

Insurance Contract Law Reforms

22 June 2011

LATEST DEVELOPMENTS

The Consumer Insurance (Disclosure and Representations) Bill has had its second reading in the House of Lords.

THE BILL

1. General Principles

The Bill, if implemented, will abolish the consumer's duty to volunteer material facts. The consumer will instead be required to take reasonable care in answering the insurer's questions both fully and accurately. In volunteering any information, the consumer must take reasonable care to ensure that it is not misleading.

Remedies for the insurer, where they have been induced to enter a contract by a misrepresentation, will then be dependent on the consumer's state of mind.

In general terms, if the misrepresentation is:

1. honest and reasonable, the insurer must pay the claim;
2. careless, the insurer will have a compensatory remedy based upon what it would have done had the consumer answered the question carefully; and
3. deliberate or reckless, the insurer may treat the policy as if it never existed and decline all claims.

The Bill also seeks to abolish "basis of contracts" clauses and establish a statutory code to determine for whom an intermediary (agent or broker) acts when arranging insurance.

2. Timetable

- Given that there has been extensive consultation and widespread support, this Bill has been deemed suitable to be considered under the procedure for Law Commission Bills. This process is intended to reduce the time that Law Commission Bills spend on the floor of the house by providing for certain stages to be carried out in Committee. This allows the Bill to be considered and scrutinised despite the pressures on Parliamentary time.
- The BBA have raised the issue of the timing of the implementation. The FSA is in the process of requiring implementation of its retail distribution review in December 2012. This Bill will involve to a certain degree the same systems, processes and people to be trained. Therefore, it has been recognised by the House of Lords that, if possible, it should be mindful of the burdens of implementation on the industry and that to implement all of the changes in one go would be advantageous. The

BBA also raised the issue of the interaction between the Bill and IMD2.

IMPLICATIONS

- In order to determine whether or not a consumer has taken care in providing the relevant information, it will be necessary for many proposal forms to be recast, with simpler and tighter questions.
- Whether or not a consumer is deemed to have taken reasonable care in answering the insurer's questions will be determined in light of all relevant circumstances (clause 3(1)). These include the type of contract in question, any relevant explanatory material produced by the insurer and how "clear" and "specific" the insurer's questions were.
- Given that insurers will no longer have the protection of the catch-all requirement that the consumer must provide everything that would be material to the insurer's decision to insure, it will be tempting to design proposal forms which are comprehensive and wide-ranging. This would create problems with either the length and complexity or the number of questions required to cover every eventuality. It has been suggested in the House of Lords that the ABI provide guidelines on this, particularly in considering whether the addition of catch-all questions such as: 'is there any other information that might be relevant' would be permissible. The FSA is likely to have strong views on the subject as regards retail sales.

COMMENT

The Bill shifts the balance from the consumer being required to volunteer information to one where the insurer is required to ask clear and specific questions. The Bill, however, does not provide a guide as to *what* questions the insurers should ask. Such guidance can instead be found in principle 6 of the FSA Principles for Business where a firm: "*must pay due regard to the interests of its customers and treat them fairly.*" There is also an obligation under the Insurance: Conduct of Business Sourcebook to ensure that customers know what they must disclose. Thus, there is a shift in the legal position, but it is designed to be a shift towards a position that is in line with industry best practice and the standards that are currently imposed by the Financial Ombudsman Service.

The FSA General Insurance Newsletter (June 2011) states:

"The current law has changed little since 1906, and, with additional layers of regulation, has become complex and confusing for consumers, and expensive for the industry to administer.

The changes within the Bill, and its shift in emphasis, will provide better protection for consumers, while reducing the cost to industry."

NEXT STEPS

The Special Public Bill Committee stage of the House of Lords review, which is a line by line examination of the Bill, is yet to be scheduled. Progress of the Bill can be followed at: <http://services.parliament.uk/bills/2010-11/consumerinsurancedisclosureandrepresentationshl.html>

FURTHER INFORMATION

Please contact the person with whom you usually deal or Christian Wells / Clare Douglas

Websites:

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