# THE INSURANCE AND REINSURANCE LAW REVIEW

TENTH EDITION

**Editor**
Simon Cooper

THE LAWREVIEWS

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# PREFACE

It is hard to overstate the importance of insurance in personal and commercial life. It is the key means by which individuals and businesses are able to reduce the financial impact of a risk occurring. Reinsurance is equally significant: it protects insurers against very large claims and helps to obtain an international spread of risk. Insurance and reinsurance play an important role in the world economy. It is an increasingly global industry, with emerging markets in Asia and Latin America developing apace.

Given the expanding reach of the industry, there is a need for a source of reference that analyses recent developments in the key jurisdictions on a comparative basis. This volume, to which leading insurance and reinsurance practitioners around the world have made valuable contributions, seeks to fulfil that need. I would like to thank all the contributors for their work in compiling this volume.

One of the defining features of 2021 was the covid-19 pandemic, which has inflicted terrible human misery around the world. The insurance industry, like most other aspects of the economy, has been badly impacted by the pandemic. Although the financial loss to the industry seems likely to be manageable, it has undoubtedly raised issues about the suitability of a range of policy wordings for the modern commercial environment, while also raising various legal issues related to, for example, causation and the quantification of loss. The different jurisdictions represented in this book will have different responses to these developments so it is vital to hear from the lawyers in each of those countries on the factors that will govern the international response.

The year 2021 was another very bad year for insured losses from natural catastrophes. Hurricane Ida was the largest single loss event but other extreme weather events including deep winter freezes, severe thunderstorms, floods and heatwaves had a significant impact. These losses reinforce the continuing concern that climate change will see a long-term increase in the number and severity of such losses. From a legal perspective, the changing nature of natural catastrophes will raise issues of policy construction in relation to, for example, aggregation clauses and the obligation on reinsurers to follow their insured's underlying settlements.

The past year also saw no respite in the number or scale of cyber events, including the data breaches at the Microsoft Exchange Server and ransomware attacks on organisations as diverse as Bombardier, Acer, JSB Foods and Kia Motors. The insurer Axa also suffered a major ransomware attack which, interestingly, came shortly after the company indicated it would be amending some of its policies to exclude cover for the payment of ransoms. Events such as these test not only insurers and reinsurers, but also the rigour of the law. Insurance and reinsurance disputes provide a never-ending array of complex legal issues and new points for

the courts and arbitral tribunals to consider. Aggregation will also be an area of uncertainty in relation to the treatment of all losses of this kind, and again different jurisdictions are likely to provide different responses.

Looking ahead, 2022 is likely to see new developments and new legal issues. In particular, the impact of insurtech on the way in which insurance is underwritten, serviced and distributed will continue to present challenges around the world. This is reflected in our chapter on artificial intelligence. The current instability in international relations means there may also be an increased focus on issues such as the impact of sanctions on insurance recoveries and the scope of war exclusion clauses; for example, in relation to state involvement in cyber events.

I hope that you find this volume of use in seeking to understand today's legal challenges, and I would like to thank, once again, all the contributors.

**Simon Cooper**
Ince
London
April 2022

Chapter 19

# ISRAEL

*Harry Orad*[1]

## I INTRODUCTION

The Israeli insurance market is an expanding and evolving environment. In this area, the focus of both the legislature and the relevant regulator is on the protection of the individual consumer. Courts of law have traditionally followed suit with this public policy, although, in recent years, a slight shift can be perceived towards a more balanced construction of insurance policies.

## II REGULATION

### i The insurance regulator

The insurance market is regulated by the Commissioner of Capital Markets, Insurance and Savings, appointed by the Minister of Finance. Two bodies advise the Commissioner: a four-member Advisory Committee and the Advisory Council, which has 15 members, of whom no more than six may be government employees.

The Commissioner is competent to resolve disputes between insurers and assureds. In practice, it will refrain from assuming this role in fact-laden cases. Its decision may be appealed to the district court.

### ii Licensing

Writing insurance requires a licence. Foreign insurance companies cannot write insurance business in Israel without an Israeli licence, but Israeli citizens may buy insurance abroad. Writing reinsurance business, however, does not require a licence and foreign insurers are therefore free to do so.

The Commissioner is authorised to license a foreign company if the latter is registered in Israel and subject to regulation in the country of origin.

In a unique act, the Israeli government enacted a regulation in December 1951 exempting Lloyd's underwriters from the stipulations of the Law of Controlling Insurance Service. The practical effect of this is that Lloyd's underwriters are permitted to write business directly in Israel.

### iii Compulsory insurance

Israeli law imposes compulsory insurance requirements on professionals or individuals in several areas, including the following:

1 Harry Orad is a founding partner at Gross Orad Schlimoff & Co.

*a* The capital market: insurance requirements are imposed on investment advisers and distributors; investment portfolio managers, mutual fund managers and trustees; provident funds and their managing companies; and underwriting companies. This compulsory insurance ensures protection of clients against negligent acts and omissions and infidelity of employees.

