

Insurance Contract Law Reform: Disclosure and Representation in Consumer Insurance

December 2009

Summary

The Chartered Insurance Institute welcomes the Law Commissions' proposed changes to the law underpinning disclosure and representation of consumer insurance contracts. These changes are meant to update the old Marine Insurance Act 1906 and clarify the remedies insurers have available if customers misrepresent themselves when taking out an insurance policy.

- On 15 Dec 2009, the Law Commissions laid before Parliament a draft Bill that sets out more proportionate remedies insurers would be able to use depending on the nature of the misrepresentation. This follows a 2007 consultation and feedback statements since then.
- We believe these reforms represent a sensible way forward. By distinguishing deliberate misrepresentations from honest mistakes made by consumers at point of sale, the changes strike a sensible balance between protecting consumers with limited financial capability and protecting insurers from proportionate financial loss due to carelessness or even fraud.
- As a result of these changes, the underlying contract law will provide a modern and stable foundation on which higher standards of practitioner professional knowledge and ethical conduct can be built in the public interest.

Policy Background

The Law Commission of England & Wales and the Scottish Law Commission have been undertaking since 2007 a joint review of the law governing disclosure and representation in consumer insurance contracts.¹ This was meant to modernise the existing law and clarify the remedies insurers have available if customers misrepresent themselves (either disclose incorrect information or fail to disclose something materially important) when taking out an insurance policy:

- Underpinned by the old Marine Insurance Act 1906, the existing law allows insurers to refuse a claim if the policyholder made *any* misrepresentation, even if all questions *asked* were answered honestly or reasonably.
- This has resulted in numerous cases of consumers being denied expensive payouts on the basis of confusion over disclosure at point of sale years earlier. It has spurred some voluntary corrective action by the industry and landmark Ombudsman decisions, but there is still a lack of market-wide certainty.

On 15 Dec 2009, the Law Commissions jointly published their findings and laid the *Consumer Insurance (Disclosure and Representations) Bill* before Parliament.² It sets out "a duty of the consumer to take reasonable care not to make a misrepresentation to the insurer"³ and establishes a set of proportionate remedies insurers would be able to use (see their summary chart on the next page):

- **Deliberately or recklessly misleading:** insurers would only be able to withhold a full claim if they can prove the policyholder was knowingly misrepresenting information they knew was material to the contract.

¹ See for example, Law Commission and Scottish Law Commission, *Insurance Contract Law: Misrepresentation, Non-Disclosure and Breach of Warranty by the Insured*, a joint consultation paper, July 2007 <http://www.lawcom.gov.uk/docs/cp182.pdf>.

² Law Commission of England & Wales, "Consumer Insurance Law: Pre-Contract Disclosure and Misrepresentation," 15 Dec 2009 http://www.lawcom.gov.uk/insurance_contract.htm; and <http://www.scotlawcom.gov.uk/html/cpinsurance.php>

³ Law Commission and Scottish Law Commission, *Consumer Insurance Contract law: Pre-Contract Disclosure and Misrepresentation*, 15 Dec 2009 "Draft Consumer Insurance (Disclosure and Representations) Bill," clause 2(2). <http://www.lawcom.gov.uk/docs/lc319.pdf>

- **Honest and reasonable:** if the misrepresentation was deemed a reasonable mistake based on the type of insurance contract and the clarity of the insurer’s questioning, then the insurer would have to pay the claim.
- **Careless misrepresentation:** if the consumer “failed to take sufficient care to understand what the insurer wanted to know or to check the facts”,⁴ then the insurer would be able to apply a “compensatory remedy.” This would be based on what the insurer would have done had it known the correct information, such as applying relevant exclusions or the increased premium the insurer would have charged.

The Bill also proposes to amend the law of agency relationship between insurance intermediaries, insurers and policyholders (for the purposes of gathering information, not other aspects of the law of agency relationship). The intermediary would be presumed to be acting as an agent of the *customer* unless there is a contractual relationship with the insurer, such as the intermediary using a limited panel.

