



FACULTY OF LAW  
Lund University

Yin Yinan

Entitlement to Insurable Interest  
in Stoppage of Transit  
Under English and Chinese Law:  
A Comparative Study

Master thesis  
30 credits (30 ECTS)

Professor Lars-Göran Malmberg

Master's Programme in Maritime Law

Spring Semester

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# Summary

As the global economy expands, international carriage of goods is playing a more and more important role all over the world. Interdependence of shipping with other commercial activities including insurance is one of the features of international carriage of goods. In the present international business climate, insurance contract is an effective method through which one recovers losses from underwriters in case damage to goods occurs during carriage at sea. Insurable interest in particular is an essential element which is indispensable to render insurance contract a practical, reliable basis of indemnity.

While insurable interest is an important term, in some cases it is problematic to define. One of the problems is to establish who has insurable interest when different contract terms are applied to different sale contracts. Another recurring problem arises when determining when the insurable interest should be attached (during the different stages of the transport of the goods). The issue becomes even more complicated in a situation where the seller orders the right of stoppage in transit.

‘Stoppage in transit’ can be enforced in English law to secure the payment and protect the interests of the unpaid seller, who is entitled to the right to stop the carrier from delivering the goods to the buyer, even after he or she has ceded possession (as long as the goods are in transit). Even though it is legally unclear as to whether the seller could regain insurable interest after exercising the right of stoppage in transit since it is neither regulated nor established through other legal means, the seller has to bear the risk in the transaction due to the insolvency of the buyer.

Chinese law does not include regulations equivalent to the maritime regime term ‘stoppage in transit’. Instead, retention is regulated in civil law as a right for an unpaid seller. Consequently, the seller can rely only

on an injunction granted by the court to prevent the carrier from delivering the goods to the buyer. Therefore, the definition of insurable interest in Chinese law becomes vague and complicated as well when the unpaid seller executes the right of 'stoppage in transit'.

In English law, the definition of insurable interest has developed from a legalistic approach to pecuniary approach gradually. The former is considered a narrower and stricter definition compared with the latter. The current trend shows that the strict approach towards insurable interest is being replaced by the more liberal one. In some sense, this helps with the clarification of ownership of insurable interest, but it does not necessarily solve all of the problems, especially when coming to the definition of insurable interest under FOB contract.

Compared to its counterpart in English law, the definition of insurable interest under Chinese legal framework is not interpreted clearly in the maritime law regime. Complicated by the lack of provisions on stoppage in transit, this directly leads to the fact that although the legalistic approach is adopted, the non-owners of goods, who actually also have interest in the goods in question, cannot get compensation for losses.

# Abbreviations

CIF	Cost, Insurance and Freight
CFR	Cost and Freight
FOB	Free on Board
GPCL	(Chinese) General Principles of Civil Law
MIA 1906	(English) Marine Insurance Act 1906
PRC	People's Republic of China
SOGA	(English) Sale of Goods Act 1979
UK	United Kingdom
US	United States

# 1 Introduction

Suppose a scenario in which one buyer purchases goods from one seller and the purchased goods are shipped to the buyer via a ship as agreed. While the goods are still on the way to destination, the buyer becomes insolvent. Realizing that he will not get paid, the seller repossesses the goods before they could be delivered to buyer. After the repossession, the ship sinks and the goods are lost. When the time comes for recovering the losses from the insurer, the crucial question of who has the right to claim for the lost goods must be answered.

This scenario is nothing out of the ordinary for today's world of multi modal transportation where goods are carried across thousands of miles via land, sea, air or any combination of the three. This paper is concerned with the sea-leg portion of the transportation where billions of dollars worth of goods are traded daily. In the scenario above, the repossession was done under stoppage in transit and the question of who has the right to recover from the insurer falls under the consideration of insurable interests. These two areas are often examined separately even though the possibility of the two aspects meeting in the above situation is not far-fetched.

This paper intends to investigate the different outcomes under English and Chinese laws to the questions arising from the above circumstances.

## 1.1 Purpose of Research

English and Chinese laws have different approaches to insurable interest, the passing of property, the passing of risk, the right to stoppage in transit and the concept of ownership and title. This paper aims to study the legal position of those concepts under both laws in order to answer the questions posed by this paper as illustrated in the introductory section above.



The writer has chosen to focus and compare English and Chinese laws as the former applies to several common law-based jurisdictions, including the United Kingdom (UK) and the United States (US), while the latter's importance is growing amidst China's advancement as a major global economic power house.

Pejovic wrote that 'stoppage in transit has only been sporadically examined by transportation law scholars'. The writer has not come across writings on stoppage in transit in the light of insurable interest. Since this area has not been widely explored, this paper will hopefully shed some light on certain issues in this area. Furthermore, the writer's knowledge and practice in Chinese law and ability to analyze sources in Chinese can contribute not only to this particular area but also towards a better comprehension on how English and Chinese laws may agree or differ on various issues in this field.

In Chapter 2, the writer lays down the concepts crucial to this paper so that readers may get a better understanding of the discussions in the following chapters. Chapters 3 and 4 serve a twofold purpose. Firstly, they aim to hold in depth discussions on issues arising under each area. Secondly, information from the discussions will be applied to the process of answering who has the right to recover compensation from the insurer in the event of the seller exercising the right of stoppage in transit against a non-paying buyer.

## **1.2 Methods**

The writer will examine provisions in statutes relating to the areas researched including those regulating marine insurance, sale of goods, general property and civil law. Decided cases, especially from the common law jurisdiction, will be studied and discussed.

This paper also derives different opinions from the review of literatures written, especially those expounding stoppage of transit and insurable interest.

Having discussed both the primary and secondary sources of law as stated above, the writer will apply statutory provisions in answering the question posed by this paper and draw from opinions of scholars where there appears to be *lacunae* in the law. The writer will also offer her own comments and views on various issues throughout the paper.

### **1.3 Delimitation**

Even though this paper aspires to study the issues of stoppage in transit and insurable interest from the English law point of view, not all the positions from all common law jurisdictions will be included or discussed. The writer will focus primarily on the law as applied in the UK but where possible or necessary, the writer will also refer to certain selected positions from other common law jurisdictions.

Discussions on the different existing contract terms are crucial to this paper as the result of whether a person has insurable interest in the situation where stoppage in transit takes place depends very much on the terms of each contract in the sale. This paper confines its examination to the Cost, Insurance and Freight (CIF), the Free on Board (FOB) and to some extent, the Cost and Freight (CFR) terms, as these are the most common terms being entered into in sale of goods transactions. Although the contract terms ( CIF, FOB & CFR) are discussed in the conception chapters respectively, they will be analyzed deeply when the legal positions of buyers and sellers are not clear under these terms.

## 2 Concepts

### 2.1 International carriage of goods by sea

Martin Dockray outlined three peculiar features of international carriage of goods by sea. The first is the international nature of this business. Whereas land travel may not always transcend national boundaries, shipping has always been connected to international business.<sup>1</sup> Before the advent of air travel, shipping was the only practical means to carry spices from the Moluccas to Venice and tea from Fujian to England. Even after the airplane was invented, shipping still accounts for a vast majority of international carriage of goods. Today, bigger ships are constantly being developed and containerization has revolutionized the international carriage of goods by sea.