*b* Bodily injury coverage: Israeli law imposes compulsory insurance requirements for the coverage of bodily injury in clinical trials on human subjects (insurance requirements are imposed on the clinical trial sponsor).

*c* Motor accidents: the Israeli Road Accident Victims Compensation Law provides compensation for all victims of motor accidents on a no-fault basis. Compulsory insurance by all vehicle owners provides the source of compensation. In addition, sport events organised by registered sports authorities and organisations are subject to compulsory accident insurance. Schoolchildren are covered by compulsory personal injury insurance.

*d* Banks: there is no statute that compels banks to acquire compulsory insurance; however, the Commissioner of Banks has issued a directive that requires banks to acquire employee dishonesty insurance.

*e* Aviation: current regulations impose compulsory insurance on operators of commercial aircraft to, from or in Israel, in respect of passengers, baggage and cargo; third parties; and acts of hostility, war or terror.

### iv Directors' and officers' insurance

Directors' and officers' (D&O) insurance, although not mandatory, has become a prerequisite for most high-ranking D&Os. Israeli courts have demanded accurate, full, updated reporting. The business judgement rule (BJR) has been adopted by the Supreme Court and affects D&O litigation.

In *Better Place Israel Ltd. (in liquidation) et al. v. Agassi et al.* (September 2018),[2] the district court ruled that the BJR is a preliminary defence available to D&Os, which is intended to encourage them to take difficult business decisions and business risks. It was ruled that this defence can and should be raised at very early stages, before a trial. In this case, the claim was dismissed.

The significance of this decision is that the court was willing to dismiss a claim that was filed by liquidators of a company following receipt of the approval of the liquidation court after extensive investigation into many officers of the company and other employees – and by dismissal of the claim the court made this very clear statement to the Israeli business community: Israeli courts will not intervene in informed business decisions reached by D&Os in good faith and without conflicts of interest. This applies to companies conducting their businesses in Israel in general and particularly to failed start-up companies. The claim was considered a challenge made in hindsight on a failed business logic and therefore should be dismissed *in limine*. An appeal to the Supreme Court is still pending.

In April 2021, the Attorney General filed his position in the appeal to the Supreme Court, opining that the BJR prevails also in the insolvency zone (an undefined period prior to insolvency).

2 CA 47302-05-16.

Recent years have seen an increase in the number of derivative claims and class actions in respect of breach of duties by D&Os, most of which end in settlements in which insurers play an important role.

The Israeli Companies Law prohibits the indemnification (as well as insurance and exemption) of a director or officer in respect of the following matters:

*a* breach of fiduciary duty towards the company, unless committed in good faith and with reasonable grounds to believe that the action would not prejudice the company's interests;

*b* acts committed intentionally or recklessly;

*c* acts committed with the intention of gaining unlawful personal benefit; and

*d* fines and penalties, including civil fines and monetary levies.

The new Insolvency and Economic Rehabilitation Law (2018) (the Insolvency Law) defines extensive duties of the CEO and the directors in companies facing insolvency and holds them liable for breach of these duties. The Insolvency Law also prohibits exemption and indemnification of directors for breach of these duties.

There is currently a difference of opinion between the Attorney General and academics of high repute on the issue to whom the D&Os owe a duty of care during the undefined period of the insolvency zone – whether to the company's shareholders or to its creditors.

The Supreme Court decision on the *Better Place* appeal will hopefully provide definitive guidelines on this matter (see Section VI.iv).

## III INSURANCE AND REINSURANCE LAW

### i Sources of law

The Israeli legal system is fundamentally a common law regime, without jury. However, throughout the years, civil law statutes have been enacted. The Insurance Contract Law 1981 (ICL) adopted principles of consumer protection. The Control of Financial Services (Insurance) Law provides regulatory provisions for the market. The ICL applies to all types of insurance other than reinsurance, marine, aviation and insurance of diamonds or valuable metals.

### ii Making the contract

The ICL does not specify a unique format for execution of the insurance contract. However, it does specify rules aimed at reinforcing consumer rights and imposing limitations on insurers, remedies and power. These rules aim to moderate the typical imbalance of power between the insurer and the insured.

### iii Duty of disclosure

The ICL imposes an explicit duty on the insured to answer the insurer's questions in full and truthfully, when presented in writing in respect of a material matter. A material matter is defined by the Law as one that could affect a reasonable insurer's willingness to assume the risk in general or to assume it under the terms specified by the policy.

The Law further stipulates that fraudulent concealment of a matter that the insured was aware of as being a material matter is regarded as an untruthful and incomplete answer. Israeli courts have interpreted this in conjunction with the questions posed by the insurer

on the proposal form: a subject not mentioned in a proposal form has been deemed to be immaterial and therefore there can be no positive duty of disclosure regarding such a subject and no sanction for non-disclosure.

