

Product liability: Looking Beyond the Terms of a Judgment

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In a recent case, the Commercial Court has held that an underlying judgment against an insured did not conclusively determine the basis of liability for the purposes of that insured's claim under its product liability insurance. It was open to the insured to contend that it was liable on other grounds or indeed to argue that the decision in the underlying judgment was incorrect.

Product liability policies often exclude contractual liability unless the liability would have attached in the absence of a contract. In the case of *Omega Proteins Limited v Aspen Insurance UK Ltd* (2010) EWHC 220 (Comm), the court considered whether a finding of contractual liability in an underlying judgment prevented a later finding of tortious liability within the same policy cover.

Background

The claimant, Omega Proteins Ltd (Omega), was in the business of processing by-products from animal carcasses used in the meat industry which it supplied to customers. Omega was supplied with animal carcasses by Northern Counties Meat Ltd (NCM). In breach of the contract with Omega, NCM supplied Omega with meat materials which were fit only for disposal within the meaning of *EC Regulation 1774/2002* (a statutory regulation introduced following the BSE crisis). Omega proceeded to mix this material with other material, thereby contaminating the whole resulting mixture, which it then supplied to its customers. The State Veterinary Service discovered the contravention and ordered that the mixture be destroyed.

The Underlying Judgment

A company which had purchased some of the contaminated material began an action for damages for breach of contract against one of Omega's customers. Omega was joined to the proceedings as a third party and, in turn, joined NCM as a fourth. In the underlying case the Commercial Court held that Omega was liable to pay damages for breach of contract to its customer and that NCM was liable to indemnify Omega in respect of this liability.

Unfortunately, NCM was in liquidation and unable to satisfy the judgment. Omega therefore brought the present claim against NCM's insurers, Aspen, under the Third Parties (Rights against Insurers) Act 1930.

Whether or not there was a liability in tort was not something that was considered by the court in the underlying case.

The Policy

The insurance policy provided an indemnity in respect of "all sums which the Insured becomes legally liable to pay" for loss or damage to property caused by any product. This was subject to an exclusion clause for liability arising "under any contract or agreement unless such liability would have attached in the absence of such contract or agreement."

Aspen contended that Omega's claim fell within the exclusion. They argued that the court in the underlying case had conclusively determined that NCM's liability to Omega was in contract and that it was not possible to look beyond the terms of this judgment to find grounds for an alternative claim in negligence.

In support of this contention, Aspen relied upon the observations of *Mr. Justice Tomlinson in London Borough of Redbridge v Municipal Mutual Insurance Ltd* [2001] Lloyd's Rep IR 545 at 550 when he commented, in respect of liability insurance, that the enquiry of whether insurers are liable should "*begin and end with the question on what basis had liability been established*" and that, in his judgment, it was "*normally neither permissible nor possible to look beyond or outside the four corners of the determination itself for the basis of liability to which the insured becomes subject*".

Omega accepted that the liability arose under the contract, but contended that the question of whether there was cover depended on whether such liability would have attached in the absence of the contract.

Omega submitted that it could not be right that the question of whether the insured was entitled to cover under the policy should be determined by the choice of grounds (whether contractual or tortious) upon which a third party elected to rely when bringing a claim against the insured.

Omega argued that Aspen's proposition that it was not possible to look beyond the terms of the underlying judgment would mean re-writing the exclusion clause so as to read "*unless the judge in the trial which established liability had expressed the view that liability would arise in the absence of contract*", or something to that effect. As the question posed by the exclusion clause was hypothetical, on which the judge in the underlying case could not have reached a binding decision, Omega submitted that the parties could not have intended that his failure to make such a decision should conclusively determine whether or not Omega could recover.

The Court's Decision

Mr. Justice Clarke ruled in favour of Omega, agreeing that the correct question for the court to ask was what liability would have attached, on the same facts, in the absence of a contract. Omega was not prevented from making recovery because of the terms of the underlying judgment.

As a first instance decision, Tomlinson J's judgment was not binding on Clarke J and he concluded that even if it was, it was distinguishable because Tomlinson J referred only to what would 'normally' be the position and each case depended on its own facts. In any event, the judge disagreed with Tomlinson J's conclusion and reasoning.

Clarke J instead agreed with and drew support from the judgments in the cases of *West Wake Price v Ching* [1957] 1 WLR 45 and *MDIS v Swinbank* [1999] 2 All ER (Comm) 722 CA. On the basis of these judgments, the judge set out a series of propositions as to the position in liability insurance generally.

Significantly, while agreeing that a judgment, award or agreement may settle the question as to whether a loss is covered by one of the perils insured against, Clarke J stated that it would not be determinative of that question. Unless the insurer was a party to the proceedings, or had agreed to be bound by the outcome, it was open to it to dispute that the insured was liable, or to challenge the basis of that liability. Similarly, the insured could argue that it was in fact liable or contend that it was liable on other grounds. The earlier judgment was conclusive that NCM had to pay Omega the judgment sum, but it was not evidence that NCM had no tortious liability.

Turning to the question of whether liability would have attached in the absence of the contract, Clarke J concluded that it would. He held that NCM would have been liable in negligence for supplying the wrong meat materials to Omega without warning that they were fit only for disposal. This was an action which would foreseeably cause and did cause actual physical damage to Omega's property (the uncontaminated material with which the supplied meat materials were mixed).

The judge held that Omega was entitled to be indemnified by Aspen for all sums which NCM would have been liable towards Omega had there been no contract between NCM and Omega. Omega was not entitled to recover that which it could recover from NCM only in contract, as this would be covered by the exclusion clause.

The Burden of Proof

Clarke J considered obiter the question of the incidence of the burden of proof, concluding that in order for Aspen, as insurer, to bring itself within the exclusion, it needed to demonstrate that the liability arose under a contract and that the exception did not apply. In the present case, the judge said this would have involved showing that: "*in the absence of a contract, there would have been no liability in negligence.*" Aspen was unable to discharge this burden of proof on the facts.

Impact of the Case

The meaning of contractual liability exclusions in relation to liability insurance has been clarified by Clarke J's decision. Such an exclusion will not apply in circumstances where the insured would also have had a liability in tort.

The decision makes it clear that both insureds and insurers may look beyond the terms of an underlying judgment, award or agreement in determining whether the insured's liability falls within the scope of the policy cover. This decision may be of assistance to insureds where a judgment, settlement or award fails to evidence an insured liability. Conversely, it may also be of assistance to insurers who wish to challenge the basis or amount of any liability determined in such a way.