund of the high fees and charges in the initial years. It is clear that by the time when he engaged Deloitte to examine the position under these policies in about January 2002 Mr McCann took the view that Generali had secured too large a portion of the premium funds through its fees and charges. The First Deloitte Report of 1 February 2002 (paragraph 17 above) showed that there had been a serious level of overcharging, and this led (inter alia) to the substantial changes and reductions which were agreed by the Endorsements no. 2 in July 2002 (paragraphs 19 and 20 above). However, before those changes were made Mr Wilkey had made some determined efforts to obtain more information from Generali, which Mr Kehoe had avoided giving, leading in April 2002 to the "impasse" with Generali as Mr Wilkey saw it. It is true that some of the information not provided to Mr Wilkey related to the reinsurance terms obtained by Generali which would normally be regarded as confidential to Generali. But having regard to the position in which Generali had found itself as a result of its overcharging, Generali might have thought it commercially sensible to allow Mr Wilkey to receive at least some more of the information he was seeking. As Mr Wilkey wrote to Mr Kehoe on 15 April 2002:

> *"Currently Generali has received $40 million of premium payments from Mr McCann and his family. It is inconceivable that Generali will not provide the information requested."*

Mr Wilkey reached the decision which the Court considers to be justified, that there was no point in pursuing his requests for the supply of information by Generali any further.

101. So when the Plaintiff came firmly on the scene in November 2002, through Mr Watlington it was appreciated that Mr McCann had lost confidence in Generali, and would prefer to leave Generali. But the Court concludes that Mr McCann was careful to leave any decision under the Endorsements no. 1 wording to the Plaintiff, and concentrated on ensuring that the Plaintiff was assisted by Mr Wilkey and others in assessing the market.

102. The Plaintiff's decision was finally taken on 26 May 2003 (paragraphs 29-32 above). In the period before then, examination of the private placement market had been made, as follows:

    (i) In the First Deloitte Report of 1 February 2002, Deloitte drew attention to market indications from brokers that Mortality and Expense charges on life policies in private placement pricing (apparently within the US onshore market) should be between 0.25% and 0.35%, and on a specific description of those insured (Mr and Mrs McCann) had an indication of 0.40% in year 1, 0.30% in years 2 to 10, 0.25% from year 11 to 20, and 0.10% thereafter.

(ii) On 27 March 2002 Mr Wilkey sent to Mr Kehoe indications of the fees which would be charged by John Hancock Variable Life Insurance Co. John Hancock was a US onshore life company. Mr Wessels submitted that a comparison with the US onshore market was irrelevant and inappropriate, since the comparison needed to be with the offshore market in which the Spring and Summer Policies had been contracted with Generali. But the correct position, in the Court's view, is that set out in paragraph 77 above.

(iii) On 8 January 2003 Mr McCann wrote to SALIC asking for illustrations of their fees for these life policies to be sent to Mr Watlington.

(iv) On 28 January 2003 Mr Wilkey sent to Mr McCann and Mr Watlington spreadsheets showing comparisons with John Hancock (a US onshore company), SALIC (an offshore company but paying US Federal tax), Titan Life and Annuity Ltd (an offshore company in Bermuda), and Bermuda Life Insurance Co Ltd (also an offshore company in Bermuda in the Argus Group).

(v) At the same time (the end of January 2003) Mr McCann was sent projections by Bermuda Life Insurance Co Ltd.

(vi) At about that time spreadsheets were prepared comparing the rates of AIG, SALIC and Generali.

(vii) On 13 February 2003 Mr Watlington was sent by Bermuda Life further details concerning its offshore life policies.

(viii) On 14 February 2003 Mr Watlington was sent by Windward Management Ltd of Bermuda (which may have been a broker) details of the Titan Life and Annuity Ltd offering.

(ix) Mr McCann in February 2003 had a medical examination for the purposes of a placement of the life policies with SALIC, if the Plaintiff decided to go with SALIC.

(x) On 5 March 2003 Mr Mercer of SALIC sent an email to Mr Watlington with an offer of its charges for life policies.

(xi) On 18 March 2003 the Second Deloitte Report was sent to Mr McCann and to the Plaintiff. Deloitte recommended that the Spring and Summer Trusts be domesticated in the USA, but noted that this was not accepted. The two most competitive offers were described as being from Pacific Annuity and Life (an onshore US company) and SALIC. A detailed comparison with these companies' rates, and the financial strength of these companies, was set out, and Pacific Annuity and Life was recommended as being the financially stronger company.

(xii) Mr Wilkey thereafter carried out further enquiries as to the strength of SALIC and its immediate parent company in the Cayman Islands, and the relationship between them.

(xiii) By 22 April 2003 Mr Wilkey was researching AIG, having received details of the likely charges (see the email to him from Financial Architects dated 3 April 2003 and attached spreadsheets).

(xiv) During April 2003 Mr Wilkey and Mr Mercer of SALIC engaged in discussions by email about potential tax charges if the Plaintiff took these out with SALIC.

(xv) On 30 April 2003 Mr Wilkey in an email to Mr Watlington reviewed the advantages and disadvantages of placing any replacement life policies with AIG, Pacific or SALIC.

(xvi) On 21 May 2003 Mr Watlington sent an email to Deloittes with a copy to Mr McCann setting out his understanding that the Plaintiff needed to make a decision between AIG and SALIC and pay the premium by 28 May 2003 (the last date on which Mr McCann's existing medical report would remain valid).

(xvii) On 23 May 2003 Mr Wilkey reported to Mr Watlington by email a further improvement in the terms offered by SALIC for new life policies.

(xviii) On 26 May 2003 Mr Watlington sent by fax to Mr Hubbard (who was then in Switzerland: paragraph 29 above) a spreadsheet comparing what was offered by AIG and SALIC.

103. Several of these comparisons related to US onshore companies offering onshore life policies (as opposed to Generali's Spring and Summer Policies which were offshore policies). Indeed Mr Wilkey more than once recommended that onshore policies should be contracted for. As the Court has already stated in paragraph 77 above, it was inevitable that some of the comparisons would need to be made with onshore companies, because of the difficulties in securing details of offshore private placement policy offers, and a comparison with onshore quotations was acceptable since private placement quotations would be likely to offer lower fees.