### iv Interpreting the contract

An insurance contract is interpreted according to the (revised) Article 25 of the Law of Contracts and case law, which clarified rules of interpretation of insurance policies, such as *Cohen v. Migdal Insurance Company*[3] and *MS Aluminium Products v. Arie Insurance Company*.[4]

The stages of interpreting a policy are as follows:

*a* The first stage is based on the subjective intention of the parties to the specific policy. If possible, the parties' intentions will be ascertained literally from the language of the insurance contract. Otherwise, for the subjective intention, the court will look at external circumstances, such as communications exchanged between the parties.

*b* Second, if the subjective intention of the parties cannot be ascertained, then the court will seek the objective intention of the parties, namely the intention of reasonable and honest parties with respect to the policy in question. The objective intention can be ascertained, for example, from common practice among other insurers in the relevant type of insurance.

*c* A policy construction that gives it force and effect is preferable over one that voids the policy provisions.

*d* Only if the court cannot ascertain the subjective or objective intention of the parties will the court interpret ambiguities in the policy against the drafter (usually the insurance company).

*e* Courts also refer to the doctrine of the reasonable expectations of the insured, but only if there are several reasonable interpretations and one of them meets the reasonable expectations of the insured. This is generally used together with other rules of interpretation.

### v Warranties and conditions precedent

The ICL provides no basis for the doctrines of warranties and conditions precedent as implemented in common law countries. The Israeli law has adopted a proportionate remedy principle regarding breach of both contract terms and the duty of disclosure. The significance of this principle is that other than in cases of fraud, there is no automatic exemption of the insurer from liability.

Where the insurer alleges breach, the court will consider its extent and effect and is authorised to reduce liability proportionately according to the ratio of the actual premium and the higher premium that would have been charged had the insured disclosed the material matter or had the insurer known that the policy condition would not have been adhered to (see Section V).

The insurer bears the burden of proof that full disclosure or non-adherence to the condition would have had an effect on underwriting.

Furthermore, the ICL negates remedies where the breach of the duty of disclosure or the policy condition did not affect the risk.

3 CA 4688/02.

4 CA 453/11.

### vi Intermediaries and the role of the broker

The licensing of insurance brokers is regulated by law, requiring a licence, which follows on from practical training and examinations. The licensing is in three areas of expertise: general insurance, marine and pension insurance brokerage.

The licence may be granted to an individual or to a corporation.

The activities of insurance agents are regulated by law. An insurance agent is defined as 'one who engages in insurance brokering between the insured and insurers, and as a liaison between the insurer and the insured'. It is considered an agent of the insurer with regard to the negotiations leading up to the formulating of the insurance contract, unless appointed in writing by the insured as an agent of the insured. As the agent of the insurer, any fact brought to its knowledge regarding a material matter will be considered as known by the insurer for the purpose of the insured's duty of disclosure.

Payment of premium to the agent is also considered as payment to the insurer.

The agent is considered the insurer's agent for the purpose of receiving notice of the identity of the insured and the beneficiary unless the insurer informed the insured and the beneficiary in writing that notification must be sent to a different recipient.

The presumption that the insurance agent is the agent of the insurer serves as an obstacle that insurers must surmount to be allowed to rely on policy terms.

In *Clal Insurance Company Ltd v. Mussa Ally* (October 2004),[5] the court ruled that the insured was not deemed to have received a copy of the policy terms as the document had been sent to the agent and not to the policyholder. The fact that the agent in that case was a close relative of the policyholder did not suffice to overcome this obstacle. Furthermore, the insured had signed the section in the proposal form appointing the agent as his own agent. However, the court ruled that in the absence of clear-cut evidence that the insured fully understood the meaning of this waiver, the legal presumption prevailed, and the agent remained the agent of the insurer. As a result, the court did not allow the insurer to rely on stipulations in the policy making cover conditional upon the insured taking measures to alleviate the risk. The court ruled that as the policy had not reached the hands of the policyholder, the insurer had not fulfilled the duty to ensure that the policyholder was fully aware of these conditions and the consequences of non-compliance.

### vii Claims

#### *Notification*

The ICL provides that the insured must notify the insurer of the insured event immediately after becoming aware of its occurrence. However, as with the approach to breach of policy terms or the duty of disclosure, the ICL does not sanction late notification with automatic dismissal of the claim. The burden of proof in this respect is on the insurer, who must prove substantive damage as a result of the failure to notify on time. To meet this burden, it is not sufficient to show a theoretical possibility that damage may be sustained by the insurer.

In any case, the claim will not be dismissed but reduced proportionately with regard to the extent of the damage caused by the delay. Furthermore, as with most provisions of the ICL, the above are reinforced as the ICL mandates that these provisions cannot be modified by agreement unless the modification is in favour of the insured. The practical effect of these provisions is that, as a rule, insurers cannot rely on a 'late notification' argument unless

5 CA 2626/01.

their rights were significantly prejudiced as a result of the late notification. These provisions have been the subject of discussion in numerous Israeli court cases wherein the courts have consistently ruled that an insurer that wishes to benefit from the remedy provisions must show that its rights were actually prejudiced by the insured's non-compliance with the duty to notify.

The burden of proof borne by the insurer is not a light one. It must prove actual damage as a result of breach of the notification duty. Statements to this effect were made in several cases, including *Hassneh Insurance Co v. Asulin*,[6] where the burden imposed on the insurers to prove actual damage was emphasised.

