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Buying a Risk: An Application of Insurance Law to Legal Gaming

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At law, the imposition of novel duties of care may be arrived at by way of analogy with extant obligations. Here, such an analogy is made between the provision of gambling opportunities and the legal duties that subsist in any contract of insurance. A legal methodology is employed to explicate the core principles that give rise to fiduciary duties resulting from contracts of insurance, and to apply judicial decisions in the area of insurance law to the gambling construct.

Keywords: Gambling; Insurance; Duty of care; Misrepresentation; Vulnerability; Risk.

Introduction

At first blush, it may not appear that gambling and insurance have much in common. To this age, the conservative stolidity of Lloyds of London seems to be a far cry from the glitter of gambling. In comparison, when opportunities to gamble were far more limited, the English Life Insurance Act of 1774 specifically made insurances on the lives of those who one had no interest in, null and void, as gaming and wagering. The distinction between insurance and gaming was one that forced the Court to strive for adequate formulations to differentiate legitimate from illegitimate enterprises:

> "if it is correctly called an insurance on life, then it is not without an interest within the meaning of the same statute; for, although Field had no vested interest in the property of Mrs. Smith which he could sell, still a promise to assign a devise which he expected would be a sufficient consideration to support a promise to pay for it, in a contract not under seal; and the purchaser of such an expected devise would have an interest so far as to prevent his policy being considered the gaming and wagering prohibited by the statute." *Cook v. Field* (1850) 15 QB 460 Lord Campbell CJ.

Other attempts were made to cast gambling as outside the law of contract on the basis of its contingent nature, and because of the uncertainty inherent in the transaction. In *Thacker v. Hardy* (1878) 4 QBD 685 CA Cotton J characterized the transaction as a contract void for uncertainty, stating that "The essence of gaming and wagering is that one party is to win and the other to lose upon a future event, which at the time of the contract is of an uncertain nature." The difficulty with this formulation is that the stock exchange transactions at issue in that case are very close to many forms of socially-acceptable speculation that also involve profit or loss dependant upon future events. Besides insurance on an interest, legitimate speculation has included such instances as an indemnity policy for a proposed trans-Atlantic cable in *Wilson v. Jones* (1867) LR 2 Exch 139, and providing a guaranteed cure for the flu in *Carlill v. Carbolic Smoke Ball Co.* (1892) 2 QB 484 (CA).

Ultimately the only coherent divide was that set out by McCardie J in *Barnett v. Sanker* (1925) 41 TLP 660:662, in which it was stated that:

> "If the parties meant that no legal bargain should be effected between them, and that there should be no right to demand a payment of differences except a moral right, the contract is a gaming contract. But if the parties intended to enter into a legal contract, which gave legal rights and imposed legal obligation, then the contract though it deals with speculative transactions was enforceable."

Clearly, this is a culture-specific divide rather than a principled distinction. It separates speculation from gambling on the basis of the social constructs that in-

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form the transaction. This is not a criticism, as there is no other defining feature for the law to fix on. Given the subtly of such distinctions, what was fundamentally at issue was the nature of the transaction; that nature was categorized in terms of the value system of the ruling morality. While outside of the prevailing morality, gaming and wagering constituted illegal contracts that would not be enforced. Gambling was not contractual for the same reasons that arrangements between husband and wife are not contracts. Despite all the elements of contract being present in agreements between husband and wife, such agreements are simply not arrangements that our culture understands as entailing legal consequences, as held in the leading matrimonial case of *Balfour v. Balfour* (1919) 2 KB 571 (CA). Broadly, where a transaction, which involves mutual exchange, is perceived to be within the law, rights and obligations follow. Transactions that a culture considers to be outside the province of the law do not give rise to a legitimate expectation of remedies at law.

This was the divide between legitimate insurance and insurance as gaming and wagering, despite the essential components of risk and vulnerability being fundamentally the same in gambling and insurance, as the actuary is nothing other than a bookmaker without the plaid, and the underwriter a bigger bag. While genuine insurance policies and other forms of futures speculation were seen as legitimate business activities by society, and gambling was not, the divide provided legal remedies to one and withheld the operation of the law from the other. With the sanctification of gambling by the state, all such speculation must conform with consumer safeguards and legal principle. Arguably then, the principles of equity and the common law duties of utmost good faith, which apply in the context of insurance law, are directly applicable to the gambling construct.