The second feature of the shipping industry as pointed out by Dockray is that the special and hazardous conditions under which contracts for the carriage of goods by sea is performed renders it practically impossible for one party to supervise the work of the other from day to day.<sup>2</sup> It is due to this condition that there is every possibility that the scenario being forwarded by this paper in the introductory section could occur.

The third feature of international carriage of goods, wrote Dockray, is the interdependence of shipping with other commercial activities. In fact, the shipping industry is sustained by trading. Thus, carriage contracts intertwine with sales and insurance contracts. When considering issues of stoppage in transit and insurable interest, carriage contracts could also play a role.

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<sup>1</sup> *Martin Dockray, Cases and Materials on the Carriage of Goods by sea, Cavendish Publishing Limited, 2004, at p.1*

<sup>2</sup> *Ibid, at p.1*

## 2.2 Insurable Interest

According to Hodgkin, “English law has narrowly defined what can and cannot be insured.”<sup>3</sup> Section 5 of the English Marine Insurance Act 1906 (MIA 1906) states that ‘every person has an insurable interest who is interested in a marine adventure’. Such person is defined by the same statute as having such interest

“where he stands in any legal or equitable relation to the adventure or to any insurable property at risk therein, in consequence of which he may benefit by the safety or due arrival of insurable property, or may be prejudiced by its loss, or damage thereto, or by the detention thereof, or may incur liability in respect thereof.”<sup>4</sup>

Hodgin opined that while it is evident from the provision that ownership of property or goods is sufficient to found an insurable interest, it is not essential.<sup>5</sup> This is because parties who are not owners of the property or goods but nevertheless may be liable for loss or damage of the said property or goods must have insurable interest in them. One such party would be the bailee of those items. Thus, legal liability is a foundation upon which insurable interest may be established.

However, it is difficult to determine the exact boundaries of what constitutes insurable interest. Howard Bennett wrote that there exists a misconception that the test for insurable interest is absence of wage since there is a close historical connection between insurable interest and wagering of contracts.<sup>6</sup> The requirement of marine insurance law that insurable interest must arise at

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<sup>3</sup> Susan Hodges, *Law of Marine Insurance*, Cavendish Publishing Limited, 1996 at p.vii

<sup>4</sup> *Marine Insurance Act 1906*

<sup>5</sup> Susan Hodges, *Law of Marine Insurance*, Cavendish Publishing Limited, 1996, at p.55

<sup>6</sup> Howard Bennett, *The law of Marine Insurance*, Oxford, 2006, at p.67

the time of loss, which will be discussed further in chapter 3, shows that such insurance policies are meant to indemnify and do not subsist on wagers. Insurable interest is based on an expectation that the claimant will have such interest if the goods are lost or damaged. As a result, if the aspiring claimant does not fulfill the expectation, he will have no claim even if he is the insured.

### 2.3 Stoppage in Transit

Pejovic wrote that 'stoppage in transit is a remedy, which secure the payment of the price and protect the interests of unpaid sellers' and that '[i]t was originally developed by the English Chancery Courts, and was based on the equitable doctrine under which a beneficial owner was allowed to trace the property held by a fiduciary, including a bailee, even where the property had been transferred'.<sup>7</sup>

According to Pejovic, when possession of goods is transferred to a buyer from the seller without the former having paid for the goods, a conditional delivery of possession arises subject to payment of the price by the buyer. Thus, should the buyer fail to make payment, the seller has the right to enforce stoppage in transit by issuing the relevant orders to the carrier.<sup>8</sup>

Under English law, stoppage in transit was defined as

"the right of the unpaid vendor, on discovery of the insolvency of the buyer, and notwithstanding that he has made constructive delivery of the goods to the buyer, to retake them . . . before they reach the buyer's possession."<sup>9</sup>

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<sup>7</sup> Caslav Pejovic, *stoppage in transit and right of control, conflict rules?* *Pace International Law Review*, Spring 2008 *Tulane Maritime Law Journal*, at p.12

<sup>8</sup> *The Carriage of Goods by Sea Act, 1992* (U.K.)

<sup>9</sup> Caslav Pejovic, *stoppage in transit and right of control, conflict rules?* *Pace International Law Review*, Spring 2008 *Tulane Maritime Law Journal*, at p.11

This concept is not only found in English law but also in most common law jurisdictions. Legislations have been enacted to incorporate the right of stoppage. Section 44 of the English Sale of Goods Act of 1979 and section 2-705 of the American Uniform Commercial Code entitle the unpaid seller of goods the right to stop the goods in transit if the buyer becomes insolvent.<sup>10</sup> The seller without receiving the payment, under this remedy, has the right to order the carrier not to deliver the goods to the buyer regardless of whether or not the buyer is the lawful holder of the document which indicates him as the consignee. Although the seller has ceded possession he still has the right to stop the goods in transit, by giving notice of this claim to the carrier or other bailees who are holding custody of the goods as long as the goods are in transit.<sup>11</sup>

Civil law recognizes the principle of contracts for the benefit of contract instead of the common law principle. As a result, most civil law jurisdictions do not recognize stoppage in transit.<sup>12</sup> According to this principle, since the seller transfers the negotiable document to the buyer he has lost the right to give instructions to the carrier. This stems from the fact that the negotiable document is the source of this right against the carrier.

Legislation on the right of retention can be found in civil law, instead of the right of stoppage in transit in common law, which can protect the seller.<sup>13</sup> The main difference between these two rights under different legal regimes rests on whether the seller has the right of giving orders to the carrier. The right of stoppage of transit entitles the unpaid seller the right to issue orders to the carrier while the unpaid seller with the right of retention cannot make the orders to the carrier directly. However, the seller has another alternative way to protect his own right, which is injunctions granted by the court as a provisional remedy. In this case, the unpaid seller

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<sup>10</sup> *Sale of Goods Act, 1979, c. 54*

<sup>11</sup> *Sale of Goods Act, § 44.*

<sup>12</sup> *Caslav Pejovic, stoppage in transit and right of control, conflict rules? Pace International Law Review, Spring 2008 Tulane Maritime Law Journal. P.14*

<sup>13</sup> *Ibid, p 15g*

may rely on the injunction to stop the carrier from delivering the goods to the consignee.

A number of remedies for sellers are also stated in the United Nations Convention on Contracts for the International Sale of Goods (CISG). One of the remedies at the seller's disposal speaks of stoppage in transit as defined in Article 71(2):

'If the seller has already dispatched the goods before the grounds described in the preceding paragraph become evident, he may prevent the handing over of the goods to the buyer even though the buyer holds a document which entitles him to obtain them. The present paragraph relates only to the rights in the goods as between the buyer and the seller.'<sup>14</sup>

This means that a seller who has already dispatched the goods may prevent passing the goods to a buyer who refuses to pay or becomes unable to pay the price regardless of whether the buyer holds the document which entitles him to obtain the goods. Under article 71(2), an actual breach of contract by the buyer is not required as a condition, which allows the seller to exercise the right of stoppage. In order to exercise the right of stoppage, it must be evident that the buyer will not ultimately fulfill his duty of payment.<sup>15</sup>

## **2.4 Contract Terms**

### **2.4.1 Cost, Insurance, Freight (CIF)**

When a sale of goods contract takes on the nature of "Cost, insurance and freight" terms, the seller delivers when the goods pass the ship's rail in the port of shipment.