In *Wile v. Phoenix Insurance Co*,[7] the court again ruled that it is not sufficient for the insurer to merely prove the breach of the notification duty, rather, actual damage as a result of the breach must be shown to have occurred.

*International Bank v. Prudential Insurance Co* was an extreme case.[8] The bank advised insurers of the court claim against it only after it had already lost the case in court. Prudential refused to indemnify the bank, dismissing the claim based on the argument of late notification. The bank filed suit and the court ruled in favour of the bank, holding that Prudential had not proved any damage as a result of the late notification. The court stated that the bank had defended the claim against it in a comprehensive and highly professional manner. Furthermore, the court ruled that the insurers had breached their duty to act in good faith by raising these 'technical arguments'.

### *Good faith and claims*

Section 27 of the ICL provides that the insurance benefits will be paid within 30 days of the day on which the insurer is in possession of the information and documents required for the ascertainment of his or her liability. However, insurance benefits not disputed on bona fide grounds will be paid within 30 days of the day on which a claim is submitted to the insurer and they may be claimed separately from the remainder of the benefits.

### *Insurer's duty to issue a coverage position letter*

Coverage position letters have been the basis of limitations on insurers' practical rights and scope of defence in Israeli courts, where the coverage position letter did not meet the regulator's requirements. These requirements have been adopted by the courts as legally binding in the framework of the insured–insurer relationship. The Supreme Court added that insurers' obligations also apply to a third party that is entitled to direct privity with the insurer.

The first directive on the subject, issued in 1998, required the insurer to specify all grounds for denial of coverage, sanctioning failure to do so by precluding the insurer from raising any new argument in future litigation. The Commissioner cited the insured's right to receive all details to be able to seek advice regarding possible legal relief on the basis of the insurer's position as the rationale for this sanction.

6 CA 215/91.

7 CA 1438/02.

8 CF 7/88.

Later, a variation on the original directive was issued, clarifying that arguments based on events subsequent to the coverage position letter, or based on grounds that could not have reasonably been known to the insurer when issuing the coverage position letter, would be allowed to be introduced at a later stage.

The courts afforded the directives the power to limit the scope of insurers' rights to evoke defence arguments beyond those cited in the coverage position letter:

*a* the insurer is obliged to effectively investigate the circumstances of the loss or claim to form its coverage position as soon as possible after receipt of the claim;

*b* the coverage position must be provided to the insured in writing, within 30 days of receipt of information and documents required from insured;

*c* where coverage is declined (whether wholly or partially), all grounds for this position must be detailed therein;

*d* the insurer is precluded from raising any argument on circumstances, conditions or exclusions that were not mentioned in the coverage position letter; and

*e* the insurer will be able to broaden its defence only in rare cases where the circumstances material to its updated coverage position were not known and could not reasonably have been known. Such cases would certainly include intentional behaviour aimed at concealing material facts from the insurer.

### viii Reinstatement

Reinstatement clauses are common in property insurance and provide coverage beyond the scope of the ICL. Reinstatement (i.e., 'new for old') is an additional cover and is subject to a time limit, which may cause friction with the insurer.

The condition that reinstatement costs are due (beyond compensation for the actual damage) only after the insured covers his or her expenses independently and only after the reinstatement is complete is a basic condition for the implementation of reinstatement insurance.

The time limit will not apply where the insurer is found to have unlawfully denied insurance benefits and so prevented the insured from reinstating the damaged property. In *Hadar Insurance Co Ltd v. Ehad Ha'am Food and Investments Ltd*[9] the insurer claimed that the insured failed to reinstate the equipment in the allotted time and therefore was not entitled to reinstatement values. The Supreme Court rejected the insurer's argument, ruling that by detaining the insurance benefits for the actual damage, the insurer prevented the insured from reinstating the equipment and therefore could not invoke the time limit condition against the insured.

### ix Dispute resolution clauses

The insertion of dispute resolution clauses is not widely accepted in standard policies, as this is considered an infringement of the insured's rights to take up matters with the courts.

### x Punitive interest

The amended Section 28 of the ICL stipulates that in personal insurance (life, auto, home, health – but not liability) the court is obliged to award, and in non-personal insurance the court may award, an additional interest award of up to 20 times the basic interest rate, when

9 CA 7298/10.

an insurer did not indemnify the insured the amounts not in dispute in good faith on the appropriate date (in long-term care insurance – up to 10 times). If the court decides not to apply this special rate, it should explain the reasons for its decision.

In *Dudi v. Phoenix Insurance Company Ltd* (August 2019)[10] – a claim for life insurance benefits – the court decided that according to the amended Section 28a of the ICL, the insurer acted in bad faith in delaying payment and ordered payment of 20 times the basic insurance rate on the undisputed benefits for the period of the delay. An appeal to the district court is pending.

