



Update on progress of the Insurance Bill

The Insurance Bill was introduced to Parliament in July 2014. As it is being debated some changes are now emerging. These include changes proposed by the Law Commission in December 2014 to the warranties provisions.

The Bill will significantly reform insurance contract law by amending some aspects which are currently perceived as being harsh on insureds. It will also amend the Third Parties (Rights against Insurers) Act 2010 to enable it to be brought into force. The plan is for the Bill to be finalised before the current Parliament ends in March 2015.

Background

The Bill is the culmination of an 8 year process which began in January 2006 when the Law Commission of England and Wales and the Scottish Law Commission began a joint review of insurance contract law. This resulted in a second report on insurance contract law which covered reform of the law of disclosure in business insurance, warranties, insurers' remedies for fraudulent claims and late payment of claims. Only the last of these recommendations has not been included in the Bill.

The government accepted the majority of the recommendations proposed by the Law Commission. The Bill was introduced on 17 July 2014 and in order to reduce the time it takes to come in to law is following the procedure for special uncontroversial Law Commission Bills. On 26 January 2015, the Second Reading Committee in the House of Commons agreed to support the Bill.

Proposed changes

The intention is to modify insurance law to bring it more in line with modern commercial practices and to reflect the diversity of the insurance market. The Bill also codifies the law to reflect case law since the Marine Insurance Act 1906 came into force over a hundred years ago.

The Bill updates the following 6 areas:

1. Duty of disclosure

The duty of disclosure in insurance law historically imposed a heavy duty on insureds to disclose all information that would be material to an insurer (even if the insurer did not ask for it) and allows an insurer to avoid all its obligations under a policy if

that duty is breached (even if innocently). This was perceived as harsh, particularly on consumers. Recent (separate) legislation removed the positive obligation to disclose on consumers, however, left the obligation of disclosure for business insureds unchanged.

The Bill now consequently addresses business insurance. For business insureds it replaces the duty of disclosure with an obligation to make a "fair presentation of the risk". This is defined as "every material circumstance" which the insured knows or ought to know (effectively the current test). If this level of disclosure is not met, the disclosure must at least provide sufficient information to put a prudent insurer on notice to make further enquiries for the purposes of revealing those material circumstances. The Bill provides examples of things that might be material.

The most important change contained in the Insurance Bill relating to disclosure is to the remedies for breach. If the breach is deliberate/reckless the insurer retains the right to avoid where it would not have entered the contract or only done so on different terms if proper disclosure had been made. If the breach was not deliberate or reckless the remedies are proportionate to the impact of the breach on the underwriting decision.

Although aimed at business insurance buyers, these changes will be welcomed by brokers who can face claims from insured clients when underwriters reject claims for failure to provide adequate disclosure.

2. Warranties

Currently a breach of warranty in an insurance policy discharges the insurer from further liability from the point of breach (even if remedied before any loss and even if the breach was unrelated to the loss). This remedy, perceived to be draconian by many, is abolished by the Bill.

The Bill proposes that an insurer has no liability in respect of any loss occurring or attributable to something happening after a warranty has been breached, but before the breach has been remedied. This means that breach of a warranty results in suspension rather than a discharge of the insurer's liability so that if the breach is remedied before the loss, then it has no impact on the insurance.

Another welcomed change is the abolition of “basis of the contract” clauses (already precluded in consumer insurance) which have the effect of converting every statement in a proposal form into a warranty with the consequence that even non-material and innocent misrepresentations give insurers the right to avoid the policy.

The Law Commission had also proposed that insurers should not be discharged from liability where the breach is unrelated to the loss. The original proposal in this regard was omitted when the Bill was introduced to Parliament in July 2014. A revised clause has now been produced and included in the Bill. The new clause will only apply to terms which reduce the risk of (a) loss of a particular kind (b) loss at a particular location or (c) loss at a particular time. If loss occurs, the insurer will not be able to rely on non-compliance with the term if the insured shows that the non-compliance could not have increased the risk of the loss. The clause therefore introduces a causal requirement between breach and loss and is a significant change to the current law.

3. Fraudulent claims

The Bill is seeking to provide clarification on this area as well. The Bill provides that when an insured submits a fraudulent claim:

- the insurer is not liable to pay that claim;
- the insurer may recover from the insured any sums paid in respect of the claim; and
- there is the option to treat the contract as terminated with effect from the time of the fraudulent act. This would give the insurer the right to terminate the insurance such that losses suffered after the fraud need not be paid whereas losses before the fraud will be.

4. Good faith

The Bill abolishes the current right to avoid a policy on the grounds that the utmost good faith duty has not been observed by the other party. However, the duty itself remains.

5. Contracting out

For non-consumer insurance contracts, the Bill provides parties with the ability to agree their own rules and “contract out” of the default statutory provisions. The only exception to this is in respect of basis of contract clause. However, where the insurer wishes to include a contractual term which puts the insured in a worse position than the Act would provide, then this must be drawn to the attention of the insured and the term must be clear and unambiguous as to its effect.

6. Third Parties

The Bill also provides a valuable opportunity to correct problems identified in the Third Parties (Rights against Insurers) Act 2010 in order for the Act to come into force to replace the current legislation from 1930.

The 2010 Act is required in order to simplify the process for third parties to allow them to bring a claim directly against the insurer.

In essence, the amendments add insolvency procedures through which an insured may qualify as a “Relevant Person” under the Act. It is hoped that this amendment will allow the Act to be brought into force later this year.

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