CII Group Position

The Chartered Insurance Institute welcomes these reforms. The existing law is over a hundred years old and does not reflect the realities and complexities of the twenty-first century consumer insurance market. We have responded to the Law Commissions’ consultation and support the changes as they have been submitted to Parliament.⁵

By distinguishing deliberate misrepresentations from honest mistakes made by consumers at point of sale, we believe the changes strike a sensible balance between protecting consumers with limited financial capability and protecting insurers from proportionate financial loss due to carelessness or even fraud.

If implemented into law correctly, these changes will result in:

- **greater clarity over the handling of claims by insurers:** thereby resulting in improved consumer confidence in the insurance industry;
- **promotion of industry best practices:** this would encourage more innovation in underwriting technology, exploring better use of techniques such as tele-underwriting; and
- **a more honest and trustworthy policyholder-insurer relationship:** consumers would have improved peace of mind that they could own up to honest mistakes without the risk of losing their insurance policy.

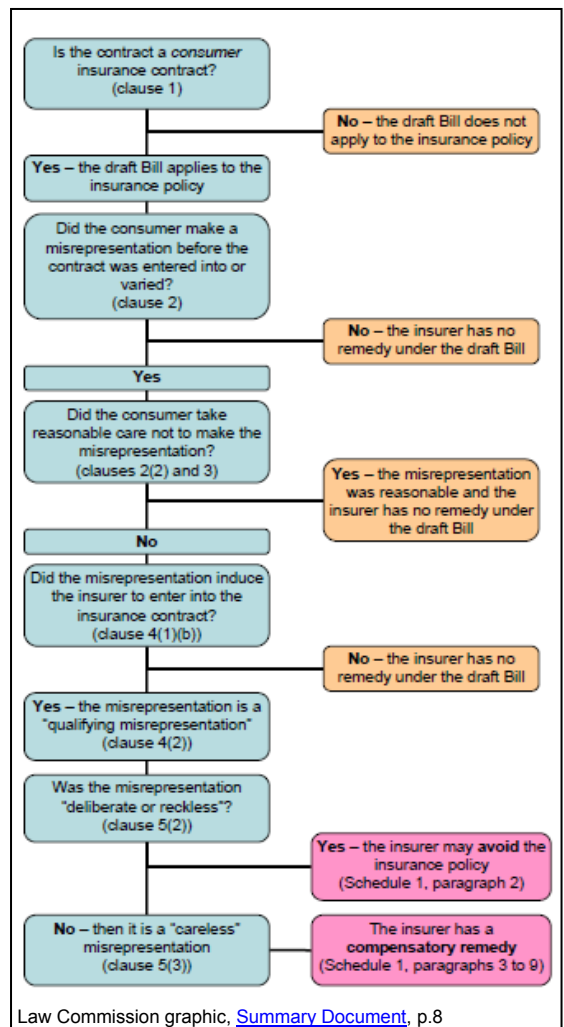
The law of agency reforms to clarify for whom the broker is acting for the purposes of information disclosure are also a sensible reflection of the current and planned market landscape. Following their 2007 consultation process, the Law Commissions’ have heeded our comments in this area and re-examined this. Their final proposal is now consistent with individual professional standards and conduct as well as wider regulatory developments.

All in all, as a result of these changes, the underlying contract law will provide a modern and stable foundation on which consumer-friendly innovation and higher standards of practitioner professional knowledge and ethical conduct can be built in the public interest.

The CII Group is the world’s leading professional organisation for insurance and financial services, with over 93,000 members in 150 countries. We are a not-for-profit body committed to maintaining the highest standards of technical expertise and ethical conduct in the profession through research, education and accreditation. Our Charter remit is to protect the public by guiding the profession.

For more information on the CII and its policy and public affairs function, including examples of the range of issues in financial services and insurance that we cover, please see: www.cii.co.uk/policy.

Please do not hesitate to contact: Laurence Baxter, Head of Policy and Research, tel 020 7417 4783; laurence.baxter@cii.co.uk



⁴ *Ibid.*, p.75, para.6.57. See also the draft bill’s Explanatory Note A.32 which refers to “a representation being careless if it is a breach of duty in clause 2(2) to take reasonable care, but is not deliberate or reckless.”

⁵ See Chartered Insurance Institute response to the Law Commissions’ consultation, Dec 2007 http://www.cii.co.uk/downloaddata/RDR_lawcommission.pdf