Section 27 provides that the insurance benefits will be paid 30 days after the insurer received all information and documents required to ascertain the insurer's liability under the insurance contract. For insurance benefits that are not in dispute, the payment should be made within 30 days of the date the insurance claim was notified to the insurer. If this Section is breached, the insurance benefits will accumulate the above-mentioned interest. According to a Supreme Court precedent, the 30-day period will be calculated from the date the insured notified the insurers regarding the insured event.

***Insurance Arbitration Institute***

A new bill proposed by the Ministry of Finance in 2018 stipulated the establishment of an Insurance Arbitration Institute and compulsory arbitration of insurance claims in this Institute (except for claims by big companies (according to turnover and number of employees) and claims against third parties). In 2021, an attempt was made to revive a more limited version of this bill. If, and to what extent, it will be approved is yet to be determined.

## IV DISPUTE RESOLUTION

### i Jurisdiction, choice of law and arbitration clauses

As a rule, insurance contracts, other than those concerning reinsurance, marine, aviation, diamonds and precious metals are subject to Israeli law. Jurisdiction is local and the competent court is determined by the amount claimed – up to 2.5 million shekels with the lower court and above this amount with the district court, as first instances.

### ii Right of appeal

There is an automatic right of appeal against judgments of the court of first instance to the appeal court within 45 days. As a rule, the appeal court will not intervene on points of fact unless a severe and obvious error is clearly evident.

Leave to appeal is required to allow access to a second appellate instance and to appeal interim decisions.

Most district courts will now complete hearing of an appeal within three years. At the Supreme Court, however, a case may take much longer.

### iii Arbitration

Arbitration is very similar to a court process – evidence is brought, and discovery and testimony can be compelled by the arbitrator by using the court's mechanism. Rules of evidence do not apply where parties have not agreed otherwise.

10 CF 55587-11-18.

As stipulated by the Commissioner, an insurance policy may not include a clause binding the insured to arbitration in the event of a future dispute. This clause is considered to be prejudicial to insured's rights. This stipulation does not apply when the insured specifically agreed to the arbitration clause.

### iv Alternative dispute resolution

Mediation is the most common form of alternative dispute resolution and a recent amendment to the Civil Procedure Rules mandates referral of all litigants in all claims for over 75,000 shekels (excluding damages for victims of motor vehicle accidents) to hold a meeting with a mediator to discuss holding mediation talks. This is a general rule and not specific to insurance cases. This is a precondition for continuing to trial, but the court is not authorised to penalise parties for not agreeing to mediation or for not making an offer to settle.

A positive incentive for early settlement is afforded by rules regarding payment and refund of court charges. Court charges are levied on monetary claims at the rate of 2.5 per cent of the claim. Half of the court charges is paid on filing the claim and the second half is paid only if the case goes to trial. Furthermore, the first half of the court charges will be refunded automatically to parties that settle before three pretrial hearings have been held and the court is authorised to refund the entire charges paid if a resolution is reached, at any stage, by mediation or arbitration.

## V SUBROGATION

### i Stricter rules

Subrogation in Israel stems from Section 62 of the ICL, which transfers to the insurer any rights that the insured may have for remedy in relation to the insured loss upon payment of the insurance benefits. It is seemingly a simple matter of transferring rights from the insured to the insurer regarding the insured damage, against third parties. However, as shown in a ruling by the Supreme Court in *Lloyd's Underwriters and IEC v. Ashdod Port* (December 2014),[11] the subrogating insurers may have to make additional efforts to prove the elements of the claim to ensure the full transfer of rights and benefits.

Under Israeli law, subrogation is contingent on the insurer establishing all the following conditions:

*a* the obligation to pay insurance benefits on the basis of a valid policy;
*b* actual payment of insurance benefits on the basis of this obligation; and
*c* proof of the insured's right for compensation from a third party in relation to the insured event or damage.

The above-mentioned Supreme Court judgment emphasises the fact that to preserve and ensure the prospects of subrogation, the insurer must invest efforts, beyond those necessary to determine coverage, to investigate and preserve evidence necessary for the future subrogation claim by determining the exact nature of the damage and cannot rely on the advice of an interested party, such as the manufacturer or supplier of the damaged product.

11 CA 12/7287.

In *Clall Insurance Company Ltd v. Vaxman Engineering* (July 2020),[12] the district court stated that a subrogation right is not an absolute right. In a case regarding contractors' all-risk insurance, the court dismissed a subrogation claim against a subcontractor who was included as an additional insured in the policy. The court stated that when an insurer agrees to include additional insureds in the policy, such as a subcontractor, it waives its right of subrogation against the additional insureds, even if they are responsible for damage to the main insured. A hearing of the appeal to the Supreme Court is scheduled for September 2022.

### ii Subrogation by a foreign insurer

On 13 December 2021, in a very important precedent, the Supreme Court finally determined that a foreign insurer, not admitted and not licensed in Israel, has a subrogation right. This new precedent has changed the legal situation in Israel with respect to this material issue.