104. The decisions that Generali was not competitive in respect of the life policies, and that the Spring and Summer Policies were to be replaced with AIG policies, were made on 26 May 2003, as set out in paragraphs 29 to 32 above. The evidence of Mr Watlington (Day 2 pp.161-168, Day 3 pp 4-7, Day 3 pp. 22, 24, 26-37) and Mr Hubbard (Day 3 pp.98-102, pp.135-142) in general confirmed that the relevant decision as regards the competitiveness of Generali's fees was finally taken that day, though it had been clear to the Plaintiff for some time before, that this decision was inevitable, given what was available in the market. The Court accepts the evidence of Mr Watlington and Mr Hubbard in this regard. As Mr Wessels pointed out, there was no documentary evidence directly relating to this decision; but in the Court's judgment this decision was inherent in all the discussions on 26 May 2003, including those recorded in Mr Watlington's memorandum of 27 May 2003.

The Winter Policy

105. In relation to this annuity policy, the consideration of the market had started well before 26 May 2003. So in the Second Deloitte Report of 18 March 2003 Mr Wilkey concluded that the Mortality and Expense charges under the Winter Policy were "*25% higher than the offers currently on the table*". The email exchanges between Mr Wilkey and Mr Mercer of SALIC in April 2003 covered the annuity as well as the life policies, as did the email exchanges on 23 May 2003 between Mr Wilkey, Mr Watlington and Mr McCann with specific reference to SALIC's offers for an annuity policy.

106. Between June and November 2003 there appears to have been no further detailed consideration as regards the Winter Policy and whether the fee levels were or were not uncompetitive. Consideration of these questions seems to have started again in December 2003. By that time Mr Nowotny had been engaged as a further adviser, and on 29 December 2003 he sent an email to Messrs McCann, Wilkey and Watlington in which he indicated that American General Life (AGL), a subsidiary of AIG, had in similar cases offered a Mortality and Expenses fee of about 0.20%, and that an existing proposal at 0.275% for 20 years was in his view a "*good deal for all concerned*". Mr McCann sent an email on the same day (29 December 2003) to Messrs Wilkey, Watlington and Nowotny. He referred to an offer by SALIC of 0.325 for the first 10 years, and 0.25 for the following 10 years. He then stated (inter alia):

> *"To avoid a Generali cancellation penalty, their present 40 bps has to be shown to be uncompetitive. And in our Claim Summary [which the Court understands to be concerned with a claim against Regent and Royal Bank of Canada], I believe Mr N[owotny] used 25 bps as a comparison based on SALIC issuing all three policies. He also felt Marsh Mac could have obtained around 20 in the market. Given the above, would you suggest that James [Watlington] offers them 27.5 for 20 years to place the funds."*

107. Mr Wessels submitted that this and other emails from Mr McCann showed that it was Mr McCann (and not the Plaintiff) who had already decided to reject Generali and surrender the Winter Policy, and simply to search for means to be able to show that the Generali terms were uncompetitive. There was some force in this submission. But the Court's conclusion, having heard the evidence of Mr Watlington and Mr Hubbard (especially in cross-examination by Mr Wessels), is that though Mr McCann was pressing for replacement, in reality the Plaintiff was making the decisions, and Mr McCann was accepting that it was for Mr Hubbard and Mr Watlington as directors of the Plaintiff to make the decision independently as the trustee, though naturally taking into account Mr McCann's views as both settlor and beneficiary.

108. On the same day (29 December 2003) Mr Watlington sent to Messrs McCann and Wilkey the text of the email of 12 December 2003 from Mr Mercer of SALIC quoted in paragraph 35 above. In the course of further investigation of the market Mr Wilkey obtained a further quotation from an onshore company, and on 16 January 2004 Mr Watlington sent details of this to Mr Mercer of SALIC stating (inter alia):

> *"Our advisers have received a quotation based on an Annuity with the balance of US$35 million for which they would be willing to offer the following terms:*
>
> *1. DAC charge – 10 BPS on premium*
>
> *2. M & E – 22.5 BPS years – 20; 15 BPS years – 21+*
>
> *We understand the quote to represent all the charges associated with the purchase."*

Mr Watlington went on to deal with a tax question which he asked Mr Mercer to answer. Mr Mercer responded by the email quoted in paragraph 36 above, and answered the tax question as set out in paragraph 37 above. There followed the email exchanges referred to in paragraphs 38-42 above.

109. The evidence of Mr Watlington (Day 2 pp.170-180) and Mr Hubbard (Day 3 pp.101-104), viewed in the light of these contemporaneous documents, shows, in the judgment of the Court, that they decided on behalf of the Plaintiff that the terms of Generali's Winter Policy were not competitive with the terms available for an annuity in the offshore private placement market and therefore the Winter Policy should be surrendered, and that the Plaintiff should take out a replacement annuity policy with SALIC rather than AIG because SALIC's terms were more competitive and they were satisfied that SALIC'S financial strength and the security of the policy to be taken out would be appropriate.

110. The Court concludes that the answer in respect of Issue no.5 in relation to each of the three policies is that the Plaintiff by Messrs Watlington and Hubbard formed a judgment that the fee levels charged by Generali under each policy were not competitive, being a judgment in accordance with the terms of the Endorsements no.1.

Issue No. 6

Whether the Plaintiff made a judgment in accordance with each of the policies as amended by the Endorsements.

111. The answer given by the Court in respect of Issue no. 5 is an answer also to this Issue.

Issues Nos. 7 and 8

Whether, if a judgment was made by the Plaintiff, the exercise of the judgment in respect of each of the policies as amended by the Endorsements was made unreasonably (Issue No. 7) or perversely (Issue No. 8).