Defining Features of Insurance Law

Two related features give shape to the distinctions that separate contract law at large from insurance law. These are vulnerability to risk, contingent upon an imbalance of information. Clearly, these are not absent from other areas of contract, but are central to insurance law, as one party is dependant on the other at different stages of the transaction, and so a trust reposes between them.

The other distinguishing feature, as most other contractual obligations are reciprocal, is the trilateral relation between the insurer, the insured and the injured party. This is the feature that requires fairness to impose upon the insurer an obligation to treat the interests of the insured equally to its own. Otherwise, the insurer's subrogatory control of litigation could open the insured to personal liability beyond the policy. It is the ability of the insurer to maximize its position as a result of the relationship itself that is tempered by the imposition of the duty on the insurer to give equal priority to the interests of the insured. At bottom, it is the meeting of the minds and contractual intention on which this duty is founded. The intention of the insurer is to gain protection from liability, and it is the representation that the insurer will assume liability that induces the insured to pay the premiums. This understanding would be defeated if the insurer unfairly resisted claims within the policy limit and, in doing so, opened the insured to liability for damages in excess of the insured peril. The law, taking the representation of the fact, then imposes the burden of that representation on the insurer by way of a duty to act in accordance with the representation.

Outside of public policy considerations there is no trilateral relationship in the gaming construct. However, what is achieved by the imposition of this duty on insurers is the holding of the insurer to their representation and the effecting of the contract in the manner it was portrayed. It will be argued that similar considerations impel similar duties being placed on the gaming consortiums, which misrepresent the risk entailed.

Risk and Vulnerability

Historically, it was the vulnerability of insurers to underwriting an unknown risk that developed the duty incumbent on the insured to inform the insurer of all information in their possession that was material to the insured peril. It was this vulnerability and the prerequisite of trust that placed insurance in the *uberrimae fidei* class of contracts.

In the leading case of *Carter v. Boehm* (1766) 3 Burr. 97 ER 1162, Lord Mansfield held that:

> "Insurance is a contract of speculation. The special facts upon which the contingent chance is to be computed lie most commonly in the knowledge of the assured only; the underwriter trusts to his representation, and proceeds upon confidence that he does not keep back any circumstances in his knowledge to mislead the underwriter into a belief that the circumstance does not exist. The keeping back such circumstance is a fraud, and therefore the policy is void. Although the suppression should happen through mistake, without any fraudulent intention, yet still the underwriter is deceived and the policy void, because the *risque* run is really different from the *risque* understood and intended to be run at the time of the agreement ... The policy would be equally void against the underwriter if he concealed ... Good faith forbids either party, by concealing what he privately knows, to draw the other into a bargain from his ignorance of the fact, and his believing the contrary."

It appears, on Lord Mansfield's analysis, that the principled basis of the action is largely in equity, and it is a form of estoppel by which it is a breach of trust to profit from another's misrepresentation. The basis of the agreement is that one "trusts to his representation, and proceeds upon confidence that he does not keep back any circumstances in his knowledge." The burden is on the parties to give an accurate representation of the risk; intent is not required, and an innocent misrepresentation suffices to void a policy "because the *risque* run is really different from the *risque* understood and intended to be run at the time of the agreement." Beyond this, good faith prevents either party drawing "the other into a bargain ... by concealing what he privately knows." At common law, if the risk run is other than that intended, the contract would be void for uncertainty.

Monopolies of Information

Historically, the law tended to consider the duty as it lay on the insured, as it was the insured who had a monopoly of information in regard to the circumstance of the loss, but the duty of disclosure was always mutual. In *Banque Keyser Ullman SA v. Skandia (UK) Ins Co. Ltd* the English Court of Appeal held that:

> "... the duty falling upon the insurer must at least extend to disclosing all the facts known to him which were material either to the nature of the risk sought to be covered or the recoverability of a claim under the policy which a prudent insured would take into account in deciding whether or not to place the risk for which he seeks cover with that insurer." (1990) 1 QB 665, 772.

