**Written Evidence on the Insurance Bill, 27 November 2014**

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We congratulate all those involved on getting the Bill thus far and hope for successful enactment. At the same time, we wish to take this opportunity to express our summary criticisms in the briefest possible terms, in the hopes that they may be of assistance.

**The duty of fair presentation**

1. We understood the policy objective as being a general clarification of and, if any change is intended, a reduction in the scope of the proposer’s duty of disclosure, to harmonise with the trend in (if not the terms of) consumer insurance. We did not think that the proposal fully met these ambitions and thought that it would be useful to set out a few of our question marks for your consideration.
2. The Bill provides for a very high standard of disclosure for two reasons. First, the expression “prudent insurer” represents an objective standard and is therefore understood to mean an ideal insurer with consistent and high standards, not affected by the vicissitudes of human nature. In fact, the judicial dicta on the concept are to the effect that it is open to interpretation, for example: “[T]his is an objective test, and the characteristics to be imputed to a prudent insurer are in substance a matter for the courts to decide.” [[2]](#footnote-2) Second, since the duty of fair presentation is on the insured, the burden of proof will be on the insured to prove that it has lived up to that high standard, if that fact is questioned by the insurer. The insured must do so by providing market evidence, that is, evidence by other underwriters. The insured must thus find an unrelated but sufficiently initiated underwriter who is willing, in effect, to testify against its own interests in the market. We felt that for these two reasons, the burden of proof was too demanding on the insured to fulfil and that the effect was too high a standard of disclosure.
3. By virtue of section 8 of the Bill and the Schedule attached thereto, ‘deliberate or reckless’ breaches of the duty of presentation lead to the remedy of avoidance, and other breaches lead to a proportionate remedy. It is assumed that the language of ‘deliberate or reckless’ is employed in place of ‘fraudulent’ as a means of avoiding any enhanced standard of proof. While we do not approve of any enhanced standard of proof in this context, we also noted that this again works to the advantage of the insurer who can now more easily demonstrate relevant facts on the balance of probabilities than if the standard of proof were to remain that for fraud.
4. Overall, the proposals shift the duty to disclose considerably in the favour of the insurer (eg the prevention of ‘over disclosure’ aka data dumping) for technical reasons not readily apparent from the statute itself and we thought such factors worth looking at before finalising the legislation. This is in contrast to the changes to the remedial scale, which is now proportionate by design.

**Warranties**

1. Our overall impression is that these sections seek to deal with the immediate rather than the root causes of the problems with ‘insurance warranties’. We see little in sections 9 and 10 that would prevent an insurer from recasting a promise currently made as a warranty as a ‘condition precedent’ to liability. If that is meant to ensure understanding by the insured as to the nature of the promise, then we have doubts as to the likely efficacy of these provisions.
2. We also have difficulty seeing that the commercial market justified wholesale reform of this type. We would have preferred targeted reforms intended to improve the clarity of remedies for breach, but retaining commercial freedom as to the ultimate remedy.
3. Section 10 of the Bill reads as a mandatory reclassification of the ‘insurance warranty’. The rule in section 33 of the Marine Insurance Act 1906 and *The Good Luck[[3]](#footnote-3)* is replaced by a complex form of combined temporal and causative exception. Cover is suspended during periods of non-compliance and for losses that occur later which are attributable to such non-compliance. In effect, this is broadly equivalent to the standard ‘navigation warranties’ in force in the marine market. What this shows is that some insurers were able to define their risk management terms in line with section 10 in the past (and indeed go further and allow for ‘held covered’ extensions), but others have preferred to insist on the stricter warranty.
4. It is not clear from section 10 that insurers could not simply state that compliance was a ‘condition precedent’ to continuing cover. Unless more was stated, this would weaken the insured’s position as technically it would now be for the insured to prove compliance and not the insurer’s responsibility to prove breach (as is the current position under warranties).
5. We have been highly critical of the default remedy in section 33 of the Marine Insurance Act. There are two criticisms that are not dealt with by the new statutory formulation (despite its substantial interference in the market): long-standing, trivial breach; and the provision of a single ‘one size fits all’ default.
6. The remedy for breach remains the simple ‘on/off’ switch. The circumstances in which liability is removed are constrained, but there is no proportionality. So, an ongoing trivial breach of a warranty would discharge liability. This approach to insurance contract promises is the result of historical accident rather than clear choice. Insurance law cannot, apparently, create a common law ‘innominate term’ but ought to consider a statutory version (at least as one option).
7. It may be that ‘waiver’ is meant to assist insureds here, but that depends on the insurer being aware of the breach and communicating permission sufficiently clearly to found an estoppel. In any event, we thought that clarification as to the triggering of the remedy would be useful for the purpose of understanding ‘waiver’. Section 9(1) abolishes the current remedy. That remedy is triggered automatically by the breach.[[4]](#footnote-4) As a result of the lack of opportunity to elect, waiver is by equitable estoppel. If the existing remedy is “abolished”, will the remedy that replaces it also be automatic or will there be an element of election? Given that the form of waiver available to the insurer and the elements to be proven depend on this question, it should perhaps have an explicit answer.[[5]](#footnote-5)
8. We would prefer to see consideration of a tailored series of defaults, with at least some having a reduction in the level of cover awarded, rather than a simple on-off remedy. We would then leave it to the market to decide which it favoured in each situation. We think it is beyond the ability of lawmakers to shape a single default which works efficiently given the breadth of commercial insurance contracts. We would, at least like to see some explanation of what this default is meant to achieve: is it to be routinely followed, or is to force underwriters to make explicit what is currently implicit in risk management terms? The development of more than one statutory form would require us to identify labels for these varying provisions, but would enable parties to be clear as to the intended effect of non-compliance. Law could recognise for example a ‘section 33’-style strict clause, and a whole range of less strict clauses. This, after all, is the basis of much of commercial contract law outside of insurance. Provisions with statutory force acquire (quite naturally) greater judicial attention and outcome certainty; and this (with other factors) will focus attention on them whatever the merits of the clause in the contractual situation under negotiation.