112. The Court takes these two Issues together because it considers that the questions raised are in reality identical.

113. The main points raised under these issues by Mr Wessels can be summarised in this way:

    (i) the Plaintiff failed to take account of fund managers' fees;

    (ii) the Plaintiff made inappropriate comparisons with fees charged by US onshore insurers;

    (iii) the Plaintiff failed to make the appropriate enquiries, including enquiries of Generali, and failed to consult Generali or to give Generali the opportunity to offer to lower its fees further.

114. The Court has held that the words "*fee levels*" in the fourth bullet point in the Endorsements no.1 meant the levels of fees charged by the insurers themselves – the Mortality and Expense fees, and did not include the fees of fund managers. The Court considers these Issues on that footing. But later the Court will consider what the position would have been if the Court had held that "*fee levels*" included the fees of fund managers.

115. Even though "*fee levels*" do not include investment managers' fees, Mr Wessels submitted that such fees were relevant to the Plaintiff's decision-making, because, he submitted, insurers' Mortality and Expense fees are often much reduced, and subsidised by the insurers sharing the investment managers' fees. Mr Wessels relied primarily on the evidence of Mr Le Boeuf, who indicated that such fee sharing was prevalent in the US retail market, and had moved also into the private placement market. Mr Le Boeuf's evidence was that by reducing their Mortality and Expense fees to a low level the insurers gave the appearance of being more competitive and presenting a better deal than they were actually offering, since the investment managers charged higher fees (perhaps by 20 to 40 base points) to accommodate such a share for the insurers. He also appeared to be saying that it was not usual for such a practice to be disclosed to the insurers' clients. He said that in the retail market it might have to be disclosed, and he could find out whether an insurer was engaging in this practice by a careful reading of the footnotes to the insurers' prospectuses. In the private placement market it was not disclosed, and could be discovered only by comparisons with other insurers' fees including the investment managers' fees they offered.

116. Mr Le Boeuf accepted Mr Cottingham's evidence that AIG was one insurer which refused to enter into any such fee-sharing, regarding such a practice as involving an unacceptable conflict of interest. But in relation to SALIC, his opinion was that the Mortality and Expense fees SALIC charged the Plaintiff for the replacement annuity policy were so low that this indicated that probably SALIC was sharing in the investment managers' fees.

117. Mr Cottingham's evidence was that in the offshore private placement market the essence of the policies was that the policy holder was able to choose the investment funds in which its premium moneys were to be invested. These were subject to regular review and changes, as was the case with the Generali policies, and as was shown to be the case with the SALIC annuity policy. Further, the majority of the policy moneys were invested with US Trust both when the Generali policies were in force, and after that when the AIG and SALIC policies were in force. He accepted that a large insurer might be able to negotiate special rates and some fee sharing in the retail market, in which the identity of the investment funds is established by the insurer in advance, and the retail policyholder is given no choice. But in the international private placement market that would be unlikely to be achieved, because the policy holder would be able to determine in which funds its premium was to be invested. He

stated that investment fund fees would vary according to the complexity of the fund management, whether the fund was a bond fund or an equity index fund, or on the other hand a hedge fund or an emerging markets fund which would be much more expensive to manage; and this would make any fee-sharing the more difficult to achieve. He stated that to assume that US domestic insurers' low Mortality and Expense fees were low because of such fee-sharing would be "*a dangerous assumption to make, because there are so many other factors that could affect*" the Mortality and Expense fees. A low level of Mortality and Expense fee in the offshore market might indicate that the insurer, particularly a smaller one like SALIC, had decided to expand its business by reducing its fees and making them more competitive, rather than spending large sums on, for example, a TV advertising campaign. That in his opinion was the more likely explanation for the level of SALIC's Mortality and Expense fees. By expanding its business with the large premium from the Plaintiff SALIC would be able to spread its fixed costs over a larger amount of business, making the low fee level a useful tool for enabling its business to be profitable.

118. As the Court has stated above, where there is a difference in the evidence of the two experts the Court prefers that of Mr Cottingham: he was a considerably more independent witness than Mr Le Boeuf, and he had more experience of the offshore international private placement market than Mr Le Boeuf, whose experience and evidence appeared to be largely related to the US retail market and to the US private placement market, and only to a limited extent the offshore international private placement market. There was in fact no evidence before the Court that any of the insurers compared with Generali (at which the Plaintiff or those advising the Plaintiff looked) engaged in fee-sharing with fund managers whether they were onshore US companies or offshore companies. Mr Le Boeuf's conclusion that SALIC's fees were as low as they were because of fee-sharing was, in the Court's view, speculation; and no attempt appeared to have been made to find out the facts relating to the SALIC policy. The Court concludes that Mr Cottingham's opinion, that SALIC would probably have quoted a low level of fees in order to increase its business and spread its fixed costs over a wider range of business, was more likely to be correct.

119. The evidence of the Plaintiff's witnesses was that they left investment fund fees out of account because (i) the Endorsements no.1 were directed to the Mortality and Expense fees of Generali (or similar fees charged by other insurers) in the market); (ii) the primary investment fund used before and after the change was US Trust and its fees would not change; (iii) the Plaintiff as the policy holder would have the power to decide in which funds its premium moneys were to be invested, and if a fund manager's fees appeared to be high (perhaps because of a fee-sharing arrangement) the Plaintiff would be able to decide that its moneys were not invested with that fee manager. In the absence of any evidence showing that any of the insurers compared with Generali by the Plaintiffs had low fees because of fee-sharing, the Court concludes that the Plaintiff was entitled to concentrate on the Mortality and Expense fees, and to ignore investment fund managers' fees.

120. However, in this paragraph the Court assumes (in case this action were to go further, and this Court's construction of "*fee levels*" were held to be wrong) that "*fee levels*" did include all the fees charged by insurers including those of investment managers. The question in that event would be whether the Plaintiff's decisions as to the competitiveness of Generali were vitiated by the Plaintiff's failure to investigate further the fund managers' fees in relation to all the comparator insurers. The Court's conclusion on all the evidence before the Court is that the same answer would be arrived at. The fact that the Plaintiff as the prospective policy holder would be able to choose the fund managers at the outset and to change them at intervals of the Plaintiff's choosing meant that the Plaintiff would be able to control the level of fund managers' fees. In those circumstances the possibility of the insurers being able to lower their Mortality and Expense fees by sharing in fund managers' fees (which would have to be increased – markedly, according to Mr Le Boeuf – so as to enable the insurers to receive their share) would be sufficiently remote to make it a factor which the Plaintiff could appropriately ignore, as the Plaintiff did.

