2015 Insurance Act

On 12th August 2016 the Insurance Act 2015 came into force and is designed to bring the statutory framework into line with the best practice in today's UK insurance market.

The Act fundamentally changes the way both commercial and consumer insurance and reinsurance contracts operate in the UK. The Act has been developed to rebalance the rights and remedies between you as the insured and your insurer, meaning that it is more likely for claims to be paid in full.

There are 3 particular issues and this document provides a summary of these and our comments:

Duty of Fair Presentation
Remedies for breach of the Duty of Fair Presentation
Warranties and other terms

As this is new legislation, the Courts will be the ultimate judge of how the Act will be interpreted and therefore this note is intended to provide guidance as to how we perceive you may realise the benefits and take measures to avoid the pitfalls.

Duty of Fair Presentation

The rules governing what information must disclosed to your insurers before the insurance policy is taken out have changed.

This new requirement is called the 'Duty of Fair Presentation' and is designed to be more structured than the current duty to disclose all material information.

Whilst the new requirement possibly increases the scope of the obligations that are imposed upon you, it extends the remedies you have against the insurers.

How to Comply

To comply with the 'Duty of Fair Presentation' you must disclose every material circumstance which you as the insured knows or ought to know. This can include disclosing the limits of the information you are able to provide.

Failing that, you must disclose any details which gives the insurer sufficient information to put a prudent insurer on notice that it needs to make further enquiries for the purposes of revealing those material circumstance.

What is a 'Material Circumstance'?

The new definition for what is a material circumstance is largely the same. Information will be material if it would influence the judgement of a prudent insurer in determining whether to take the risk and, if so, on what terms.

What am I deemed to know or ought to know?

The assessment for what material circumstances you are deemed to know, and therefore disclose, is broader than it is currently in that you are deemed to know the following:

a) What is known to the individuals who are part of your "senior management"

b) What is known to the individuals responsible for your insurance for example, your insurance manager and/or Estate Insurance Group?

c) What should reasonably have been revealed by a reasonable search of information available to the Insured, including information which is "held within the insured's organisation or by any other person".

Who are your 'Senior Management'?

The Act does not identify who your "senior management" are beyond saying they are individuals who play significant roles in the making of decisions about how your activities are to be managed or organised.

We will endeavour to agree with your insurers who your "senior management" are and to assist us, we will require you to provide information on your management structure, identifying those people who make decisions throughout your organisation.

What is a 'reasonable search'?

In order to discover and disclose material circumstances you are obliged to conduct a reasonable search of the information available to you. This search is for "information held within your organisation or by any other person.

This will include information held by us (with reference to the specific risk) or, for example, your outsourced IT provider or joint venture parties.

The insurer does not have to agree to a specific scope and so the more extensive your search is and the more evidence that you can provide on your internal policies and procedures the more likely an insurer will agree to the scope.

It is also extremely important that your internal record keeping (including of the enquiries undertaken and responses) is sufficient to prove that the reasonable search has been undertaken.

How do I disclose "sufficient information to put a prudent insurer on notice that it needs to make further enquiries for the purpose of revealing those material circumstances"?

If you fail to disclose every material circumstance which the insured knows or ought to know, you may still have satisfied the Duty of Fair Presentation if you disclose information which gives the insurer sufficient information to put a prudent insurer on notice that it needs to make further enquiries for the purposes of revealing those material circumstances.

If the insurer does not then make enquires of you to reveal the material circumstances, the insurer cannot later claim you failed to disclose them.

We will try to ensure that your presentation to your insurers is as comprehensive as possible, but it is clearly more advisable to endeavour to discover and disclose all material circumstances than to rely on the presentation putting insurers on notice that they need to ask further questions.

Because of this new rule, insurers are likely to ask more questions about your presentation than they did previously, so you need to make sure you have sufficient time to answer them fully before the start of your policy (and for any amendments to existing cover or endorsements).

What else do I need to know about the Duty of Fair Presentation?

The Act says your "knowledge" includes matters which you suspected, and of which you would have had knowledge but for deliberately refraining from confirming them or enquiring about them.

Therefore, you cannot 'turn a blind eye' in your search or fail to make enquiries in the knowledge that the answer will be damaging. Nor are you allow to "data dump", It must be presented in a 'reasonably clear and accessible' matter.

Remedies for breach of the Duty of Fair Presentation

There is a range of proportionate remedies which are based on the severity of the breach and depend on whether the breach is deliberate or reckless, or if the breach was not deliberate or reckless, what the insurer would have done if the Duty of Fair Presentation had been complied with.

What if the breach of the duty to make a fair presentation of the risk is deliberate or reckless?

If it is found that a breach is deliberate or reckless, then the position remains the same as under the current law, which is that the insurer is entitled to avoid the policy and retain the premium.

Where a policy is avoided it is deemed to never have existed, so you would have to repay any sums that you have received from the insurer in respect of claims under the policy. The insurer's ability to keep the premium is essentially a penalty that is imposed to deter such deliberate or reckless conduct.

A breach is deliberate where you know that you are in breach of the Duty of Fair Presentation; it will be reckless if you do not care whether you are in breach of the Duty of Fair Presentation.

What if the breach of the duty to make a fair presentation of the risk is not deliberate or reckless?

If it is found that the breach of the duty is not deliberate or reckless, but it is still a breach, there are a range of proportionate remedies available to the insurer.

There are broadly three options available to the insurer based on what they would have done if there had been a fair presentation of the risk:

a) Avoidance

If it is found that there was a breach of duty and the insurer would not have written the risk at all, then they may avoid the policy but must return the premium. This means that avoidance is still available as a remedy for insurers even where the breach is "innocent" (or at the very least, not deliberate or reckless).