**Fraudulent claims**

1. We took the policy objective against which the proposals should be assessed to be the reduction in fraudulent claims and encouraging honesty in the claims process.
2. We felt that the proposals were good in their minimalism, but that they represented an excessive swing of the pendulum in favour of the insurer and might benefit from tempering.
3. The proposals leave intact the meaning of ‘fraudulent claim’ by not providing a definition. We believe that the definition of fraudulent claims is not currently unclear or problematic, at least not to an extent where it cannot be handled by the courts, and that therefore this is a good solution. Nonetheless it is worth noting that the assumption that the courts will continue to develop the definition of ‘fraudulent claim’ to fit the remedy as drafted relies on the courts recognising that section 11 is not establishing a statutory codification of the appropriate default for minor exaggerated claims and fraudulent devices. Also, codifying the remedy but not defining the circumstances to which it attaches risks the courts having to ‘reverse engineer’ a rule to fit. The difficulties that this can cause are evident from the ‘avoidance’ rule found in section 17 of the Marine Insurance Act 1906 and elsewhere.
4. Furthermore, there is a problem of overall imbalance. The scope of the definition of fraudulent claims has in recent years been increased to encompass also entirely honest claims promoted by fraudulent means and devices. This was described by Lord Mance as ‘deliberately designed to operate in a draconian and deterrent fashion’.[[6]](#footnote-6) The recent judicial discussion of subjective intent is unlikely to represent a major shift.[[7]](#footnote-7) Even though the judgment of Popplewell J in the *DC Merwestone*[[8]](#footnote-8) expressed considerable concern that the forfeiture rule overly favoured underwriters, even to the extent that it may breach the Human Rights Act, the Court of Appeal disagreed. It would be unfortunate to codify the rule just as it is under critical consideration by the highest court in the land.[[9]](#footnote-9)
5. It was already the case that an exaggeration made for the purpose of negotiation was not a fraudulent claim. The law has therefore for some years been subtly shifting in favour of the insurer – this is consistent with the policy aims, but care must be taken that the shift does not go too far when statutory form is considered, and the equilibrium needs to be considered in the context of the global reforms.
6. We noted that the termination remedy under section 11 of the bill represented the option harshest on the insured. Termination by notice with retrospective effect from the date of the fraudulent act is a more onerous remedy for the insured than other potential termination remedies, such as notice of prospective termination following a stipulated notice period or termination with immediate effect from receipt of notice. The remedy is in reality an election to terminate with retrospective effect and would affect subsequent honest claims made in reliance upon notice not being given and the insurance remaining in place. This would affect the position of a generally honest insured who had lapsed into a fraudulent claim but had made several honest claims before and afterwards, and who would have had the opportunity to take out a policy elsewhere but relied on the policy to remain in place.
7. It should be noted that the forfeiture rule is already designed to be punitive.[[10]](#footnote-10) If it is now accepted that avoidance is not an available remedy for fraudulent claims, out of the potential termination options, the one opted for by the Law Commissions is the harshest one. We therefore felt that from a more global overview perspective, it would be good to temper the proposals slightly in favour of the honest or not-so-dishonest insured.
8. We thought that the judicial discretion rule embraced by section 56 of the Australian Insurance Contracts Act 1984 would be appropriate also in our jurisdiction, especially in relation to entirely honest claims following a mostly genuine claim tainted by “slight” fraud and taking into account the exaggeration or other dishonesty in proportion to the total claim. This was considered especially appropriate in view of the relative harshness of the retroactive effect of termination in section 11(2)(a). Section 56 created a statutory discretion in the event of a fraudulent claim. Should the Supreme Court in the *DC Merwestone* find that the ‘draconian’ forfeiture rule is bad law, section 56 could provide a useful model for statutory reform. It seems much more likely that a statutory discretion would be created than a judicial one (as the case law in common mistake etc, makes clear). Judicial remodelling of the law is much more likely to impose familiar common law restrictions such as ‘materiality’ and ‘inducement’.