This statement of the insurer's duty was accepted by Lord Bridge in the House of Lords, although the duty does not extend to providing the insured with such information, as cover could be obtained elsewhere at a lower premium. It would also be necessary for the insured to show that the nondisclosure induced the contract. Both parties share the obligations, which stem from the trust and the duty of good faith, as the objective of the law is to place parties on an "equal footing" *Greenhill v. Federal Insurance Co.* (1927) 1 KB 65, 76 (CA). What is central then to the contractual relationship is the imbalance of information, "as the underwriter knows nothing and the man who comes to him to insure knows everything" *Rozanes v. Bowen* (1928) vol. 31 LIL Rep 231. Good faith applies to all types of insurance, *Seaton v. Heath* (1899) 1 QB 782; however, the duty of utmost good faith does not rest on an implied term of the contract, but arises outside of it, as it is based in equity not contract, *The "Good Luck"* (1992) 1AC 233.

Society's transition from the heroic phase of capital accumulation to structural monopoly, in which the balance of power has swung to favour the insurer, has meant that the burden has swung from generally reposing with the insured to catch the insurer with all its technocratic access to information. Beneath this legal transition lies a sociological substrata that charts the law's protectionism as it swings from favouring the fledgling entrepreneurs of the Seventeenth century to shielding the dwarfed individual of the Twentieth. As the economic muscle of the insurer must now be factored in to maintain equality, the law places a burden on the dominant party, which is an obligation to act fairly at all times. *Ontario Inc. v. Lloyds* (2000) 184 DLR (4th) 687 (Ont CA) The Canadian court has allowed substantial punitive damages for serious breaches of this duty. In *Whiten v. Pilot Insurance Co.* (2002) 209 DLR (4th) 257 (SCC), where information in the hands of an insurer did not support the palpably weak affirmative defence of arson put forward by them, the Supreme Court of Canada upheld punitive damages. In *Whiten*, the jury had clearly thought that the defence had been maintained in bad faith and had severely disadvantaged a family, which had lost their home. In the majority, Justice Binnie described the insurer's breach of good faith as an "actionable wrong" that was independent of the contractual terms The extent of this duty of good faith is demonstrated by the Canadian Court's refusal to strike out pleadings that claimed an independent duty of good faith on an insurer's employees, *Spiers v. Zurich Insurance Co.* (1999) 45 OR (3d) 726. In an obiter comment it has been considered a breach of this duty to lure a customer into a contract, knowing there has been a nondisclosure that would obviate any claim, *Gate v. Sun Alliance Insurance Ltd.* (1995) 8 ANZ Ins Cas 75,806.

Misrepresentation

While in *Carter v. Boehm* it was held that even an innocent misrepresentation voided an insurance contract, that decision drew upon the precedents of maritime insurance, which has always been in a special category of insurance. It is now considered that the legal rationale for this burden is that maritime insurance contracts contain the implied term that all material representations had been made by the insured. General insurance law makes a distinction between a misrepresentation, which was careless or negligent, and one that results from innocent misapprehension not amounting to negligence. Negligent misrepresentation or misstatement that is detrimentally relied upon may ground an action in tort for damages, as in *Hedley Byrne v. Heller* (1964) AC 465. Alternatively, rescission or statutory damages for misrepresentation may be available. Beyond common law relief, innocent misrepresentations in the insurance context are actionable in equity if: (1) it is a statement of fact, not opinion or law; (2) it is untrue or inaccurate; (3) it was material to the acceptance of the risk; (4) it is a statement of present fact, not as to the future; and (5) it must have induced the creation of the contract.

Fact, Not Opinion or Law

In regard to the distinction between fact and opinion, statements by those who are assumed to know the facts may be fixed by their status, so that their statements are deemed to be grounded on fact. What is pivotal here, is whether the representor is holding themselves out as someone who is authoritative and can be relied upon.