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<sup>14</sup> CISG, art. 71(2)

<sup>15</sup> Alexander von Ziegler, *The Right of Suspension and Stoppage in Transit*, 25J. L. & Com. 353, 368 (2005)

The seller must pay the costs and freight necessary to bring the goods to the named port of destination but the risk of loss of or damage to the goods, as well as any additional costs due to events occurring after the time of delivery, is transferred from the seller to the buyer. However, in CIF contracts, the seller also has to procure marine insurance against the buyer's risk of loss of damage to the goods during the carriage.

Consequently, the seller contracts for insurance and pays the insurance premium and the buyer should note that under CIF terms, the seller is required to obtain insurance only on minimum cover. Should the buyer wish to have the protection of greater cover, he or she would either have to expressly agree with the seller or arrange for extra insurance coverage. The CIF term requires the seller to clear the goods for export and these terms can be used only for sea and inland water way transport.<sup>16</sup>

#### **2.4.2 Free on board (FOB)**

"Free on board" terms reflects the condition where the seller delivers when the goods pass the ship's rail at the named port of shipment. This means that the buyer has to bear all costs and risks of loss of or damage to the goods from that point. The FOB term requires the seller to clear the goods for export. This term can be used only for sea or inland waterway transport.<sup>17</sup>

#### **2.4.3 Cost and freight (CFR)**

"Cost and freight" means that the seller delivers when the goods pass the ship's rail in the port of shipment.

The seller must pay the costs and freight necessary to bring the goods to the named port of destination but the risk of loss of or damage to goods, as well

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<sup>16</sup> <http://www.iccwbo.org/incoterms/preambles/pdf/CIF.pdf>

<sup>17</sup> <http://www.iccwbo.org/incoterms/preambles/pdf/FOB.pdf>



as any additional costs due to events occurring after the time of delivery are transferred from the seller to the buyer. The CFR term requires the seller to clear the goods for export. Like the CIF and FOB, this term can be used only for sea and inland waterway transport.

# 3 Insurable Interest Under English and Chinese Laws

## 3.1 Background comparison

Insurable interests developed in order to distinguish indemnity insurance from wager policies and to satisfy the requirement of the indemnity principle itself that the assured should suffer a loss against which he can be indemnified. The background and development of this concept under English law and Chinese law are as follows.

### 3.1.1 English law

In relation to marine insurance, the requirement of insurable interest is statutory. The concept of insurable interest occupies a significant position in the historical development of marine insurance law. An entire part of the codified marine insurance, extending from section 4 to 15, is devoted to insurable interest.

Before statutory intervention in 1745, the law relating to insurable interest developed at common law. Gaming and wagering contracts are also the subject of restrictions in the general law of contract.

The requirement of an insurable interest is a manifestation of the fundamental characteristic of an insurance contract as a contract of indemnity.<sup>18</sup> Historically, however, the common law enforced contract to public policy,<sup>19</sup> and, after some initial reluctance, the courts came to the

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<sup>18</sup> *Lucena v. Craufurd*(1803)2 Bos & Pul (NR) 269, 302

<sup>19</sup> *Robert Merkin, Colivaux's Law of Insurance, London, Sweet & Maxwell, 1990, p45.*

view that it was open to the parties to conclude an enforceable wager policy by expressly dispensing with the insurable interest requirement.<sup>20</sup>

The MIA 1906 addresses insurable interest as an essential element of a civil commercial contract and provides for the consequences that follow when it is absent. There is also a criminal dimension to the subject which is established by the Marine Insurance (Gambling Policies) Act 1909. Under the statute, assureds, employees of ship owners, brokers and other agents, and insurers may be guilty of a criminal offence if they effect or are party to effecting a marine insurance contract without an insurable interest. The 1909 Act has been of little consequence for it appears that a prosecution has never been instituted under its provisions. The contemporary legal significance of the Act is whether by implication it colors the status of a marine insurance contract made without interest and renders it illegal as distinct from merely void.

### **3.1.2 Chinese law**

There is no separate legislation governing marine insurance in China. But some provisions on Marine insurance are laid down in chapter XII of the Maritime Code, Contract of Marine Insurance. This chapter consists of six sections: Basic Principles; Conclusion, Termination and Assignment of Contract; Obligations of the Insured; Liability of the Insurer; Loss of and Damage to the Subject Matter Insured and Abandonment; and Payment of Indemnity.<sup>21</sup> However, Chapter XII of the Maritime Code, Contract of Marine Insurance, does not expressly address the issue of insurable interest. Only a general reference in relation to the insurable interest in property can be found in article 12 of the Insurance Law of People's Republic of China

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<sup>20</sup> *Ibid*, p52

<sup>21</sup> Kevin X. Li Tingzhong Fu Ling Zhu Yunlong Liu, *Marine insurance law in China*, *Tulane Maritime Law Journal*, Summer 2008, p 24

(PRC).<sup>22</sup> Unfortunately, the Insurance Law does not include a specific provision on insurable interest in property. There are less than seventy provisions governing insurance contracts, which is admittedly inadequate to cover all aspects of insurance contract law. Accordingly, article 90 of the Insurance law provides that, when there is a lacuna, the relevant provisions of the General Principles of Civil Law of the PRC and the Contract Law of the PRC shall apply<sup>23</sup>.

According to the Chinese legal system and the current insurance law structure, marine insurance law in the Maritime Code is a specific law and the Insurance Law is a general law. By virtue of article 153 of the Insurance Law, provisions in the Maritime Code shall be applicable to marine insurance; meanwhile, for matters not specified in the Maritime Code, the Insurance Law shall apply. However, this article cannot adequately address all of the possible issues that may arise, such as insurable interest.

Laws pertaining to maritime transport and ships, which have many elements originating from the English legal system, are different from the continental tradition of the overall legal system in China so that these laws are alien to the Chinese legal system to some extent.

Accordingly, marine insurance law also embodies many characteristics that are distinct from the general insurance law. The Insurance Law was a product of civil law while the enactment of chapter XII of the Maritime Code, Contract of Marine Insurance, was greatly influenced by common law<sup>24</sup>. Thus, many stipulations with respect to marine insurance in the Maritime Code are not in line with their counterparts in the Insurance Law. Insurable interest becomes an issue.

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<sup>22</sup> *Insurance Law of PRC, Art 12*

<sup>23</sup> *Ibid, Art90*

<sup>24</sup> *Huag Weiqing, On the Insurable Interest of International Marine Cargo, Annual of China maritime law*

## **3.2 When must insurable interest be demonstrated?**

A party involved in a sale of goods may or may not have insurable interest at different points of time in the entire duration of the transaction. This is to say that when the goods are damaged or lost, only the party having insurable interest will be entitled to receive compensation from the insurer. Therefore, the importance of timing during which insurable interest arises cannot be overemphasized.