**Good faith**

1. Part 5 is designed to remove the remedy of avoidance for breaches of the duty of utmost good faith. It addresses solely the remedy and does not purport to affect the contents of any doctrine of good faith. We consider this a minimalistic incision with potential for a successful outcome for insurance law, in particular in view of dicta in *The Star Sea* and *Goshawk v Tyser*.[[11]](#footnote-11)
2. However, we have considered the implications on the amendments on the Marine Insurance Act 1906. Following the amendments, section 17 of the MIA 1906 will be situated directly underneath the header “Disclosure and representations” and immediately followed by section 21, “When contract is deemed to be concluded”. This new geography may influence its interpretation and cause an unintended construction in the context of marine insurance so that any application of the provision in a post-contractual context is put in question.
3. Finally, it appears clear from the consultation process preceding the introduction of the Bill that the Law Commission would like good faith (or utmost good faith, which we do not consider to be anything different) to remain as a guiding principle. That being the case, we would recommend including a provision to that effect in the new Act. The principle currently only appears in section 17 of the Marine Insurance Act 1906 and in its wording makes direct reference to marine insurance, so that it could feasibly be inferred in the interpretation of new legislation applicable to insurance in general that it did not apply to other forms of insurance.

**Late payment**

We would like to express our regret that the issue of remedies available to the assured in the event of late payment of the claim by the insurer has not been addressed in the Bill.

1. \* Mateusz Bek, Professor James Davey, Johanna Hjalmarsson and Katie Richards. [↑](#footnote-ref-1)
2. *Norwich Union Insurance Ltd v Meisels* [2006] EWHC 2811 (Tugendhat J). [↑](#footnote-ref-2)
3. [1991] 2 Lloyd’s Rep 191. [↑](#footnote-ref-3)
4. *The Good Luck* [1991] 2 Lloyd’s Rep 191. [↑](#footnote-ref-4)
5. *Argo Systems FZE v Liberty Insurance (PTE)* [2012] 1 Lloyd’s Rep 129. [↑](#footnote-ref-5)
6. *Axa General Insurance Ltd* v *Gottlieb* [2005] 1 C.L.C. 62, [31]. [↑](#footnote-ref-6)
7. Both *Aviva Insurance Ltd v Brown* [2012] Lloyd's Rep IR 211 and *Versloot Dredging BV v HDI-Gerling Industrie Versicherung AG (The “DC Merwestone”)* [2013] Lloyd's Rep. IR 582, [2014] EWCA Civ 1349 (subject to the appeal to the Supreme Court) were decided in favour of the insurer. [↑](#footnote-ref-7)
8. *Versloot Dredging BV* v *HDI Gerling Industrie Versicherung AG, The DC Merwestone* [2013] EWHC 1666 (Comm). *The DC Merwestone* [2014] EWCA Civ 1349. [↑](#footnote-ref-8)
9. The codification of a rule just before its reversal by the highest court occurred when the Marine Insurance Act 1906 incorporated the rule in *Angel* v *Merchants' Marine Insurance Co* [1903] 1 K.B. 811. See FD Rose ‘Restating Insurance Contract Law: Centennial Reflections on Landmark Reform’ [2006] LMCLQ 458, 473. [↑](#footnote-ref-9)
10. “The fraudulent insured must not be allowed to think: if the fraud is successful, then I will gain; if it is unsuccessful, I will lose nothing”; Lord Hobhouse in *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] UKHL 1; [2001] 1 Lloyd's Rep. 389 at [62]. [↑](#footnote-ref-10)
11. Lord Hobhouse in *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] UKHL 1; [2001] 1 Lloyd's Rep. 389 at [52]-[53] and *Goshawk Dedicated Ltd v Tyser & Co Ltd* [2006] EWCA Civ 54 at [53]. [↑](#footnote-ref-11)