NEWSSTAND

UK Insurance Contract Law Reform: Draft Consumer Insurance (Disclosure and Representations) Bill

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In our December 2009 issue of *Insurance and Reinsurance Review* we reported on the contents of the draft Consumer Insurance (Disclosure and Representations) Bill as previewed by the Law Commissioner, David Hertzell, at a discussion before the British Insurance Law Association on 16 October 2009. On 15 December 2009, the English and Scottish Law Commissions published their draft Bill and we can now review their proposals in detail.

The draft Bill applies only to consumer insurance contracts, ie contracts of insurance bought by individuals for purposes wholly or mainly unrelated to their trade, business or profession. It also only deals with the issue of what a consumer must tell an insurer before entering into or varying an insurance contract.

The Insured's Duty to Take Care Responding to Questions
The current law requires a consumer to volunteer information about anything which a "prudent insurer" would consider relevant. The Law Commission believes this no longer corresponds to the realities of a modern mass consumer insurance market. Most consumers are unaware that they are under a duty to volunteer information. Even if they are aware of it, they usually have little idea of what an insurer might think relevant the Law Commission has stated that it is clearly important that insurers receive the information they need to assess risks. Most insurers, however, now accept that they should ask questions about the things they want to know.

The draft Bill abolishes the duty currently imposed on consumers to volunteer material facts and replaces it with a duty to take reasonable care to answer the insurer's questions fully and accurately. Where a consumer does make a mistake on an application form, the insurer is entitled to avoid the policy entirely, as if it never existed, only in certain circumstances dependant on the consumer's state of mind.

The draft Bill distinguishes between mistakes which are "reasonable", "careless" and "deliberate or reckless":

- Where a misrepresentation is honest and reasonable, the insurer must pay the claim. The applicant is expected to exercise the standard of care of a reasonable consumer, bearing in mind a range of factors, such as the type of policy and the clarity of the question. The test does not take into account the individual's own subjective circumstances (such as knowledge of English), unless these were, or ought to have been, known by the insurer.

- Where a misrepresentation is careless, the insurer has a compensatory remedy. This is based on what the insurer would have done had the consumer taken care to answer the question accurately and completely. For example, if the insurer would have added an exclusion, the insurer need not pay claims which fall within the exclusion, but must pay all other claims. If the insurer would have charged more, it must pay a proportion of the claim.
- Where the misrepresentation is deliberate or reckless, the insurer may avoid the policy. The insurer would also be entitled to retain the premium, unless there was a good reason why the premium should be returned.

For a misrepresentation to be considered "deliberate or reckless", the insurer must show on the balance of probabilities that the consumer knew the following:

- that the statement was untrue or misleading, or did not care whether it was or not
- that the matter was relevant to the insurer, or did not care whether it was or not.

However, if a reasonable person would have known that the statement was untrue, the burden of proof would fall on the consumer to show that he or she had less than normal knowledge. Similarly, if the question was clear, it would be up to the consumer to show why he or she did not think the matter was relevant.

The Law Commission believes that these new requirements reflect the approach already taken by the Financial Ombudsman Service (FOS) and are generally accepted as good practice within the industry. It believes that the proposed reforms would, however, make the law simpler and clearer, allowing both insurer and insured to know their rights and obligations. Insurers would therefore be less likely to turn down claims unfairly, and consumers would have greater confidence in the insurance industry.

Intermediaries

The Law Commission has tackled the controversial issue of intermediaries and who they act for in consumer insurance. It has recommended a statutory code, based largely on the existing law, as supplemented by FOS practice and industry understanding. The aim of the proposals is to give greater guidance, while retaining flexibility for the FOS and the courts to adapt to new arrangements.

The draft Bill states that an intermediary is considered to act for the insurer if:

- the intermediary is the appointed representative of the insurer
- the insurer has given the intermediary express authority to collect the information as its agent
- the insurer has given the intermediary express authority to enter into the contract on the insurer's behalf.

In other cases, the intermediary is presumed to act for the consumer unless it appears that it acts for the insurer. Schedule 2 to the draft Bill sets out factors which tend to show whether the agent is acting for either the insurer or the insured.

Examples of factors which may tend to confirm that the agent is acting for the consumer are:

- the agent undertakes to give impartial advice to the consumer
- the agent undertakes to conduct a fair analysis of the market
- the consumer pays the agent a fee.

Examples of factors which may tend to show that the agent is acting for the insurer are:

- the agent places insurance with only a small proportion of the insurers who provide insurance of the type in question
- the insurer provides the relevant insurance through only a limited number of agents
- the insurer permits the agent to use the insurer's name in providing the agent's services
- the insurance in question is marketed under the name of the agent;
- the insurer asks the agent to solicit the consumer's custom.

The Law Commission was conscious that in some transactions, it is common for intermediaries to "*change hats*" during the transaction, acting for the consumer in advising on the choice of insurer, and acting for the insurer in binding it to cover. The focus is on the intermediary's capacity at the time of the action in question. In addition, it states that this list of factors is "*indicative and non-exhaustive*" and that flexibility is key.

Basis of the Contract Clauses
The draft Bill abolishes "basis of the contract" clauses by stating that any representation made by a consumer is not capable of being converted into a warranty by means of any provision of the contract. The draft Bill, however, does not abolish warranties and is remains possible for insurers to include specific warranties within their policies.

Group Schemes
The draft Bill makes special provisions for group schemes providing that where a misrepresentation is made by a group member there are only consequences for that individual rather than the whole group.

Life Insurance Policies
Where one person takes out insurance on the life of another person and that individual (who is not a party to the contract) makes a misrepresentation (such as regarding their age or health) the Bill imposes the same duties upon the person whose life is insured as upon the policyholder. Where the individual makes a misrepresentation the insurer will be entitled to the same remedies as had they been a party to the contract.

No Contracting Out
The draft Bill prevents insurers from contracting out of the changes to the detriment of consumers.

Comment
There is wide consensus that consumer insurance law is in urgent need of reform and so it is

likely that the draft Bill will be passed in time. However, in light of the impending General Election, it is unlikely that anything further will happen until Autumn of this year.