The right of a foreign insurer to file a subrogation claim had been questioned several times by Israeli courts. The subrogation right of an insurer is determined by Section 62 of the ICL. The reasoning raised in several rulings opposing subrogation actions by foreign insurers has been that the ICL applies to 'an insurer' as defined in the Control of Financial Services (Insurance) Law, 1981, which refers only to an Israeli insurer licensed to write insurance business in Israel or a foreign insurer with a licence to operate in Israel.

The leading decision on this issue, until recently, was in the matter of *VIG Vienna Insurance Group v. the Drainage & Streams Authority Sharon (VIG)*[13] in which the district court ruled that a foreign insurer not licensed in Israel is precluded from filing a subrogation claim pursuant to Section 62 of the ICL.

On 13 December 2021, in *Teva Pharmaceuticals Ltd v. Ayalon Insurance Company Ltd*, the Supreme Court[14] handed down a comprehensive precedent and determined, contrary to the VIG ruling, that a foreign insurer has a right to file a subrogation claim in Israel even if not admitted or licensed to write insurance business in Israel. The court emphasised that an insurer's right of subrogation is based on the important principle of unjust enrichment (i.e., that the tortfeasor should not benefit from the fact that the injured party purchased insurance). Furthermore, the court also stressed that the right of subrogation is an important factor in the pricing of insurance. Thus, it is an important consideration of the insurance industry. In addition, it is important to give insurers an incentive to pay insurance benefits by acknowledging their potential recovery from the tortfeasor. The legal and regulatory requirement under the Control of Financial Services (Insurance) Law, which applies to insurers that transact insurance business in Israel, was not aimed to protect the tortfeasors and enable them to avoid their liability merely because the insurer is foreign.

The Supreme Court determined that if the insurance contract is governed by Israeli law, the foreign insurer is entitled to file a subrogation claim pursuant to Section 62 of the ICL. If the insurance contract is not governed by Israeli law, the foreign insurer is entitled to file a subrogation claim by virtue of the principles of unjust enrichment.

12 CC 18638-11-18.

13 CC 53025-11-14.

14 CA 206/20.

## VI YEAR IN REVIEW

### i Amendments to the Insurance Contract Law

Recent amendments to the ICL include extending the limitation period of life, health and nursing insurance claims from 3 to 5 years. In addition, the new Section 31a mandates that in response to an insurance notification, the insurer must include in his or her answer to the insured details of the limitation period, specifying that the limitation period is not suspended following such notification. The information regarding the limitation period should be clear and noticeable and should be repeated periodically by the insurer.

The Ministry of Justice published a bill for additional proposed amendments to the ICL. It includes proposed widening of the Commissioner's authority to impose punitive interest if they find that an insurer did not indemnify the insured the amounts that are not in good faith in dispute, within the relevant time frame. The bill also proposes to extend the limitation period if a complaint was made to the Commissioner. If and when the bill will be approved remains to be seen.

### ii Effects of covid-19

***Covid-19 exclusions – directive of the Commissioner of Insurance***

On 8 December 2020, the Commissioner of Insurance issued a directive to insurance companies regarding exclusions in reinsurance regarding covid-19 in elementary insurances.

The directives of the regulator are as follows:

*a* It is not permissible to exclude by way of a pandemic exclusion losses that had already materialised, or to implement a 'continuity rule' so that an exclusion will be retroactively applied to policies that were already purchased, including extensions of periods of existing policies, even in cases where the policy period had not been concluded. In claims made against policies sold starting from 2021 onwards, it is permissible to apply an exclusion regarding insured events that occurred prior to 2021.

*b* A pandemic exclusion will be limited to losses from a pandemic declared by the World Health Organization or any authorised governmental entity. In property insurance, it is also permitted to exclude contagious disease viruses, bacteria or other microorganisms, etc.

*c* It is permissible to exclude damage that is covered by the state of Israel.

*d* An insurance company requesting to exclude pandemic cover will present a designated disclosure to the insureds regarding the exclusion, in a specific and highlighted manner, in any policy sold until 31 December 2022.

*e* An insurance company seeking to include a pandemic exclusion in a specific policy shall submit to the Commissioner details regarding the relevance of the exclusion to the coverage afforded under the policy and an assessment of the economic implications that the company attributes to the exclusion, based on, inter alia, the information available regarding the pandemic at that time. In addition, the company will detail the extent of loss that the company is intending to retain and in which instances.

*f* The declaration page (schedule) will include for the insureds a clarification that the onus to prove that the circumstances specified in the exclusion had materialised (namely that the damage results from a pandemic) attaches to the insurance company that intends to repudiate coverage on this basis.

***Cover under property insurance – business interruption losses***

Generally speaking, most property policies in the Israeli market require physical damage to the insured property and only then is the insured entitled to business interruption cover. The view in the market is that such policies are not triggered by covid-19.

There are a few policies in the market (mainly issued to hotels) that include specific endorsements, under which booking cancellations as a result of the pandemic may be covered, even in the absence of physical damage. In principle, and depending on the language of the policies, insurers have paid benefits under such specific endorsements.

In November 2021, the Tel Aviv Hilton Hotel filed a claim against Harel Insurance Company for loss of profit as a result of covid-19-related cancellations, alleging that Harel agreed to pay only half of the insured amount.