Untrue or Inaccurate

In regard to the accuracy of the statement, the law looks to the whole truth, and whether the statement reflects that. In *Aarons Reefs v. Twiss*, Lord Halsbury held:

> "It is said there is no specific allegation of fact which is proved to be false. Again I protest, as I have said, against that being the true test. I should say, taking the whole thing together, was there a false representation? I do not care by what means it was conveyed, by what trick or device or ambiguous language, all those are expedients by which fraudulent people seem to think they can escape from the real substance of the transaction. If by a number of statements, you intentionally give a false impression, and induce a person to act upon it, it is not the less false, although, it one takes each statement by itself, there may be difficulty in showing that any specific statement is untrue." (1896) AC 273:281.

Materiality

In general terms, materiality is conditional upon the misrepresentation being in regard to information that a prudent person would have wanted to be accurately informed of, prior to entering the contract.

Present, Not Future Fact

Any representation of facts *in futuro* is a promise, a statement of opinion, or a statement of intention. As equitable relief looks at all the conduct of the parties, statements as to the future can be construed as promissory warranties and as "basis of contract" clauses, as considered in the House of Lords decision in *Anderson v. Fitzgerald* (1853) 4 HL Cas 484. Statements of opinion or belief may be a representation of present fact where there is the implied representation that there is an honest expectation, on reasonable grounds, that events will transpire as forecast, *Bank Leuni le Israel v. Britain National Ins.* (1988) 1 Lloyds Rep 71:75. A statement as to future intention can be construed as a statement of present intention, as the present state of a man's mind is a fact like anything else. The Courts may favour such broad interpretations of *in futuro* facts where there is deceit, *Edgington v. Fitzmaurice* (1884) 29 Ch D 459 483.

Inducement

For the misrepresentation to be actionable, it must have induced the contract, in that it would not have been entered into had the truth been known, *St. Paul Fire & Marine Ins Co. (UK) v. McConnell Dowell* (1995) 2 Lloyds Rep 116: 124-125.

Application of Insurance Principles to Gambling Law

Legally, gambling is almost a *terra nullis*. As an illegal activity, it has long been outside of the law and, as such, contracts of wagering were unenforceable. As Christian morality has been eclipsed by a market ideology, gambling has been sanctioned by the state and, indeed, embraced as a source of revenue. As a now lawful activity, it falls to be treated as any other exchange relationship, but has no body of precedent to define the rights and obligations that condition the transaction.

At civil law, where individuals may seek a remedy for the personal harm caused to them by legalized gambling, new duties of care require proximity; that is, a causative link and an absence of contraindicating policy considerations, *Anns v. Merton London Borough Council* (1978) AC 728. Beyond these two broad fields of inquiry, it is helpful to be able to analogize the extant duties recognized at law. It is maintained that such an analogy between insurance law and legal gambling is tenable.

Vulnerability and Risk

As gaming is nothing but risk, it could be argued that the punter assumes these risks and enters the construct knowing what they are in for. However, the comparison made here is with insurance law, which embodies *uberrimae fidei* duties, the highest class of obligations at law. As with gambling, a contract of insurance is a form of speculation. The terms or circumstance of either is the *risque* understood—the represented odds. What is at issue then, is whether the punters are on notice of the nature of the risk and the extent of their vulnerability. The promoters are also caught with this vulnerability.

By an application of insurance principles, a trust reposes on the parties to ensure that each is not deceived in this, and the risk intended to be run is known. Insurers utilize the most exacting actuaries and access detailed personal databanks to appraise their exposure to risk. Similarly, in calculating their exposure, gambling consortiums bring enormous resources and expertise to bear in determining the risk borne. Against this tour de force, the gamblers are effectively hamstrung or, more accurately, de-brained. They can do nothing but trust to the whim of fate the lotteries or pokies; and, in the casino, skill is specifically prohibited on the part of the punter. Significantly, the gambling consortiums are increasingly promoting a steady shift away from forms of punting such as horseracing, where knowledge of form and odds is of some assistance (if you haven't been told which horse is going to win) to gambling opportunities where intelligence is an obstacle. This shift is not a fortuitous one, but is driven by the promotion of those outlets that direct the most predictable revenue streams back to the consortiums.