### **3.2.1 English law**

The law is clear in the UK on when insurable interest must be demonstrated. Section 6(1) of the Marine Insurance Act 1906 states that

the assured must be interested in the subject-matter insured at the time of the loss though he need not be interested when the insurance is effected:

Provided that where the subject-matter is insured “lost or not lost,” the assured may recover although he may not have acquired his interest until after the loss, unless at the time of effecting the contract of insurance the assured was aware of the loss, and the insurer was not.

Thus, unlike life insurance, insurable interest must exist at the time of loss and not at point of time when the contract is made. The now obsolete SG policy, used by the London market until the early 1980s,<sup>25</sup> included “lost or not lost” wording. The modern institute cargo clauses do not.

### **3.2.2 Chinese law**

Li, Fu, Zhu and Liu wrote that Chinese insurance law does not specify when insurable interest is required. However, Li Yuquan pointed out that article

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<sup>25</sup> *Howard Bennett, The law of Marine Insurance, Oxford. P72*

12 of the Chinese Insurance Law mandates that insurable interest must exist at the time the insurance contract is made regardless of whether the insurance cover life or property.<sup>26</sup> On this, Li, Fu, Zhu and Liu remarked that these regulations reflect the socialist ideology of China. However, they represented the beginning of insurance law in the then newly established People's Republic of China and was the first step towards rule of law. However, Li Yuquan and Sun<sup>27</sup> opined that a difference must be made between life and property insurance. This opinion reflects the position of English law where insurable interest must arise only at the time of loss and not at the inception of the insurance contract. Li, Fu, Zhu and Liu noted that 'Chinese judges tend to follow this point of view'<sup>28</sup>

### **3.3 Who has insurable interest?**

#### **3.3.1 English law**

This question was addressed by the House of Lords in *Macaura v. Northern Assurance*.<sup>29</sup> In this case, the insured was the sole shareholder in a company as well as an unsecured creditor of the company. The company had only one asset, which was a certain timber. The shareholder then insured the timber against fire in his own name. The timber was actually destroyed by fire and the insured accordingly filed claims with the insurer. In holding that the shareholder had no insurable interest, Lord Sumner remarked that a company has its own legal personality separate from that of its shareholders. The shareholder stood in no legal or equitable relationship to the timber and therefore, could not recover from the insurer for his losses.

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<sup>26</sup> Li Yuquan, *Insurance Law* (2003), p44-45

<sup>27</sup> *Ibid*, p 81, 86

<sup>28</sup> Kevin X. Li Tingzhong Fu Ling Zhu Yunlong Liu, *Marine insurance law in China*, *Tulane Maritime Law Journal*, Summer 2008, p 446

<sup>29</sup> [1925] AC 619

In an earlier decision, *Wilson v. Jones*,<sup>30</sup> the company in question was attempting to lay the first transatlantic telegraph cable on the bed of the ocean, which was the subject insured. The court held that if the shareholder was attempting to insure the cables in his name, he would have no insurable interest to do so as he did not have any legal or equitable interest in relation to the cable. However, the court considered the construction of the insurance policy and found that the shareholder was in fact insuring his interests in the value of the shares. Obviously, in this case, the value of the shares would be tied to the mega project that the company undertook and would take a plunge in the event of failure.

From these cases, though they wielded different results, the *ratio decidendi* behind both decisions was the same, i.e., persons without legal or equitable connection to the goods insured are not deemed to have insurable interest. However, as in the case of *Wilson*, this problem could be circumvented by designing the terms of the insurance policy in a way that causes the person who would not have direct insurable interest in the goods to have a legal nexus to the goods via a link between the two.<sup>31</sup>

In some other commonwealth jurisdictions, however, the approach of the courts towards this issue is not as narrow. Canada, for example, places an emphasis on whether the insured person has suffered pecuniary loss as a result of the property damage rather than requiring the insured to demonstrate legal or equitable interest in relation to the goods. In *Constitution Insurance Co of Canada v. Kosmopoulos*,<sup>32</sup> the insured was the sole shareholder, director and lessee of a business who insured the premises of the business in his own name. When the building was damaged, the Supreme Court held that he had insurable interest due the pecuniary damage he suffered.

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<sup>30</sup> (1867) LR 2 Ex 139

<sup>31</sup> *Susan Hodges, law of marine insurance, Cavendish Publishing Limited, 1996*  
P 61

<sup>32</sup> 34 DLR (4th) 208 (1997)

Similarly, section 17 of Australia's Insurance Contracts Act 1984 states that

where the insured under a contract of general insurance has suffered a pecuniary or economic loss by reason that property the subject-matter of the contract has been damaged or destroyed, the insurer is not relieved of liability under the contract by reason only that, at the time of the loss, the insured did not have an interest at law or in equity in the property.

In the UK, in conformity with *stare decisis*, the position in *Macaura* is applicable. More than one person could have insurable interest if they can show legal and equitable interest in the goods insured and the apportionment of insurable interest to each of the claimants depends on the factual circumstances occurring at the time of the goods being damaged or lost. Thomas wrote that “under an international sale contract it is not only the party who bears the risk who has the right to insure. (...) The title to the goods may not be conveyed at the same time as the transfer of risk, and so the owner without risk continues to possess an insurable interest by virtue of the retained title.”<sup>33</sup>

Questions regarding risk, title, possession and other relevant matters that weigh in on the determination of insurable interest status can only be answered based on the terms of the sale of goods, as follows:

**i) Passing of property**

Section 17(1) of the English Sale of Goods Act 1979 (SOGA) states that ‘where there is a contract for the sale of specific or ascertained goods the property in them is transferred to the buyer at such time as the parties to the contract intend it to be transferred.’

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<sup>33</sup> D. Rhidian Thomas, *Insurance for the Benefit of Buyers under International Sales* p 120



**a) CIF**

In *Ross T. Smyth and Co Ltd v. TD Bailey, Son and Co*,<sup>34</sup> property in a CIF sale passes upon transfer of documents to the buyer and payment of the price by the buyer to the seller. However, the buyer receives the property conditional on the goods being in conformity with the contract of sale, failing which, the goods will revert in the seller.<sup>35</sup>

Section 16 of the SOGA used to be the single determining factor in the passage of property for goods that form part of a bulk. It states that ‘where there is a contract for the sale of unascertained goods no property in the goods is transferred to the buyer unless and until the goods are ascertained.’ Carr & Stone noted that this presents a disadvantage to the CIF buyer in a situation where the seller becomes insolvent or bankrupt.<sup>36</sup> The injustice of this rule has since been redressed by the amendment of the SOGA in the form of section 20A.

Under section 16, since the buyer must pay the seller before the property has passed, the buyer could suffer enormous losses. In *Re Wait*,<sup>37</sup> the buyer purchased and paid for 500 tons of wheat out of a total of 1,000 tons onboard a ship. The seller was declared a bankrupt before the goods could be ascertained. Since property is not deemed to have passed to the buyer due to the lack of ascertainment of the goods, the trustees in bankruptcy claimed the goods. The court held that the buyer could not appeal to equity for passage of property as it is determined solely by the SOGA.

