The City of London Law Society

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COMMENTS AND RESPONSES BY THE INSURANCE COMMITTEE OF THE CITY OF LONDON LAW SOCIETY TO THE LAW COMMISSIONS' REVIEW OF INSURANCE CONTRACT LAW, ISSUES PAPER 6 – Damages for Late Payment and the Insurer's Duty of Good Faith

The City of London Law Society ("CLLS") represents approximately 13,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi jurisdictional legal issues.

The CLLS responds to a variety of consultations on issues of importance to its members through its 17 specialist committees. This response in respect of the captioned subject has been prepared by the CLLS Insurance Committee. The Committee's purpose is to represent the interests of those members of the CLLS involved in the insurance industry.

Introduction

(A) The Issues Paper seems to include three separate topics:

(1) Should there be reform of S.17 Marine Insurance Act 1906 to permit an award of damages for breach of the duty of good faith?

(2) Should the decision in Sprung be reversed?

(3) Should late payment of claims be categorised as potentially a breach of the duty of good faith such as to entitle an insured to an award of damages not limited to interest?

(B) The approach which underpins the remarks and suggestions set out below in response to Part 10 of Issues Paper 6 is threefold:

(1) the 'singling out' of insurers from insured and other commercial entities for special/different treatment ought properly to be avoided;

(2) England in general, and London in particular, has attractions to insurers as a place to carry on business and the reasons for that are a mixture of the relative certainty perceived to exist under English insurance law and

(3) the perceived fairness of English insurance law and the expertise available to deal with disputes.

(C) Dealing briefly with the first point: an insurer in England is a commercial entity, offering a product for sale, and is, in principle, no different from many other commercial entities doing likewise. In a contract for the supply of goods or services the party with the obligation to pay is not susceptible to a claim for damages in the event of late payment beyond an award of interest. If one assumes that a sum payable under a policy of insurance is, or is no different from, a simple debt, then whilst we agree that an insurer should be liable in damages, other than interest, for late payment the same should be said of any other creditor. In so far as that is not achieved by the decision in *Sempra Metals –v- IRC* then it should be the subject of legislation

(D) As to the second point it is a matter that needs to be borne in mind when framing the scope and content of new legislation; the creation of obligations which are uncertain and which depend upon judicial or other construction before they can be fully understood and/or applied is a recipe for litigation and has little to commend it.

Should s.17 Marine Insurance Act 1906 be reformed?

The short answer is 'yes' – the view taken by some of our members is that Steyn J. at first instance in *Banque Keyser Ullmann –v- Skandia* was correct and that a breach of the duty of good faith by an insurer should have a remedy in damages. We go a stage further, however, in suggesting that, to mirror English contract law generally, either party to the contract of insurance should be entitled, in the event of breach by the other party, to elect either for avoidance from the date of the breach or for damages. In this way one preserves an even playing field and fairness to those involved. In our view, however, different considerations apply to late payment of claims such that one has to develop a separate set of rules relating to claims and payment thereof if one is to maintain a position parallel to contract law in general.

We should also mention that in the experience of some of our members it is wrong to be dismissive of the right of an insured to avoid a contract of insurance which has been known and, in suitable cases, may continue to be. Whilst it does not, and is unlikely to, happen often it is still a right which has value.

We now turn to the Consultation Questions using the same numeration. Our remarks from this point deal only with the question at (A) (2) above: late payment.

THE LAW ON DAMAGES FOR LATE PAYMENT

10.1 In so far as the present law entitles an insured only to interest where a claim is paid late then it is unsatisfactory and is in need of reform. As far as awards of interest are concerned, to remove doubt (which often arises where the claim is not litigated) one can enshrine the common law position as to interest in statute. If one wishes to create

an incentive, and protect the smaller business in particular, then the express extension of the Late Payment of Commercial Debts (Interest) Act 1998 to payments under policies of insurance would achieve the apparently desired object although, again in the interests of fairness, it seems reasonable to suggest that the 1998 Act should apply equally to unpaid premium or other sums due from an insured to the insurer.

10.2 and 10.3 relate to Scotland and are thought to be for Scottish lawyers to deal with rather than English.