121. So the Court's conclusion is that the Plaintiff was entitled to leave out of account the fees of investment managers in its decision-making.

122. The central point in this regard is that the Plaintiff obtained offers of policies comparable to the Spring, Summer and Winter Policies from offshore insurers, AIG and SALIC, which were at fee levels definitely below those of Generali. The Plaintiff chose AIG for the life policies and SALIC for the annuity policy. The Plaintiff took fully into account in respect of both AIG and SALIC what it had learned of the security of both these insurers. The process which the Plaintiff had undertaken, though perhaps less professional in its approach than one undertaken by lawyers, was a reasonable one and valid for the purposes of the Endorsements no.1.

123. Mr Wessels submitted that the Plaintiff inappropriately compared Generali's fees (which were for policies in the international offshore market) with the fees of insurers in the US onshore market. The Court has already indicated its view as to the range of "*market competition*" which the Plaintiff was entitled to consider in paragraph 77 above. As there set out, the offshore market is relatively opaque (it being difficult to ascertain what fees are in fact being charged by other insurers) and relatively small, and apart from the fees actually offered to the Plaintiff by other insurers in the offshore market it was clearly difficult for the Plaintiff to obtain any substantial number of comparables in that market. So in the Court's judgment it was appropriate to take into account the fee levels in the onshore market as a means of checking whether the fees actually offered to the Plaintiff were realistic and suitable for comparison with Generali's fees.

124. Mr Wessels submitted strongly that the Plaintiff ought to have consulted Generali fully. Indeed at one point it appeared that he was contending that the Plaintiff had a contractual obligation to consult Generali, though this was a line of argument which in the end he did not pursue. Mr Wessels relied on Mr Watlington's memorandum to Mr Hubbard dated 20 November 2002 in which Mr Watlington stated as quoted in paragraph 22 above. Mr Watlington was there telling Mr Hubbard that the Plaintiff's responsibility was either "*to remedy the disparity with Generali*", or to move the funds to another insurer. Mr Wessels pointed out that in fact no attempt was made to remedy this disparity with Generali, and Generali was to some extent kept in the dark in relation to the life policies (though the First Deloitte Report was sent to Generali) and completely in the dark in relation to the annuity policy. The Court's conclusion on this point is that the submission is not a valid one. The Plaintiff owed Generali no contractual obligation to consult Generali when reaching its decisions. What the Plaintiff had to form a judgment about was whether Generali's **existing** fee levels "*remain substantially competitive*", and not whether Generali could be persuaded to lower those fee levels even further.

125. Further, the suggestion that Generali was kept in the dark is misconceived. The history summarised above shows that Generali was at all times well aware that the Plaintiff was considering the surrender of the three policies and their replacement with policies taken out with other insurers. This is clear from paragraphs 23, 26 and 33 above, and after the initial decision had been made in respect of the Winter Policy from paragraphs 41 and 45-49. As the Court has noted in paragraphs 28 and 43 above, though Generali was aware that the Plaintiff was examining the competitiveness of the three policies, Generali refrained from asking about the progress of this examination, from putting forward any offers of better terms, and from seeking to show that Generali's fees were substantially competitive with market competition. Having itself remained silent, it hardly lies in Generali's mouth now to complain of not being consulted by the Plaintiff, or given the opportunity to offer to lower its fees further. In any event the Court concludes that Mr Watlington and Mr Hubbard were justified in assuming that Generali, having brought their initial fee levels down by a very considerable amount in the two tranches covered by the Endorsements nos.1 and 2, were most unlikely to agree to any further reductions.

126. The Court concludes on Issues nos.7 and 8 that the exercise of the Plaintiff's judgment in respect of each of the three policies was not made unreasonably or perversely.

Issue No.9

Whether, if a judgment was made by the Plaintiff, the exercise of the judgment in respect of each of the policies as amended by the Endorsements was made in bad faith.

127. As indicated in paragraph 80 above, a claim that the Plaintiff acted "*in bad faith*" was pleaded. At the pre-trial review Mr Wessels was asked about this plea, because in the judgment of the Lieutenant Bailiff such a plea involved a charge of dishonesty. Mr Wessels indicated that no charge of dishonesty was made against the Plaintiff. But the plea was not withdrawn (and this Issue was included in the agreed Statement of Issues provided at the start of the last day of the trial) until Mr Wessels finally withdrew it in his closing submissions. Accordingly this Issue no longer arises.

Issue No.10

If the nine factor implied term is found by the Court to be implied into Endorsement no.1 and/or the policies, whether the Plaintiff had regard to all of the nine factors in the exercise of its judgment in respect of each of the policies as amended by the endorsements.

128. As appears above under Issue no.3 (paragraphs 90-94) the nine factor term is not to be implied in any of the policies or endorsements.

129. No reference was made in this or any other of the Issues to Mr Wessels' alternative argument that the nine factors were factors to be taken into account by the Plaintiff if its judgment was to be reasonable and not perverse. But it is right that the Court should here deal with that alternative argument. The Court repeats what is set out in paragraph 92(iv) above. In the judgment of the Court those factors which the Court has there decided were relevant for the Plaintiff to take into account were taken into account by the Plaintiff. The Court will not refer at length to the evidence of Messrs Hubbard, Watlington and Wilkey in this regard; but that evidence showed that the relevant factors were taken in account, and in particular the financial strength of AIG and SALIC and the security of the policies which they offered, as well as the competitive offers AIG and SALIC made at fee levels well below those charged by Generali.

Issue No.11

Whether Generali gave an undertaking not to retain the fees in issue

130. This Issue turns on the wording of Mr Le Page of Generali's email of 1 March 2004 to Mr Watlington quoted in paragraph 50 above. In the judgment of the Court the words "*after which no further policy charges will accrue*" clearly referred only to the monthly charges, and did not refer to the question of "*claw-back*" under the Endorsements no.1. There is no basis for the contention that this email amounted to a binding undertaking not to exercise any rights, if any, to the claw-back.