Fortunately for buyers in such situations today, section 20A provides, among others, the following remedy:

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<sup>34</sup> [1940] 3 All ER 60, 68

<sup>35</sup> *Indira Carr, Peter Stone, International trade law, 2005, 26*

<sup>36</sup> *Ibid*, p 26

<sup>37</sup> (1927) 136 LT 552

20A Undivided shares in goods forming part of a bulk

(1) This section applies to a contract for the sale of a specified quantity of unascertained goods if the following conditions are met—

(a) the goods or some of them form part of a bulk which is identified either in the contract or by subsequent agreement between the parties; and

(b) the buyer has paid the price for some or all of the goods which are the subject of the contract and which form part of the bulk.

(2) Where this section applies, then (unless the parties agree otherwise), as soon as the conditions specified in paragraphs (a) and (b) of subsection (1) above are met or at such later time as the parties may agree—

(a) property in an undivided share in the bulk is transferred to the buyer, and

(b) the buyer becomes an owner in common of the bulk.

**b) FOB**

In *Pyrene and Co v. Scindia Navigation Co Ltd*<sup>38</sup> it was held that in FOB sales, property usually passes upon the goods crossing the ship's rail. However, according to section 19(2) of the SOGA, 'where goods are shipped, and by the bill of lading the goods are deliverable to the order of the seller or his agent, the seller is prima facie to be taken to reserve the right of disposal.' The court in *The Parchim*<sup>39</sup> held that section 19(2)'s presumption is, however, rebuttable.

For the case of goods forming part of a bulk, like in CIF sales, property passes on ascertainment. What constitutes ascertainment in FOB sales is

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<sup>38</sup> [1954] 1 Lloyd's Rep 321

<sup>39</sup> (1918) 117 LT 738

discussed in *Carlos Federspiel and Co SA v Charles Twigg and Co Ltd*<sup>40</sup> where 85 bicycles were bought and paid for. Just before the seller became insolvent, the bicycles were packed and tagged with the buyer's name but not sent to the port of loading. The court ruled that these acts do not amount to irrevocable earmarking and therefore ascertainment has not occurred. As a result, property had not passed and the goods were acquired by the receiver.

## **ii) Passing of risk**

Section 20 of the SOGA states, among others, that

(1) Unless otherwise agreed, the goods remain at the seller's risk until the property in them is transferred to the buyer, but when the property in them is transferred to the buyer the goods are at the buyer's risk whether delivery has been made or not

(2) But where delivery has been delayed through the fault of either buyer or seller the goods are at the risk of the party at fault as regards any loss which might not have occurred but for such fault.

## **a) CIF**

However, as Carr and Stone pointed out, the position in section 20 above is obviously not applicable to CIF contracts as risk rarely passes along with the property.<sup>41</sup> Even though the risk passes at the ship's rail, the property will only pass to the buyer upon delivery. Due to the risk passing at the ship's rail, the buyer is usually obliged to pay against valid documents, even though he has not received the goods. If the goods are lost or damaged on transit, the buyer is still obliged to complete payment. However, he could file a claim with the insurer to recover his losses, unless the losses were

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<sup>40</sup> [1957] 1 Lloyd's Rep 240

<sup>41</sup> Indira Carr, Peter Stone, *International trade law*, 2005, 27

caused by incidents not covered by the terms of the insurance policy. This principle was approved by the court in *Mabre Saccharine Co Ltd v Corn Products Co Ltd*<sup>42</sup>.

Thomas wrote that “a CIF seller who is to be paid against documents usually retains title until payment and consequently retains also an insurable interest until this moment, notwithstanding that risk passed to the buyer on shipment.<sup>43</sup>” This was also the view of Carr and Stone.<sup>44</sup>

## **b) FOB**

In *Pyrene*, it was held that risk passes upon shipment in FOB sales. Thus, a majority of FOB sales would reflect section 20 above. However, should there be a delay in the passing of property to a time later than the goods passing the rail of the ship, the passing of risk is unaffected regardless of whether goods have been ascertain or whether the seller retains the document of title.<sup>45</sup>

However, since property passes upon shipment, the document of title would have been given to the buyer when the goods are placed onboard the ship. Therefore, it would seem that title vests with the buyer in FOB sales and this means that the buyer would have insurable interest after the goods pass the rail of the ship.

### **3.3.2 Chinese law**

The term insurable interest or its equivalent is not found in Chinese statutes including Chapter XII of the Maritime Code, Contract of Marine Insurance.

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<sup>42</sup> [1915] 1KB 189

<sup>43</sup> *Thomas*, footnote 6

<sup>44</sup> *Indira Carr, Peter Stone, International trade law*, 2005, 26

<sup>45</sup> *Indira Carr, Peter Stone, International trade law*, 2005, 45

Nevertheless, in practice, the concept of insurable interest is recognized and used by the industry in China. When claims are presented in courts, however, different interpretations have been given by different courts. According to Li, Fu, Zhu and Liu, the Supreme Court of the People's Republic of China 'has recognized that the person who has legal possession of an insured subject matter has an insurable interest in its safety' but this opinion 'has been given a narrow interpretation by the maritime courts'.<sup>46</sup> The Maritime Court of Tianjin has held that 'only the owner of the insured subject matter can be the insured'.<sup>47</sup> This is clearly disadvantageous to those who may have perfectly legitimate and justifiable interests in the goods insured but are not owners of the goods. According to such interpretation, these parties may not be insured or claim for compensation should the goods become damaged.

**i) Passing of property :**

Although in Chinese Civil Law there are provisions in relation to the passing of property there is no provision that addresses how to define the passing of property during international carriage of goods. It is difficult to point out the factors that determine whether and when good title passes from the seller to the buyer. There are many different opinions on this issue. Should the passing of property be dependent on "passing of risk", be determined by the delivery, or be defined by passing of documents?

Since China is one of the parties to the Convention on Contracts for the International Sale of Goods, according to Chinese Civil Law, the provisions of CISG should be applied. Article 142 of the CISG states that

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<sup>46</sup> *Kevin X. Li Tingzhong Fu Ling Zhu Yunlong Liu, Marine insurance law in China, Tulane Maritime Law Journal, Summer 2008*

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<sup>47</sup> *Ibid,447*

The application of law in civil relations with foreigners shall be determined by the provisions in this CHAPTER.

If any international treaty concluded or acceded to by the People's Republic of China contains provisions differing from those in the civil laws of the People's Republic of China, the provisions of the international treaty shall apply, unless the provisions are ones on which the People's Republic of China has announced reservations.

International practice may be applied on matters for which neither the law of the People's Republic of China nor any international treaty concluded or acceded to by the People's Republic of China has any provisions.<sup>48</sup>

However, the Incoterms 2000-type of contract terms as applied in China includes a provision for the moment during which the risk of loss or damage in the goods will pass from seller to buyer. This will be different points of time depending upon the particular contract terms adopted. The transfer of risk is however limited to the risk of loss or damage to the goods and no more. It does not confer any transfer of proprietary interest in the goods. It also does not cover loss or damage specifically caused by the seller or buyer. The time of transference of ownership in the exported goods will be governed by other express terms in the sales contract and/or the governing law. Transfer may be linked if a maritime carriage is done through the transfer of a bill of lading. Transfer of ownership may be expressly subject to receipt of payment. These clauses, commonly referred to as "retention of title" clauses, are independent of the contract terms. Its applicability and enforcement will depend upon how clearly it is worded and whether such clauses are valid under the law governing the sales contract.