There is a marked imbalance of power in the gaming construct that is as great, if not greater, as that between a multinational insurance company and a private individual. Just as most individuals could not sustain the loss of their house or the consequences of a serious personal accident, so too gamblers who are out of control have to gamble more, if they are to have any hope of recovering their losses. It is this vulnerability and the potentiality for such dependency that arguably could ground the placing of a duty of care on gaming consortiums as applies at insurance law.

Monopolies of Information

Casinos routinely deprive customers of even knowing what time of day it is or even whether it is day or night, as casinos are designed to avoid revealing any indication of the passage of time, so as to keep the punters at the wheel. The enormous profits derived from licensed gambling enables the gaming consortiums to amass scientific and statistical data on the efficacy of various forms of gaming. Through psychological profiling, games are purveyed to their maximum effect. The pokies, which are the most profitable form of gambling, are the most sophisticated Skinner boxes known to man or, rather, known to the consortiums, as the design characteristics are never revealed to the punter. To paraphrase *Rozanes v. Bowen*, the casino knows everything and the man who comes to it to gamble knows nothing. Arguably, this imbalance opens the consortiums to a good faith duty to not conceal "what he privately knows, to draw the other into a bargain from his ignorance of the fact, and his believing the contrary," *Carter v. Boehm*.

Misrepresentation: Common Law Remedies

Beyond breaches of good faith attaching to a duty not to conceal, misrepresentations that were careless or negligent could ground an action for damages in the tort of negligent misstatement, as in *Hedley Byrne v. Heller*. Innocent misrepresentation not shown to be culpable could be actionable if the Courts were persuaded that the special circumstances that pertain to maritime insurance law are applicable in the gambling construct. In *Carter v. Boehm*, it was held that even an innocent misrepresentation voided an insurance contract in the special category of maritime insurance. Importantly to this analysis, the special nature of maritime insurance was a consequence of the heightened risks involved and the difficulty of forensic determination of the cause of the loss. Arguably, similar considerations apply to gambling.

Misrepresentation: Equitable Relief

If analogies from the insurance context can be transposed to the gambling construct, then innocent misrepresentations may be actionable in equity if the standard criteria are met. In regard to truth, the legalization of gambling gives authoritative weight to the truth of the consortiums' assertions. As Lord Halsbury held in *Aarons Reefs v. Twiss*, the law looks to the whole truth and whether the statement reflects that. It is the impression given with which the consortiums are fixed. In regard to materiality, it is the information that a prudent person would have wanted to be accurately informed of that is at issue. That information would include the lethality of the machines in question, and the effect of alcohol on the anticipation/adrenaline reaction designed into the display.

As all forms of gambling are contingent upon future events, all facts could be said to be *in futuro* as either a promise, a statement of opinion, or a statement of intention. However, as equitable relief looks at all the conduct of the parties, statements as to the future can be construed as promissory warranties, particularly where the implied representation is that there is an honest expectation, on reasonable grounds, that events will transpire as forecast, or where there is deceit. It would remain necessary for the misrepresentation to have actually induced the contract of gaming or wagering.

Conclusion

The same features of risk and vulnerability, and trust and representation characterize both the gambling and insurance constructs. As applies in insurance law, it is maintained that, in the gambling construct, it is the reliance on the representation that the transaction is a reasonable one that creates the trust. It follows then, that at civil law, purveyors of gambling opportunities could be fixed with the same duties of utmost good faith as apply in insurance law.

In the context of legislative control, this means placing a higher obligation on gambling agencies, both public and private, than that which accords to normal commercial transactions, such as are controlled by Fair Trading and Consumer Guarantees Acts. Given the level of vulnerability, gambling legislation should parallel legislation such as the Door-to-Door Sales Acts, which recognize similar vulnerabilities. The application of this higher threshold would recognize the common law principle that, in high-risk situations, the burden is on the person knowing the risk to inform the other of its extent. If this threshold applied, gambling consortiums would be bound by strict liability, as in this context even an innocent misrepresentation remains a fraud. At a minimum, it would be incumbent on gambling agencies to provide accurate information as to the risk customers undertake and not to conceal what they privately know.

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