Issue No.12

Whether Generali wrongfully clawed back fees totalling US$809,102 from the surrender proceeds of each of the policies in purported reliance on Endorsements no.1 and 2

131. In the light of the Court's conclusions on the previous Issues, the Court decides that Generali was not entitled to make any retention based on the Endorsements, and wrongfully did so.

Issue No.13

Whether the Plaintiff is entitled to recover its loss on the basis of its legal and beneficial interest (as Trustee for the Winter, Spring and Summer Trusts) in the policies as amended by the Endorsements or the proceeds thereof.

132. At an earlier stage of the proceedings it appeared that the Plaintiff was seeking to rely (perhaps in the alternative) on the rights of AIG and SALIC in the surrendered policies, which had been assigned to the Plaintiff. Indeed pleas to that effect appeared in the Amended Cause. However, Miss Ozanne has made clear to the Court that the Plaintiff does not seek to rely on any such assigned rights, since she takes the view that the assignments were ineffective, having been made without Generali's consent. Mr Wessels did not demur. In any event the Court has considerable doubt whether AIG or SALIC at any time had any rights in the policies which each of them purportedly assigned.

133. The claim as presented by Miss Ozanne to this Court is based on the assignments from Regent to the Plaintiff which were assented to by Generali by the Endorsements no.3 to each policy. The Court understands that Mr Wessels does not seek to contend that the Plaintiff is not entitled to any rights it has under the policies by virtue of those assignments and those Endorsements to the policies. Accordingly in the judgment of the Court the Plaintiff is entitled to recover the monies retained by Generali wrongfully and in breach of the terms of each of the three policies.

Issue No.14

Quantum – Whether the Plaintiff is entitled to recover the following losses arising from the claim.

14.1 Judgment in the sum of US$809,102.

134. As stated above, the Plaintiff is entitled to recover the monies wrongfully retained by Generali amounting to US$809,102.

14.2 Trustee costs of US$234,785 as at 31 August 2010, together with any further trustee costs incurred up to and during the trial.

135. It was confirmed in his evidence by Mr Hubbard that all these costs incurred by the Plaintiff at the expense of the Winter, Spring and Summer Trusts were incurred in connection with the proceedings against Generali. In so far as any of these costs could be recovered as costs in and of the action, those costs will have to be considered in the context of the assessment of the costs when this judgment has been delivered. Here the Court is concerned solely with the question whether the Plaintiff's own costs, which are not recoverable as costs in and of the action, can be recovered as damages flowing from Generali's breaches of the terms of each of the three policies.

136. Where a cause of action is for breach of a contractual obligation to pay money, the amount recoverable is normally limited to the amount of the debt and interest. This will be the measure of damages no matter what inconvenience the Plaintiff has suffered from the failure to pay on the day payment was due. The reason for this rule in English law appears to be that any further damage is too remote a consequence of the non-payment because it is not within the contemplation of the parties. But where the circumstances are such that a special loss is foreseeable at the time of the contract as a consequence of non-payment, damages may be recoverable for that loss: see Halsbury's Laws of England, Damages volume, and for example Trans Trust SPRL v Danubian Trading Co Ltd [1952] 2 QB 297; [1952] 1 All ER 970 CA, and also at first instance per McNair J [1952] 1 KB 285; [1952] 1 All ER 89: and also the discussion of this and other cases in McGregor on Damages. Such authorities were not cited to the Court, and it appears that they had not been researched.

137. There is a potentially obvious answer to the claim for this head of damages that, though the incurring by the Plaintiff as trustee of the costs claimed resulted from the non-payment by Generali, all such costs were incurred in the usual way in dealing with the claim against Generali, and there were no special factors resulting in this head of claim not being too remote. As Mr Wessels submitted, if such costs could be recovered in this action, there would appear to be no reason why they could not be recovered by any plaintiff, whether or

not a trustee. This may be the correct answer to this Issue 14.2, and it may be thought by Miss Ozanne that there is no point in pursuing this head of claim further. If, however, she considers it appropriate to pursue this head of claim after having researched the relevant case law, including authorities more recent than Trans Trust, the Court will be willing to hear further argument when this judgment is delivered, though the Court gives no encouragement to any such further argument, and the risk of adverse costs orders would have to be borne in mind.

Issue 14.3 Costs and Disbursements

138. The Court will hear argument as to the appropriate order for costs when this judgment is delivered.

Issue 14.4 Interest-pre and post judgment

139. The Plaintiff claims interest before and after judgment on the basis of simple interest on the sum wrongfully retained at the rate of 8% per annum. The Court will hear argument as to the rate and period for which interest is to be ordered. It is to be hoped that this can be agreed between the Advocates with a figure to the date when judgment is delivered, and a daily rate thereafter.

Case Preparation

140. In paragraph 41 of the Judgment of the Court of Appeal in Pirito v Curth (2003) GLJ, that Court made recommendations for the preparation of files for presentation to the Court of Appeal. In the judgment of the Lieutenant Bailiff similar preparation of the files is needed when cases are presented to the Royal Court for trial in civil proceedings (and in interlocutory applications, especially at case management hearings and pre-trial reviews). His recommendations (which are naturally subject to the approval of the Bailiff) are based also on those which he made in paragraph 82 of his judgment in Sohail Masood et al v. Mohammad Zahoor et al Royal Court, 3 November 2006, unreported (coincidentally the same Advocates appeared in that case as in the present case), and are as follows:

    (a) there is needed a file containing pleadings, interlocutory applications and orders of the Court and judgments, and other formal documents filed or delivered in the course of the action (the plaintiff's advocate should perhaps open such a file when the action starts and keep it up to date so that it is ready to be put before the Court on any interlocutory hearing including case management and pre-trial review hearings, and then is ready for the trial);

    (b) if necessary, a file of any affidavits to which the parties wish reference to be made;

    (c) a core file of documents in chronological order;

    (d) the file or files of documents to which the parties propose to refer in the course of the trial, in which the core documents should appear again; these should be in strict chronological order (unless there is a good reason for any other order);

    (e) a file or files of all authorities relied on by the parties, divided into sections: first, Guernsey authorities and Guernsey statutes; secondly; any Jersey authorities; thirdly, any Privy Council authorities; fourthly, any English authorities; each section being put in chronological order.