#### **a) CIF**

One of the obligations of a CIF seller is to procure insurance for the benefit of the buyer to cover the risks during ocean transit, and to obtain and deliver

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<sup>48</sup> *Chinese Civil Law Art.142*

to the buyer the appropriate insurance document(s). After the goods pass the ships' rail, buyer starts to undertake the risk of goods. So, before the goods pass the ship's rail, the buyer has no ownership of the goods and has not undertaken the risk. Once the loss or damage to goods happens, whether buyer has insurable interest to the subject-matter becomes an issue. In Chinese law, the person who has legal possession of an insured subject-matter has an insurable interest in its safety. It means that the buyer may not receive any indemnity even though the goods have been insured by the seller.

#### **b) FOB and CFR**

In FOB and CFR, procuring insurance is the buyer's obligation in covering the risk of goods during the transit. So, before the goods pass the ship's rail, the buyer has to sign an insurance contract with the insurer in advance. However, the buyer has yet to gain possession of the goods and has not started to bear the risk. As discussed earlier, according to Chinese law provisions, insurable interest must exist at the time the insurance contract is made, whether it is a life insurance or property insurance contract. In other words, if the buyer has no insurable interest to the subject-matter insured, the insurance contract could not have come into effect in the first place. If the buyer, as a party to the insurance contract can not fulfill the requirement of the rule, which states that insurable interest must exist at the time the insurance contract is made. In this case, whether the policy is a valid contract then becomes a question.

Therefore, there can be no more crucial issue than the proper formulation of the test of insurable interest. Unfortunately, one cannot find a clear definition on insurable interest in Chinese law, neither in Chinese Maritime Law, nor in the Insurance Law of the PRC. The only provision that can be applied here to explain the issue is provided in Article 12 of the Insurance Law of the PRC, as follows,

An insurant shall own the insurable interest in the objects of insurance.

If an insurant has no insurable interest in the objects of insurance, the insurance contract shall be invalid.

Insurable interest refers to the interest of the insurant in the objects of insurance recognized by law.

Objects of insurance refer to property or related interest insured or life and health of a person insured

Apparently, this definition on insurable interest is the legalistic approach. In fact, it follows a narrow and strict approach, which had been accepted by the House of Lords, the majority, including *Lord Eldon*<sup>49</sup> in common law. However, even though the English decision is narrow and strict, it concerns the requirement of having a legal and equitable relationship with the goods insured while the Chinese maritime courts' narrowness in approach is much more restrictive as they have held that only the owner of the goods may be insured. From the discussion above, it would seem that the approach in regard to the definition of insurable interest could not accommodate the development of modern international business for long.

Thus, it is proposed that the position as expounded by the Supreme Court of the PRC is also applied alongside the provision permitting the owner of the insured goods to be the insured. Recognizing persons who have legal possession of an insured subject matter as having an insurable interest in its safety ensures that parties who should receive protection of insurance coverage should have the right to do so.

## **ii) Passing of risk**

A legalistic approach is adopted to define who has the insurable interest to

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<sup>49</sup> *Cf. Wilson v Fones (1867) LR 2 139*



the subject-matter insured in Chinese law, which is a very strict approach. Thus, insurable interest during carriage of goods is only related to the passing of property which has been mentioned in the previous section. Therefore, when discussing the definition of insurable interest, the passing of risk would not be regulated under Chinese law as it would be dealt with under the passing of property instead.

### **3.3.3 From the legalistic approach to pecuniary interest approach**

The proper formulation of the test of insurable interest is definitely a crucial issue. It is therefore unfortunate that the law has yet to arrive at a clear and certain test. In its present condition the law is unquestionably in a state of flux, embodying several approaches to the question of interest, some settled and others less so, but cumulatively suggesting an expansive outlook.

The legalistic approach to insurable interest has had a significant impact in the development of the law. It was adopted by the House of Lords in *Anderson v Morice*<sup>50</sup> and *Inglis v. Stock*,<sup>51</sup> decisions which indicate that the purchaser of goods without title does not possess an insurable interest until risk has passed to the purchaser. This stance was again adopted by the House of Lords in *Macaura*,<sup>52</sup> a case which may be regarded as the high water mark of the legalistic approach and which confirmed that a person who was effectively a sole shareholder and unsecured creditor of a company did not have an insurable interest in the assets of the company. This approach is said to be an effective counter to any attempts of gambling in the guise of insurance contracts. Furthermore, another advantage derived from this approach is that it produces a relatively greater degree of certainty and protects against the insurance of speculative losses.

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<sup>50</sup> *Anderson v. Morice* (1876) 1 App. Cas. 713

<sup>51</sup> *Inglis v. Stock* (1885) 10 App. Cas. 263

<sup>52</sup> *Macaura v Northern Assurance Co Ltd*, [1925] AC 619

Although Section 5 of MIA1906 gives a complete picture of the contemporary legal approach to insurable interest, the definition in section 5 reflects the narrow, restrictive legal approach, and conveys nothing of the wider dynamic approach being developed by the common law. However, the provisions of the MIA 1906 do not represent a hurdle to the adoption of the pecuniary interest approach for it is now accepted that definition set out in section 5(2) is inclusive and not exclusive<sup>53</sup>

The pecuniary interest approach is much wider in relation to the question of insurable interest with the emphasis placed wholly on pecuniary interest, free from the additional constraint of having to prove that the pecuniary interest arose from the insured's legal or equitable relation to the subject-matter insured. This approach finds its most compelling expression in the opinion given by Lawrence J in *Lucena V Craufurd*,<sup>54</sup> which was rejected by the House of Lords.

The advantage of the approach is that it renders the test of insurable interest less technical and legalistic, and gives the law a desirable flexibility.<sup>55</sup> However, the approach is far from clear as to the degree of evidence that is required to establish a pecuniary interest. Pecuniary interest is not stable and is devoid of certainty.

As per the discussion above, the question of how does one define insurable interest, therefore, becomes an issue during international carriage of goods. Although China applies to maritime law principles from common law, only the legalistic approach on how to define insurable interest seems to have been adopted. Additionally, the provisions on marine insurance in the

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<sup>53</sup> D. Rhidian Thomas, *Marine insurance in transit*, London Informa, 2006; P 35

<sup>54</sup> GAO Tao, *Insurable Interest of Transportation Contract in International Trade*, *Journal of Shenzhen Polytechnic*, No4 2006

<sup>55</sup> D. Rhidian Thomas, *Marine insurance in transit*, London Informa, 2006; P 36

Chinese legal framework and Chinese Civil Law (including contract law and insurance law) belong to common law system and continental law respectively. Thus, when problems arise amidst the environment of complex international trade, the issue of insurable interest could not be fixed appropriately.

# 4 Position of Insurable Interest in Stoppage of Transit

## 4.1 The Position of Stoppage in Transit

### 4.1.1 English law

Section 39(1)( b) of the SOGA provides that ‘notwithstanding that the property in the goods may have passed to the buyer, the unpaid seller of goods, as such, has by implication of law— in the case of the insolvency of the buyer, a right of stopping the goods in transit after he has parted with the possession of them’

When the seller has parted possession with the goods, possession passes to the master of the ship, i.e., the carrier. The question of transit arises here since once transit has ended, the right of stoppage in transit ceases to exist. Transit is said to end once the buyer takes delivery, which is determined by the master of the ship acknowledging that he is holding the goods for the buyer. This usually takes place when the ship has arrived at the port of destination and the buyer has presented the master with proper documents of title for the goods.

