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Dutch Court adopts new approach to test of reasonableness and fairness in primary coverage provisions

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The Supreme Court of the Netherlands[i] issued an important judgment in the treatment of insurance provisions and whether they must pass the test of reasonableness and fairness.

In its decision of 16 February 2024 (ECLI:NL:HR:2024:258[ii]), the Supreme Court put an end to the historic approach where primary coverage provisions do not have to meet the restrictive standard. Going forward, both preventive warranty clauses and primary coverage clauses may potentially be set aside on the principle of reasonableness and fairness.

The decision marks the second time in less than five years that the Supreme Court has instigated a development of law in the area of insurance.

Background

Under Dutch law, a party can invoke article 248 CC Bk 6, par. 2 if a provision in a contract is considered to be contrary to the principles of reasonableness and fairness.

This article reads: "A rule binding upon the parties as a result of the agreement shall not apply to the extent that, in the given circumstances, this would be unacceptable according to standards of reasonableness and fairness".[iii]

This article equally applies to insurance contractsiv, although under Dutch law historically there has been an exception regarding applicability.

To date, the Court has been obliged to determine whether the provision represents a primary coverage provision or a preventive warranty clause.

In the case of a preventive warranty clause, the Court was permitted to judge whether the provision was contrary to the principles of reasonableness and fairness.

However, if the provision was determined to be a primary coverage provision, the test of reasonableness and fairness could not be applied. The underlying intent here is that an insurer is entitled to define the extent of coverage.

Facts

The case follows a horse-riding accident in the Netherlands. The claimant was seriously injured after falling from a horse during a ride supervised by the insured, a horse-riding school. The claimant held the insured liable for damages. The insured claimed for the damages under its liability insurance.

The insurance company rejected the claim, referring to the "rental-clause". This clause prescribed specific diplomas for, in this case, either the employee of the insured party or the injured horseback-rider. The insured stated that in terms of causation it was not acceptable to rely on the clause at issue and invoked the restrictive

standard of reasonableness and fairness.

The insurer stated, on the contrary, that invoking the restrictive standard of reasonableness and fairness was not possible because the clause should be considered as a primary coverage clause.

The Dutch Court of Appeal concurred with the decision of the Court of First Instance that the clause should not be considered as a primary coverage clause but as a preventive warranty clause.

Causation therefore played a role in the interpretation and application of the clause. Non-compliance with the preventive warranty clause was deemed to have caused the damage. However, in this case, the non-compliance was not considered to be the cause of the damage and the Court instructed the insurer to provide cover.

The insurer appealed the decision to the Supreme Court.

Decision

The Supreme Court distanced itself from the *stare decisis*, considering it no longer necessary to first identify a clause as either primary coverage clause or preventive warranty clause.

According to the Supreme Court, both types of clause could be considered. Furthermore, the Supreme Court enumerated a list of probable perspectives to be taken into account when judging whether article 248 CC Bk 6, par. 2 could be invoked:

The Supreme Court mentions:

- to what extent does the provision limit the insured risk in general, e.g. in a temporal or geographical way or by a limit of cover;

- to what extent does the provision ensure that the insured takes measures to narrow the chance of damage or, if damage occurs, to limit the extent of the damage;

- to what extent does the provision take other interests into account in addition to the limitation of the damage suffered by the insured, e.g. to prevent problems of evidence or discussion about causation.

Comment

The Supreme Court is typically very reluctant to list points of view as guidance for interpretation. However, this guidance will be of help and can bring new perspectives to the ability of insurers to invoke clauses which define the extent of coverage.

The insurer has freedom of contract; it can decide what it intends to cover and what it will not cover. At the same time, the insured must be able to count on having its risk covered by its insurance.

Following the judgement, an insured party that wishes to set aside a provision relying on the restrictive standard of reasonableness and fairness can invoke the restriction, no matter the qualification of the provision. The Court no longer has to determine the qualification of the clause.

Instead, the Court must judge whether the clause is in conflict with the restrictive standard of reasonableness and fairness in the specific situation with due regard to the perspectives given by the Supreme Court.

Conclusion

The Supreme Court decision clears the way for legal development in this area of insurance law, and marks the second time in less than five years that the Supreme Court has instigated a development of law in the area of insurance.

Previously, in its causation decisions of 2021[v] , the Supreme Court suggested to seek a link with the type of insurance to determine causation in situations where no causation criterion follows from the policy. In these situations, determining which causation criterion to use continues to be arbitrary and the development of law on this subject will set a course.[vi]

In this latest decision, the Supreme Court has instigated once again a development in the law, putting forward angles which could be used as a perspective in the judgment of whether a clause constitutes a provision invoking the restrictive standard of reasonableness and fairness.

For insurers confronted with the argument that a provision invokes the restrictive standard of reasonableness and fairness, it remains an attractive prospect to refer to freedom of contract. From this point of view, insurers must express more clearly which risks they intend to cover and which risks explicitly not.

Furthermore, the insurer still has the obligation to furnish the facts and, if disputed by the insured, the burden of proof falls on the insurer to show that the damage is caused by an infringement of the provision.

By contrast, if insured parties wish to rely on coverage, they must ensure they know the intentions of the insurer and comply with the conditions. In cases where the insurer claims non-compliance with a certain provision in its clauses or conditions, the insured party must counter this with clear and justifiable reasons.

Room for discussion and opportunities!

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