141. In the present case there was not a full file such as (a) above, and such a file is likely to be needed when questions of the costs of this action are considered. Affidavits were not assembled as in (b). The core file was excellent, but the core documents were not also in the general file of documents, which meant that it was necessary to dart to and fro between the

core file and the general file. The general file had many duplicated documents and was not in full chronological order. The files of authorities were not assembled as in (e). If the scheme in paragraph 140 above had been adopted, it would have much helped the Judge and Jurats in finding their way round the files, and in finding specific documents when they were needed to be found.

IN THE ROYAL COURT OF THE ISLAND OF GUERNSEY

ORDINARY DIVISION

BETWEEN

WOODBOURNE TRUSTEES LTD

Plaintiff

and

GENERALI WORLDWIDE INSURANCE COMPANY LIMITED

Defendant

Before Lieutenant Bailiff Richard Southwell QC

Advocate for Plaintiff: A M Ozanne

Advocate for Defendant: J M Wessels

JUDGMENT

1. This further judgment deals with ancillary matters (including costs) following the judgment of the whole Court which was formally handed down on 17 January 2011 (having been delivered to the parties in draft on 6 December 2010).

Trustees' Costs

2. At the trial a claim was made in respect of costs incurred by the Plaintiff Trustee (and paid by the Spring, Summer and Winter Trusts) in connection with these proceedings. The claim amounted to US$234,785 at 31 August 2010, but would have continued to increase up to and during the trial. This claim was considered in paragraphs 135 to 137 of the judgment. The Court indicated in those paragraphs that it would be willing to hear further legal argument on this head of claim, if so wished by the Plaintiff, in particular in respect of the issue whether or not such costs are too remote to be recoverable as damages flowing from the Defendant Generali's failure to make timely payment of the sums which this Court has now held to have been due and payable by Generali to the Plaintiff. The reason for this indication of readiness to hear such further argument was that there appeared not to have been research into the position where breach of a contractual obligation to pay a sum of money

is the foundation of the Plaintiff's claim. At the hearing of the ancillary matters on 17 January 2011 Advocate Ozanne sought briefly to re-argue this issue.

3. Miss Ozanne referred first to the basic principles of recovery of damages as set out in *Hadley v Baxendale* 9 Exch 341 and *Victoria Laundry v Newman* [1949] 2KB 528 CA: see at pages 539-540 the following passage:

> *"What propositions applicable to the present case emerge from the authorities as a whole, including those analysed above? We think they include the following:*
>
> *(1) It is well settled that the governing purpose of damages is to put the party whose rights have been violated in the same position, so far as money can do so, as if his rights had been observed: (*Sally Wertheim v Chicoutimi Pulp Company *[1911] AC 301*). *This purpose, if relentlessly pursued, would provide him with a complete indemnity for all loss de facto resulting from a particular breach, however improbable, however unpredictable. This, in contract at least, is recognized as too harsh a rule. Hence,*
>
> *(2) In cases of breach of contract the aggrieved party is only entitled to recover such part of the loss actually resulting as was at the time of the contract reasonably foreseeable as liable to result from the breach.*
>
> *(3) What was at that time reasonably so foreseeable depends on the knowledge then possessed by the parties or, at all events, by the party who later commits the breach.*
>
> *(4) For this purpose, knowledge "possessed" is of two kinds; one imputed, the other actual. Everyone, as a reasonable person, is taken to know the "ordinary course of things" and consequently what loss is liable to result from a breach of contract in that ordinary course. This is the subject matter of the "first rule" in* Hadley v Baxendale *(9 Exch 341). But to this knowledge, which a contract-breaker is assumed to possess whether he actually possesses it or not, there may have to be added in a particular case knowledge which he actually possesses, of special circumstances outside the "ordinary course of things," of such a kind that a breach in those special circumstances would be liable to cause more loss. Such a case attracts the operation of the "second rule" so as to make additional loss also recoverable.*
>
> *(5) In order to make the contract-breaker liable under either rule it is not necessary that he should actually have asked himself what loss is liable to result from a breach. As has often been pointed out, parties at the time of contracting contemplate not the breach of the contract, but its performance. It suffices that, if he had considered the question, he would as a reasonable man have concluded that the loss in question was liable to result (see certain observations of Lord du Parcq in the recent case of* A/B Karlshamns Oljefabriker v Monarch Steamship Company Limited [*1949] AC 196.*
>
> *(6) Nor, finally, to make a particular loss recoverable, need it be proved that upon a given state of knowledge the defendant could, as a reasonable man, foresee that a breach must necessarily result in that loss. It is enough if he could foresee it was likely so to result. It is indeed enough, to borrow from the language of Lord du Parcq in the same case, at page 158, if the loss (or some factor without which it would not have occurred) is a "serious possibility" or a "real danger." For short, we have used the word "liable" to result. Possibly the colloquialism "on the cards" indicates the shade of meaning with some approach to accuracy."*

I should add in relation to proposition (6) above that "liable to result" is the test which is in my judgment the appropriate test.

4. In relation to obligations to pay money Miss Ozanne cited a 19th century case, *Behn v Royal Bank of Liverpool* (1870) LRS Exch 92, which shows that particular losses resulting from a failure to pay under a contract were in that case recoverable by reason of the specific knowledge of special circumstances. She cited also *Trans Trust Sprl v Danubian Trading Co Ltd* [1952] 2 QB 297 CA, in which the breach consisted of a failure to open a confirmed letter of credit to meet the price of some steel to be paid by the defendants to the plaintiffs. In that case the Court of Appeal held that the plaintiffs' loss of profit on the transaction must have been in the contemplation of the parties as a consequence of a breach of the contract by failure to open the letter of credit. On the other hand the Court of Appeal held that loss resulting from a claim against the plaintiffs by a sub-purchaser was too remote and so irrecoverable, because on the evidence not within the contemplation of the parties. The importance of the decision in *Trans Trust* lies, not in the decision on the particular facts of that case, but rather in the decision as a matter of principle that damages may be recoverable for a breach of contract consisting of no more than a failure to pay money: see per Denning LJ at p.306 and Romer LJ at p.307.