However, in certain cases, the buyer owns the ship or is the charterer of the ship. If the master of the ship also acts as an agent of the buyer, he can act on behalf of the buyer in taking delivery of the goods. In such cases, transit ends upon the goods being placed on the ship and the seller ceases to have the right to exercise his right of stoppage.

In another situation, where the goods are still in transit but the buyer had sold the goods to a third party either before or after he becomes insolvent or bankrupt, the seller could still exercise the right of stoppage of transit if he did not assent to such sale and if the document of title had not passed to the

*bona fide* third party purchaser for valuable consideration.<sup>56</sup>

#### **4.1.2 Chinese law**

Fei Ning wrote that

unlike other countries, Chinese law provides no express statements concerning the principle of stoppage in transit. However, Article 71 of the General Principles of Civil Law (GPCL) states, “‘Property ownership’ means the owner’s rights to lawfully possess, utilize, profit from and dispose of his property.”<sup>57</sup>

The right of stoppage includes the right of the seller to repossess the goods he sold and which are being delivered to the buyer. The implication of article 71 of the GPCL adds a twist to this in that only sellers who hold the title of ownership may exercise the right exercise the right of stoppage in transit. Therefore, if the seller holds the bills of lading to the goods, for example, he could be considered to be the owner of the goods still and would be able to exercise his right of stoppage in transit. However, if the title no longer resides with the seller, he loses the right to exercise such right. This would include situations where the seller has sold the goods to a third party. It is not immediately clear if this would also apply to cases where the third party owner is not a purchaser in good faith for valuable consideration.

Since China is a member of the Vienna Convention, the principle of stoppage in transit expressed in Article 85 of the Convention can be applied in cases where both contractual parties are members of this Convention or where the parties choose the Convention as the applicable law for the contract.

As noted by Li, Fu, Zhu and Liu previously, Chinese laws are moving

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<sup>56</sup> *Indira Carr, Peter Stone, International trade law, 2005, 24*

<sup>57</sup> *Fei Ning in Alexander von Ziegler, Transfer of Ownership in International Trade, 1999, 292*

forward from their socialist origins. Fei Ning stated that China's law of contracts is in the process of drafting and that article 52 of the sixth draft of the said law provides that

a party having pre-performance obligations arising out of the contract or the law has the right to suspend his performance if he has evidence which proves that the other party : a) is incapable of fulfilling the obligation; b) has unreasonably transferred property or other assets in order to escape from his obligation; c) commits fraud during the transaction; d) is in severe financial difficulties to such an extent that he may be insolvent; or e) has failed to notify the other party in the case of merger, reorganization, or change of legal residence.

It would seem that the wording in this draft provision permits stoppage in transit in line with current practice. Thus, Fei Ning expected that this right will be recognized by Chinese law and might even be promulgated in Chinese statutes in future.<sup>58</sup>

## **4.2 What happens when an unpaid seller stops the goods from being delivered to the buyer and during that time, the goods become damaged or are lost**

Consider the situation where the seller, upon discovering that the buyer has become bankrupt or insolvent, exercises the right of stoppage and repossesses the goods in transit. After doing so, the ship sinks and the goods are lost. In this case, which party has insurable interest and is entitled to recover compensation from the insurer?

### **4.2.1 English law**

Hodges wrote that "the buyer's interest, as it is contingent, is also defeasible. (...) The buyer's interest could be defeated or forfeited by the action of the seller. Even though his interest may be defeasible, at the option

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<sup>58</sup> *Ibid*, 292

of the unpaid seller, this does not prevent him from insuring his interest.” This is because the seller’s priority in a case involving stoppage in transit is “the reversion of his interest than with the loss of his interest.”<sup>59</sup>

Stoppage in transit causes the seller to resume his interest in the goods. However, this is also true when a buyer rejects the goods. They are, of course resumptions of different natures having been caused by different reasons. Hodges considered the problem that arises in such cases and remarked that “in each case, the major difficulty is not whether there is an interest but where the interest lies (in the buyer or the seller) at the time of the loss.”<sup>60</sup>

Carr and Stone wrote that the problem can be solved by asking the question of who was holding the title either by way of document of title or other equivalent proof at the time of loss.<sup>61</sup> An unpaid seller who retains the title is usually presumed to reserve his right of disposal. The buyer could, however, rebut this presumption.

Who has the title depends on sale of goods contract terms.

**a) CIF:**

Carr and Stone stated that it is highly unlikely that a CIF seller does not retain title of the goods against payment. As has been established in the previous chapter, retention of title usually indicates insurable interest regardless of passage of risk. Thus, in a vast majority of CIF contracts in situations of stoppage of transit, the seller would have insurable interest over the goods.

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<sup>59</sup> Susan Hodges, *law of marine insurance*, Cavendish Publishing Limited, 1996, 17

<sup>60</sup> *Ibid*, 17

<sup>61</sup> Indira Carr, Peter Stone, *International trade law*, 2005, 26

**b) FOB:**

Even though property and document of title usually passes at the ship's rail in FOB contracts, the likelihood that the seller would reserve the right of disposal means that in most FOB cases, the seller would retain title. However, an FOB buyer could contest this presumption and if he succeeds, title would vest in him thereby giving him entitlement to insurable interest after stoppage in transit has taken place.

**4.2.2 Chinese law**

Since the law states that sellers who still have title of ownership can practice stoppage, when the stoppage happens, it must mean that the seller is the owner of the goods. Based on Chinese courts' position that only owners can have insurable interest, it means that the seller has insurable interest at the time the stoppage occurred.

As discussed above, stoppage in transit can only be exercised by the seller if he has the ownership of the goods during the carriage of goods. So, whether the seller has the ownership becomes a point that could decide whether seller can have the right of stoppage in transit. However, no applicable law or legislation expresses the ownership of goods during international carriage of goods, unless there is provision that indicates the issue in the contract between the buyer and seller. Thus if there is no agreement on ownership of property, does it mean that stoppage in transit can not be exercised? Jiangli wrote that the only applicable legislation to handle same situation could be found in Article 308 of Contract Law of the PRC, which states that

prior to carrier's delivery of the cargoes to the consignee, the consignor may request the carrier to suspend the carriage, return the cargoes, change the destination or deliver the cargoes to another consignee, but it shall compensate



the carrier for any losses thus caused.<sup>62</sup>

However, the right indicated here is different from the stoppage in transit under English law. There are four conditions that must be fulfilled before the right of stoppage can be exercised namely: The buyer has failed to pay the price (only an unpaid seller can exercise this right); the buyer has become insolvent; the seller has parted with the possession of the goods; and the goods must be in transit<sup>63</sup>. There are no details on the requirements of the consignor's right in the Contract Law of the PRC and there is no clear expression on whether this right can be exercised by the seller (consignor) at any time as long as the seller still has the ownership of the goods. Since the right to exercise stoppage in transit involves the carrier's rights as discussed above, whether the seller can give instructions to the carrier is another issue here under a different legal system. There is no clear definition on stoppage in transit in Chinese law.