***Liability claims as a result of covid-19***

Until now, only very few liability claims have been filed, mainly against employers who breached instructions or against management of nursing homes for deaths of members as a result of covid-19.

One class action was filed against D&Os of a company alleging misleading information in the company's financial reports regarding the implications of covid-19.

On 4 August 2021, the Haifa District Court dismissed a class action motion *Kama Mia Textile Ltd v. Migdal Insurance Company Ltd*,[15] claiming that insurance companies should reduce the premium charged in employment policies and third-party liability policies as a result of government restrictions imposed following the pandemic. The court said that applicants failed to prove that a reduced level of activity in the business reduces the insured risk. The court added that had applicants estimated the insured risk is reduced, they should have advised the insurer accordingly in advance, and not in hindsight.

### iii Cyber technology

The Regulations for the Protection of Privacy (Information Security) became effective in May 2018. The Regulations established, for the first time in Israel, a specific arrangement regarding protection of databases, including establishing organisational procedures and risk management enhancement steps. They also include a duty to report any severe data breach to the Database Registrar at the Privacy Protection Authority, which may instruct that notification be given to persons who may be affected. This constituted a substantial development in the data breach regulatory regime in Israel and highlighted the importance of purchasing cyber insurance.

In November 2021, the Israeli parliament approved in first reading the bill for amending the Privacy Protection Law (Protection of Privacy Bill) (Amendment 14), 2021, which constitutes another step in adapting the Privacy Protection Law to technological developments. The bill is pending for final approval.

A new bill titled Cyber Protection and the National Cyber Directorate (Authorities to Strengthen Cyber Defense) (Temporary Provision) was published in 2021. The bill has been brought for approval as a temporary provision for a period of two years, while legislative

15 ClA 25472-04-20.

efforts will be made to complete a comprehensive 'Cyber Law'. The bill deals with the authorities of the National Cyber Directorate to be involved in cyber events, while protecting 'vital public interests'.

The EU General Data Protection Regulation, which became effective in May 2018, applies to Israeli companies that either target the European Union (by offering goods or services to individuals from EU Member States) or monitor the behaviour of individuals from EU Member States (e.g., by tracking them online).

Several class actions have been filed against companies in Israel for breach of privacy protection following cyberattacks. Case law is still not developed in this respect.

According to a survey of the Israel National Cyber Directorate regarding cyber insurance in 2019, only 13 per cent of Israeli companies purchased cyber insurance. However, penetration of cyber insurance was growing as a result of increased awareness and the impact of the new regulations, as well as published reports on significant events in 2020 and 2021, which increased the appetite of Israeli companies to purchase cyber insurance. However, similarly to the global trend in cyber insurance, we expect that the terms for cyber insurance will be hardened during 2022, including co-insurance, increased deductibles and premium etc.

### iv D&O insurance

The new Insolvency and Rehabilitation Law imposes liability on the CEO and the directors of companies in any case where these individuals knew or could have known that the company was insolvent and did not take reasonable measures to mitigate the scope of the insolvency. In such cases, the directors and the CEO could be held liable towards the corporation for the losses sustained by the creditors, as a result of their failure to prevent or mitigate the losses. Certain provisions of the law provide a safe harbour defence for directors and CEOs; however, the law prohibits the corporation from granting them exemption or indemnification.

Insurers that write D&O policies in Israel may wish to address the extended duties of directors and CEOs under the law.

There are also new duties attached to D&Os of companies regarding cyber risk management and reporting that could be included in the company and D&O insurance.

The new amendment to the Economical Competition Law (formerly known as the Anti-Trust Law (ECL)), imposes a positive duty on an officer of a company to observe the law and to do his or her utmost to prevent violations of the law. If an offence is committed by the company (or one of its employees) the officer will be deemed to have breached this duty unless it can be proved that the officer took all possible measures to fulfil his or her duty.

In recent years, D&O insurers have been facing a challenging legal environment as a result of the broadening of the scope of D&Os' duties by Israeli courts. This trend manifested especially in respect of directors' supervisory duties over the implementation of company policy. In the absence of any substantial court decisions, the accepted legal position is that the ordinary concept of duty of care also attaches to supervisory duties. Without clear guidelines on this crucial issue, insurers have preferred to settle derivative actions against directors based on cases of breach of supervisory duties to contain significant costs and the risk of adverse judgments and very high compensatory awards. The author's firm, Gross Orad Schlimoff, has in the past met and communicated with different relevant regulators (the Commissioner for Insurance, Savings and Capital Markets, the Ministry of Justice) to express insurers' concerns in these matters. In January 2021, a major breakthrough occurred when the State Attorney exercised his prerogative to intervene in derivative actions and requested the courts to consider

forming clear guidelines on the required standing and nature of directors' supervisory duties. The State Attorney suggested that the standard of fault on the part of directors required for imposition of liability be somewhere between the standard formed by the US Delaware Court of Chancery and 'merely' negligence.