5. Miss Ozanne seeks to apply these principles in the present case in this way. She says that the costs incurred in relation to these proceedings by the Plaintiff Trustee Woodbourne (which the three trusts had to bear) are not too remote. She contends that when Generali contracted with the Plaintiff in respect of each of the three trusts, Generali knew that it was contracting with a professional trustee, and that if it wrongfully withheld money due to the trustee, this would cause the trustee to incur costs (apart from legal costs) measured by the time spent by persons in the Plaintiff trustee company in connection with the proceedings, which the three trusts would have to pay in order to pursue these legal proceedings against Generali to recover the moneys wrongfully withheld. So she contends that it was in the reasonable contemplation of Generali that the Plaintiff would incur such costs, which the three trusts would have to pay. If the Plaintiff cannot recover such costs from Generali, then the moneys which the Court has ordered to be paid will be reduced by the amount of the Plaintiff's costs, so that the three trusts through the Plaintiff will recover, net, substantially less than the amounts which Generali failed to pay. The "special factor" in relation to this head of damages is, Miss Ozanne contends, Generali's knowledge that it was contracting with a professional trustee, and that if such trustee had to sue Generali to recover money lawfully due from Generali, the three trusts and the beneficiaries would incur the expense of the trustee's costs in pursuing litigation against Generali.

6. On the other hand Mr Wessels for Generali points out that in any case involving a company (or indeed an individual) there will be some expense incurred due to personnel of the company (or the individual) having to devote time and effort to the case while it is ongoing. He argues that in the present case there is no evidence of any special knowledge or contemplation which would distinguish this case from the ordinary run of cases in which expense incurred by the plaintiff is recoverable only in so far as falling within the categories of litigation costs which can always be recovered. He relied on one recent authority, *Aerospace Publishing Ltd v Thames Water Utilities Ltd* [2007] EWCA Civ 3

in the English Court of Appeal (apparently unreported). But *Aerospace* dealt with a rather different point, which related to the circumstances in which staff costs incurred in investigating or mitigating the wrongful act (in Aerospace a tort, but similar considerations would apply to a breach of contract) could be recovered. The Court of Appeal held, following an earlier decision of that court in *Standard Chartered Bank v Pakistan National Shipping Corporation* [2001] CLC 825, that to recover such costs it must be shown that the staff time involved had led to disruption of the claimant's business, or loss of profit, or increased costs in carrying out a project.

7. In my judgment Mr Wessels' contention is correct. The costs claimed were no more than costs inevitably incurred by the Plaintiff in liaising with its lawyers to ensure that the action proceeded efficiently. There was no general or specific foreseeability or contemplation by the parties which could enable the Plaintiff to claim such costs as damages flowing from Generali's failure to pay. The Plaintiff did not rely on any disruption of its business, or loss of profit occasioned by the failure to pay. As Mr Wessels observed, if this claim could succeed, it would follow that any company involved in litigation as a plaintiff could recover its costs of dealing with the litigation as damages, a proposition for which there is no authority, and which does not succeed in this case.

Legal Costs

8. It is common ground that the Plaintiff is entitled to its costs of this action on the recoverable basis. But the Plaintiff claims certain of its costs on a partial indemnity basis, pursuant to Rule 83 of the Royal Court Civil Rules 2007. I therefore have to consider each of the grounds on which Miss Ozanne relies.

9. The first is that by "without prejudice save as to costs" letters dated 28 October and 21 November 2008 the Plaintiff's Advocates A O Hall offered to compromise the action for US$1,571,504 and US$1,157,133.99, plus agreed or assessed costs, respectively. Those offers were not accepted by Generali, and Generali made no counter-offer. (I should, however, mention that there had been previously an unsuccessful attempt at mediation.) The lower of these offers was in fact at a figure higher than the recovery to which the Plaintiff is entitled under the judgment of this Court by about US$57,000. So this offer does not give rise to the normal consequence that, having offered to take the same or less than it actually recovered, the Plaintiff would be awarded indemnity costs from the date when the offer should reasonably have been accepted. Nevertheless Miss Ozanne submits that all the Plaintiff's costs from 21 November 2008 should be assessed on the indemnity basis, because the offer though too high was realistic and reasonable and thereafter no effort was made by Generali to settle the action by making a counter-offer.

10. Mr Wessels argued that where an offer to settle is pitched too high it would be inappropriate to grant indemnity costs, and that there was no sign that the Plaintiff would have accepted a lower offer. But he accepted that Generali had failed to respond to these overtures from the Plaintiff.

11. In my judgment the making of the offers by the Plaintiff and the failure of Generali to respond are grounds for making a partial indemnity costs order. It would be wrong to take 21 November 2008 or any date near that as the starting point, since the offer was too high. But in an age in which reasonable conduct is expected of all civil litigants the failure of Generali to respond with a counter-offer is conduct which should be marked by an indemnity costs order. I consider that the fair and reasonable order to make is that the Plaintiff's costs from 1st January 2010 are to be assessed, if not agreed, on the indemnity basis.

12. The second ground concerns the many and vigorous battles between the parties concerning discovery of documents, and the late disclosure of some documents by Generali. Miss Ozanne submits that Generali failed to disclose some documents until made to do so by an order of the Court, and that Generali pursued applications for further disclosure by the Plaintiff despite renewed affidavits of Mr Hubbard making clear that all relevant documents had been disclosed. Mr Wessels sought to put the various battles in their proper context, and pointed out that Mr Hubbard's affidavits had to be sworn because the Court had so ordered. Generally in relation to this ground I am not satisfied that any of the skirmishing over discovery was at all out of the ordinary, or would be such as to justify an order for indemnity costs.