If one were to apply the GPCL to protect the seller's right once the buyer has failed to pay for the goods and the buyer has become insolvent, it would seem that the task of defining insurable interest becomes much easier. It has already been discussed that the definition of insurable interest in Chinese law follows a legalistic approach. As such, only the seller who has ownership can have the right of stoppage in transit. Obviously, after stoppage happens, the seller still has insurable interest.

However, it is unfair for the seller that the right as indicated by the GPCL is applied to international carriage of goods. Firstly, how one defines the passing of property becomes an issue under international carriage of goods if there is no agreement on passing of property between the seller and the buyer. It must be noted that the seller bears the burden of proof. Secondly,

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<sup>62</sup> *Contract Law of the People's Republic of China*

<sup>63</sup> *Caslav Pejovic, stoppage in transit and right of control, conflict rules? Pace International Law Review, Spring 2008 Tulane Maritime Law Journal*

once the buyer has become insolvent, the liquidator would most probably take over the buyer's company. What happens then to the ranking of the seller among parties claiming payment from the buyer? Since as a seller *per se*, he usually would not have priority in ranking, how would the seller claim unpaid monies from the buyer? More importantly, if the seller no longer has ownership over the goods, he or she also has no insurable interest over the subject-matter insured. Thus, in such situations, the seller is also unable to recover from the insurers. For these reasons, the right of stoppage in transit under English common law should be adopted and applied by the Chinese legal regime.

Although Chinese law has her own disadvantages in this area compared with English law, the latter is not free from unresolved issues either as there are outstanding issues under English law on stoppage in transit and the definition of insurable interest.

As discussed in chapter 3, under English law, the reform of definition on insurable interest resulted in a relaxation of the requirement of "legal relationship." The pecuniary interest approach has seen much development and is replacing the legalistic approach. So, the significant feature of the current law is the recognition that an assured with a specific or particular interest in an insured subject-matter may insure beyond his own particular interest to the full insurable value of the subject-matter.

Firstly, the statutory categories of insurable interest in the MIA 1906 provide a limited list when an insurable interest does or may exist, as follows:<sup>64</sup>

- 1) ownership
- 2) charters
- 3) mortgages

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<sup>64</sup> *NJJ Gaskell, C Debattista and RJ Swatton, Chorley and Giles's shipping law, Person, P511- 514*

- 4) trustees
- 5) the adventure
- 6) creditors
- 7) lien holder
- 8) buyer of goods

When the right of stoppage in transit is exercised by the seller, the relationship to the subject-matter is changed. Under FOB terms, after the goods pass the rail, the buyer takes over the risk, in which case he definitely has insurable interest. If the seller exercises the right of stoppage in transit after the buyer bears the risk, according to the concept of stoppage in transit, the seller now has possession of goods instead of the ownership of goods. The issue arises as to whether it can be said that the seller now holds the goods under lien? If so, the seller as a lien holder has insurable interest. At the same time, buyer who has ownership or bears risk in relation to the goods has insurable interest as well. Is there then a conflict of interest between the two parties? In this case, both parties can have insurable interest to the same subject-matter insured. Therefore, there is no conflict as such. However, the problem of apportioning percentages of indemnity to the seller and buyer once loss happens is another matter altogether. There appears to be no provisions which can be applied here to deal with the issue.

Secondly, whether the bearing of risk could be changed after stoppage in transit is another question since insurable interest is related to adventure as mentioned above. Under FOB and CIF terms, risk is borne by the buyer after the goods have passed the rail of the ship. However, the right to stoppage in transit is exercised by the seller during transit and instruction is given by the seller to the carrier to withhold delivery to the buyer. So, if the stoppage in transit is imposed by the seller after the goods have passed the rail, the risk in relation to the goods should be borne by the seller. In other words, can we now say that insurable interest in relation to adventure has reverted to the seller? No provisions seem to offer any explanation that could clarify this matter. Stoppage in transit is a right which protects unpaid

sellers. After exercising stoppage, the seller could have resold the goods. Undoubtedly, sellers and buyers under international trade should be made to bear their respective responsibilities in a fair manner. Thus, when the seller is accorded the right to repossess goods sold and the right to give instructions to the carrier to withhold delivery of the goods, it is the writer's opinion that he should also be made to take over the risks in relation to the goods.

If such is the case, it follows that the seller also has insurable interest as to the subject-matter insured having exercised his right of stoppage of transit.

## 5 Conclusion

Insurable interest is a very important principle as it is only with an insurable interest in the subject-matter of the insurance that an assured may recover from the insurer. This principle has been established in order to prevent insurance from being used as a cloak for wagering. Approaches of definition of insurable interest developed hand-in-hand with international trade. Current trends show that the strict approach towards insurable interest is being replaced by the more liberal approach.

As discussed, definition of insurable interest is not expressed clearly in the maritime law regime of the PRC. Although Chinese contract law can be applied when there is *lacuna*, it is difficult to place boundaries on international carriage of goods. The issue of defining insurable interest of sellers and buyers under contracts terms of FOB, CFR and CIF generates a lot of discussions among the legal scholars of China. Admittedly, the codifying of Chinese maritime law is influenced by common law. However, only the legalistic approach of insurable interest originating from the common law is adopted by the Chinese legal framework.

Obviously, the Chinese courts' strict approach on insurable interest could have unjust effects on non-owners of goods who may have interests in the goods in question. Additionally, transfer of ownership and property during international carriage of goods is not addressed in Chinese Civil Law. The Incoterms 2000 which could be applied does not amount to transfer of property. These disadvantages under the Chinese legal regime, in this case, create more hurdles in defining insurable interest with regard to carriage of goods. Along with China's entry to the WTO, a review of this position has been in order.

Even though the liberal approach (pecuniary interest approach), which keeps in tandem with the modern market, has been accepted by English law, it has

disadvantages as well. As stated earlier, container shipment is quickly gaining popularity all over the world and is widely used during international carriage. Thus, from the time the goods part with the seller to the time they are delivered to the carrier is extended. The definition of insurable interest during this period of time under FOB is problematic.

When one comes to stoppage in transit, the issues of defining insurable interest and how to claim indemnity for sellers and buyers under policies become more complex. Firstly, in Chinese law there are no provisions on stoppage in transit. This puts the seller in a disadvantageous situation should the buyer become insolvent. Even though the simple and strict approach (legalistic approach) can be used to draw clear boundaries, it is still unclear in Chinese law regarding whether the seller or the buyer has insurable interest when loss occurs after the seller has exercised the right of stoppage in transit.

There is a separate provision on stoppage in transit under English law. However, whether seller could have insurable interest again after the right of stoppage is exercised and whether the seller should bear the risk of loss after henceforth are unclear. Even if the seller and buyer both have insurable interest to the same subject-matter insured at same time, there is still the problem of delimitation of the percentages of indemnity shared by the seller and buyer.

Evidently, insurable interest after the exercise of the right of stoppage in transit lies in a gray area of marine insurance law. Considering the high probability of incidents that may lead to this conundrum, it is crucial that current statutes are amended to reflect a clearer legal position on this issue.

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