To be able to avoid the policy the insurer would have to be able to demonstrate that if you had made a fair presentation of the risk, they would not have been prepared to write the risk at all. This would have to be proved by evidence from the underwriter who was responsible for writing the risk

b) Variation of the terms

If, in the absence of a breach of duty, the insurer would have written the risk but on different terms, the contract will be treated as if it had been written on those terms. This does not include terms relating to premiums (as to which, please see below).

This means, for example, that the insurer may impose certain exclusions where they can establish that these would have been imposed if there had been a fair presentation of the risk. This could affect whether they pay the claim in question.

This remedy can also have an effect on losses which the insurer has already paid because it involves treating the contract as if it had been entered into on those different terms, therefore having retrospective effect.

Therefore, if the insurer proves that it would have contracted on different terms, that would have reduced or extinguished its liability for losses which pre-date the insurer's discovery of a breach of the duty of fair presentation, you may have to reimburse the insurer for those losses.

c) Reduction of the claim

If it is found that there was a breach of duty and the insurer would have written the risk, but for a higher premium, then the insurer is entitled to reduce the claim settlement proportionately.

This remedy may be used on a standalone basis or alongside the variation of terms discussed above.

Warranties and other terms, contracting out and abolition of basis clauses.

Compliance with all terms and conditions in your policy is the best way to ensure that you have full protection under your insurance policy.

The below only becomes relevant where you have failed to do so.

A warranty is a term in a policy which, if breached under the current law, discharges the insurer's liability to you from the moment of the breach, even if the breach is later remedied.

Under the Act, the insurer will not be liable to pay any claims while you are in breach of warranty. If you later remedy the breach, then the insurer is liable for subsequent claims, unless they are attributable to something that happened before the breach was remedied.

The insurer is also liable for losses which occur or are attributable to something that happens before the breach of warranty

How to remedy a Breach of Warranty

In view of the importance of these terms, you need to understand how you can "remedy" a breach of warranty to regain the benefit of your policy.

Where the warranty requires something to be done by a particular time i.e., installation of a sprinkler system by a particular date, and the sprinkler system is not installed by the required date, the breach will be remedied if the "risk to which the warranty relates later becomes essentially the same as that originally contemplated by the parties" - so if the sprinkler system is subsequently installed, that will remedy the breach.

For other warranties, the breach is remedied if you cease to be in breach. For example, if you warrant that you will always have a security guard at your premises, but in fact one day there is no security guard, the breach will be remedied when there is a security guard once again present.

There may be situations where a breach cannot be remedied. For example, if you have a policy covering a shipment of goods in which you warrant that the goods will be stored in refrigeration units at all times, and during transit the

goods are not refrigerated causing them to become damaged, but are then later moved to refrigeration units, then it is unlikely that the insurer would be liable because the damage caused by the breach cannot be remedied.

Terms not relevant to loss

The Act will prevent an insurer from relying on your breach of a term of a policy if that breach is entirely unconnected with the actual loss you suffer. For example, it is unlikely that the insurer can rely on breach of a fire alarm warranty where loss is caused by flood or burglary.

This applies to any term of the policy if your complying with that term would be likely to reduce the risk of loss of a particular kind, or at a particular location or time. For example, where you warrant that your sprinkler system will be inspected every six months, since that would reduce the risk of loss caused by fire.

This does not apply to terms which define the "risk as a whole"– for example, terms which define who is entitled to drive a vehicle, or a warranty that a ship will not enter a war zone – breach of those terms will allow insurers to deny a claim regardless of their connection to the loss.

The determination of whether a term is one that either –

a) Reduces the risk of loss of a particular kind, or at a particular location or time, so that the insurer cannot rely on a breach that is unconnected with actual loss suffered, or a term which defines the risk as a whole, so that the insurer's full rights are preserved in the event of a breach,

b) A term which defines the risk as a whole, so that the insurer's full rights are preserved in the event of a breach, is not straightforward and is likely to lead to disputes. It is therefore imperative that you comply with all policy terms and conditions to avoid being in this position.

Contracting out

In business contracts, the parties are free to contract out of any part of the Act, apart from those relating to basis clauses (see below). In order to do this, the insurer must overcome two hurdles:

a) First, the insurer must take sufficient steps to draw the term to your attention before the contract is concluded, and

b) Second, the term must be drafted so that it is clear and unambiguous as to its effect.
This means that the insurer has to explain the effect of the term.

For example, there may be circumstances where an insurer seeks to preserve the protection provided by the current law in respect of breaches of particular terms, such as premium payment warranties.

We will inform you if we become aware of insurers who look to contract out of any elements of the Act, for your particular insurances and what this might mean for you.

Abolition of 'Basis Clauses'

Any representation made by you in connection with a proposed insurance policy is currently capable of being converted into a warranty as to its truth/accuracy by means of a term in either the policy or the proposal. Such "basis clauses" will no longer be allowed.

This means that a term which states that the facts stated in the proposal form the basis of the contract will no longer be of any effect.

The parties cannot contract out of this provision, which is good for you as it reduces the risk of inadvertent pre-contractual misrepresentation. However, please note that this does not have an impact on your Duty of Fair Presentation (as referenced above).

Conclusion and how to start planning

To benefit from the Act, you will need to consider how you currently collect the information you provide for insurance purposes. Does this support the detail and scope required to comply with a 'reasonable search'?

Demonstrating how you have decided:

a) What is a reasonable search and how you have achieved it, and

b) Who are the relevant senior management who play a significant role in making decisions on the business activities to which the insurance relates will also mitigate the potential for insurers to question your compliance with your duty of fair presentation. Therefore, there is an expectation that implementing the Act will take time so you should start work on this as soon as possible.

Should you wish to discuss this matter further, please speak to your usual Estate Insurance Group contact