13. However, the late production of some documents by Generali just before the trial was thoroughly inappropriate, and could justify an indemnity costs order on its own. But in view of the order indicated in paragraph 11 above it is unnecessary for a separate order to be made in this regard.

14. The third ground concerns the unfortunate position that the Court at the interlocutory stage had been persuaded by Mr Wessels for Generali to order that different questions be put to the parties' rival experts. That might be thought a recipe for confusion, and in the event the trial Court found that it resulted (inter alia) in the evidence of Generali's expert witness being less relevant than it should have been (his evidence was for other reasons not accepted by the trial Court). Mr Wessels submitted that the decision to have different questions was made by the Court, and that the Plaintiff tried to have a preliminary issue decided, but failed to persuade the Court to order such issue. His submission was that the Court having made these decisions, an order for indemnity costs would be inappropriate.

15. In my judgment for Generali to seek to have a different, and in fact irrelevant, question put to their expert was to be regretted, not least because it did not assist Generali in the development of its own case. But Miss Ozanne's criticism of this interlocutory matter is enlarged by reference to the inadequacies of the evidence of Generali's expert which are a different and distinct matter. Though I judge Generali's conduct in securing from the interlocutory Court an order for different questions to have been unwise, it does not quite justify an indemnity costs order in itself and separately from the order indicated in paragraph 11 above.

16. The fourth ground concerns delay by Generali in telling the Court and A O Hall of its availability for a trial in November 2010. This does not justify an order for indemnity costs.

17. The fifth ground relates to the nine factor implied term for which Generali contended, and which was dealt with at length in the main judgment. The point was in the view of the Court a bad point. But an indemnity costs order is not justified.

18. The sixth ground concerns delays by Generali in serving witness statements, the expert's report and a verified supplementary list of documents. Any such delay is to be regretted. But these delays do not justify an indemnity costs order.

19. The seventh ground relates to Generali's witness statements. This ground has from the moment when I first saw the statements caused me much concern. The witness statements as originally filed and served contained a large proportion of matter of which the witnesses were not in a position to speak. In the worst case, the statement of Mr Tradelius, the great majority of the statement consisted in a description of circumstances relating to the case which occurred before he came on the scene at all, as to which he had no personal knowledge at all, and of speculation as to what a missing witness might have thought or done. The Plaintiff by Miss Ozanne protested about this abuse of the Court process. When I had read the statements I arranged a hearing at which I explained to Mr Wessels the unacceptable state of Generali's witness statements, which were not in a form in which they could be shown to the Jurats as the judges of fact. The statements were then reduced in length to some extent, but by no means enough. In the event the evidence given orally by Generali's witnesses was confined by Mr Wessels to what they could properly speak to, resulting in the case of Mr Tradelius in brief evidence about the short period in which, and the limited degree to which, he had been involved. I consider it essential to emphasise that the statement of a witness filed and served before trial should contain only the evidence which the witness can give from their own knowledge, and should not contain (as, for example, did Mr Tradelius' statement) long passages taken from other witnesses, and speculation as to what a person not called as a witness would have thought or done. In my judgment this part of the interlocutory steps fully justifies an order for indemnity costs; and accordingly I order that all the costs incurred by the Plaintiff in connection with Generali's witness statements are to be assessed, if not agreed, on the indemnity basis.

20. The eighth ground concerns what is said to be a failure by Mr Wessels to reveal Generali's stand in relation to the assignments of the causes of action. There is nothing in this to justify any special order. The problem was created by the pleading on the Plaintiff's behalf in the Cause of two sets of assignments.

21. The ninth ground relates to an attempt shortly before trial by Generali to have it ordered that an affidavit and further witness statements be filed by the Plaintiff. Though unfortunate, this does not justify an indemnity costs order.

22. The tenth ground concerns an allegation by Generali in its Defences that the Plaintiff had acted "in bad faith". This was dealt with in paragraphs 80 and 127 of the main judgment. In civil proceedings between private litigants a charge of "bad faith" always involves an allegation of dishonesty. There was no basis for such a charge in the present case, and it should never have been pleaded. At the Pre-Trial Review, as the Judge who had only recently taken charge of the case, I specifically raised this point with Mr Wessels. He assured me that no charge of dishonesty was intended, and I indicated that presumably the Defences would be amended to delete these words. No application to amend was made. The allegation remained throughout the trial, and surprisingly was included as a separate issue, Issue no.9, for the Court to decide in the agreed Statement of Issues provided at the start of the last day of the trial. But Mr Wessels finally withdrew it in his closing submissions. As I have indicated, there was no justification whatever for the making of a charge of "bad faith", and no justification was put forward in the Defences or otherwise. In my judgment this does make appropriate an order that any costs incurred by the Plaintiff in respect of this issue be assessed, if not agreed, on the indemnity basis.

23. The eleventh ground relates to disbursements, of Court fees, to the Plaintiff's witnesses of fact and expert witness, and to LiveNote for the transcription of the trial hearings. No good reason was advanced for these to be assessed on an indemnity basis, and I make no such order.

24. So the orders the court will make for the Plaintiff's costs to be assessed on the indemnity basis are those referred to in paragraphs 11, 19 and 22 above.

Pre-Judgment Interest

25. This has been agreed between the Advocates, as follows:

Spring and Summer Policies	US$ 35,488.72
Winter Policy	US$256,022.36
Total	**US$291,511.08**

Post-Judgment Interest

26. This will have to be paid by Generali at the statutory rate of 8% on the costs and disbursements of the Plaintiff as either agreed or ordered by the Court.

Security for Costs

27. The Plaintiff paid £5,000 into Court as security for Generali's costs. The Court orders that this sum with accrued interest is to be paid out to the Plaintiff's Advocates A O Hall.

Costs of the Hearing on 17 January 2011

28. The Court orders that Generali shall pay 50% of the Plaintiff's costs of and occasioned by this hearing, since in terms of success on the issues raised at the hearing the Plaintiff succeeded in my judgment only in part.