### v Breach of policy conditions – the new *Piccali* precedent

The case, which was heard by four separate instances of the Israeli courts, including twice by the Supreme Court, concerns an insurance claim for damage as a result of a car crash. The insured car was driven at the time of the accident by a 23-year-old employee (the insured). The motor vehicle policy included an age limitation pursuant to which cover applied only to drivers aged 30 years or above. Accordingly, the insurer declined cover on the grounds of the driver's age.

Both the Magistrate Court and the District Court held that because the insured intentionally did not purchase a policy to cover younger drivers, insurers' declinature of cover is justified.

However, on second appeal to the Supreme Court, this ruling was overturned. The Supreme Court based its precedential ruling on the insurance contract principle of proportionate cover as opposed to an 'all or nothing' approach. The ICL mandates in Sections 17 and 18 that where there has been material aggravation of the risk, cover will apply based on a pro-rata proportionate rule – by calculating the premium terms that would have applied had the aggravated risk been known to the insurer, in relation to the terms that applied, reducing benefits accordingly. The Supreme Court viewed the young age of the driver through the prism of the proportionate cover for aggravated risk. The Supreme Court ruled that cover applied at a reduced rate, in accordance with the proportion between the premium that was in fact charged, divided by the premium that would have applied had the insured purchased cover for younger drivers.

In view of the importance of the issue subject of the *Piccalli* appeal, the Supreme Court granted an additional hearing with an expanded panel of judges. The additional hearing overturned the previous precedent.

In this final and binding decision, the Supreme Court ruled that in this case the insurance policy cannot apply to the damage caused while the car was driven by the young driver in breach of the policy age limitation. This is not a situation of aggravation of the risk which the insurer can be seen in retrospect to have agreed to cover, but rather a simple case of breach of the policy terms as a result of reasons that are under the insured's control.

A distinction should be made between events and terms that are under the insured's control and external events that are beyond the insured's control.

The provisions of the ICL, which applies a proportionate remedy in case of risk aggravation, are only relevant to external events that are beyond the control of the insured. It would not apply where the policy was breached knowingly by the insured – in this case, by allowing a young person to drive the car.

There was no dispute in the *Piccalli* case that the insured intentionally did not purchase cover for a young driver, to save the additional incremented premium. The Supreme Court ruled that this intentional decision cannot be rectified retroactively.

To conclude, where the insured has breached the policy terms as a result of an intentional decision or conduct, the policy does not apply, and the insurer is fully exempted from any liability under the policy.

Although this case concerns a motor vehicle policy, it has far-reaching implications to other classes of insurance. The Supreme Court places a clear dam to stop the growing trend in recent years towards expanding policy coverage under the 'proportionate cover application', which started with the *Slutzki* ruling (2013). The new decision takes a clear stand on full exemption from liability based on whether there has been aggravation of risk as a result of an external event that was beyond the insured's control, or as a result of a conscious decision of the insured to take a risk for which he or she deliberately refrained from purchasing cover, in a controlled decision to breach the policy terms. We expect that this new ruling will reduce the uncertainty that prevailed in recent years.

## VII OUTLOOK AND CONCLUSIONS

There is no doubt that 2021 was a challenging year for the insurance market in Israel, mainly as a result of the covid-19 pandemic. However, contrary to expectations, insurance companies in Israel ended the year with significant profits over and above all expectations.

Many transactions occurred during 2021 in the insurance market in Israel, including: the entrance of the global broker Willis Towers Watson to Israel by acquiring a local broker (Leaderim), purchase by a technology company (Wesure) of the controlling shares of a traditional insurance company (Ayalon), mergers and acquisitions of brokers, the establishment of a reinsurance company by Howden and more. These transactions indicate that the Israeli insurance market is very dynamic and is perceived with potential, mainly because of the technological and digital capabilities.

To encourage the development and use of technology by the local market, the regulator published new conditions that allow investments in insurtech companies as preferred investments.

Israel as a start-up nation is aiming to be a leader in innovation and in creating a synergy between the many insurtech companies and the traditional insurance market.

**Appendix 1**

# ABOUT THE AUTHORS


**HARRY ORAD**

*Gross Orad Schlimoff & Co*


Harry Orad is a founding partner at Gross, Orad, Schlimoff & Co (GOS). He began his legal career as a commercial lawyer specialising in corporate and property law. He also served as a municipal court justice. Harry later joined the highly acclaimed National Fraud Unit of the Israeli Police, rising to the rank of chief superintendent, where he investigated complex financial institution fraud and white-collar crimes. After leaving the police, Harry has specialised in insurance and reinsurance law. He drafted some of the first D&O policies in Israel and later redrafted these policies to comply with new legal provisions. He has lectured on corporate governance issues in Israel and abroad, and worked in London as a consultant to one of the major insurance law firms. Harry's expertise in insurance law includes D&O liability, banking insurance (bankers' blanket bonds), financial institutions, crime insurance, credit insurance, product liability and pollution and contamination.

Harry acts for underwriters and insurers worldwide on complex financial insurance matters and has been inducted into the *The Legal 500* Hall of Fame.


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