LEGISLATIVE REFORM OF THE INSURER'S DUTY TO ACT IN GOOD FAITH

10.4 We do not believe that this present area of interest, which is essentially one of claims handling issues, is the place to consider or to introduce the concept of a duty of good faith during the currency of the policy. We understand that the question of an insured's duty of good faith is to be the subject of a further Issues Paper and assume that this will include the concept of a duty which continues beyond conclusion of the contract of insurance. This would be the place to consider the issue raised here. We do not think the concept of a duty of good faith in the claims process necessary to a reversal of the *Sprung* decision (see below).

If, however, there was to be legislation as to the duty of good faith in the making and handling of claims then we suggest that the legislation should go in both directions and should spell out the duty, in principle, of each of the claimant and the insurer. Much of claims handling is, in practice, bedevilled by the apparent reluctance of insured to provide an intellectually coherent claim, supported by the right information with full disclosure of relevant or material documents. All too often it is left to the loss adjusters appointed by the insurer to compile the claim and then adjust it to the point of agreement with the insured. All too often, the claims made by insured, with or without the assistance of a loss assessor, are inflated and often, for instance, based on the false premise that the amount payable for loss of stock, plant and machinery, is to be calculated on a replacement as new basis which is, in commercial insurance, more the exception than the rule.

10.5 Items (1) to (4) are unobjectionable: indeed perhaps one should add to (1) that investigation should take place in a reasonable time. One might impose a duty upon insured to:

> (1) Act promptly and reasonably to mitigate/minimise the insured loss (thus resolving the difficulties left by *Yorkshire Water –v- Sun Alliance*)
>
> (2) Present its claim in reasonable detail within such time as may be agreed or a reasonable time after the loss.
>
> (3) Disclose all documents which may be material to the claim or the insurers' investigation of it.
>
> (4) Respond to requests by the insurer for documents and information within a reasonable time of the request being made.

In response to those who might say that (1) to (4) above are implicit, so are (1) to (4) at 10.5 of the Issues Paper. Our point is that if we are going to enshrine this kind of obligation in legislation then it should go both ways and not appear to impose on one party for the exclusive benefit of another.

10.6 We refer to (A) and (C) above: any list should be exhaustive. The alternative leaves an area of doubt as to what other terms may be applied which is not at all attractive to those who commit significant resource to establishment of their insurance business in England or to those who are in the unfortunate position of having to make a claim. If there is to be an exhaustive list then there are sufficient trade bodies (ABI, Lloyd's, IUA, AIRMIC, BIBA, BILA for instance) well able to put both sides of the story and develop a fuller set of guidelines if required.

Damages for breach of good faith

10.7 We agree that an insured should have a remedy in damages (see below) but not using the concept of the duty good faith during the currency of the policy.

10.8 Damages should be limited to losses within the contemplation of the parties at the time of the contract. In our understanding the current state of English Law is that where parties are in contract they are presumed to have stipulated for the various aspects of their relationship and the rights and liabilities arising such that a party can owe no greater duty in tort than he or she can by virtue of the contract. The use of a concurrent tort remedy could, therefore, benefit only a third party who is unlikely to be a potential claimant. The addition of a new tort remedy unilaterally available to an insured against insurers is unlikely to contribute to the continuation of England's pre-eminence as a popular place to do insurance business.

Delay during litigation

10.9 Loss caused by delay in litigation should not be precluded: the loss should be treated in no way different to an award of interest on the premise that, if the insurer is unsuccessful in the litigation, it will have interest and damages to pay having had them in its pocket for the duration of the litigation. If, on the other hand, the insurer is successful the problem will most likely not arise.

A non-excludable duty

10.10 Since parties to a contract are free to stipulate the terms of their bargain as they please it should be permissible for exclusion of the duties.

Impact of reform of the insurer's duty of good faith

10.11 The reforms as contemplated by the Issue Paper offer no benefit to insurers: they are, almost entirely, 'anti-insurer' in character. Our impression is that those reforms will increase claims costs which will inevitably mean a rise in premiums. If one wants to achieve a nil increase in premium from today's levels then the answer can only be to do nothing.

10.12 The number of successful claims is impossible to predict; the assertion that the number will be low can only be to justify the need for reform on the basis that it will make little difference; an argument, we observe, in favour of doing nothing!

THE "STRICT LIABILITY" APPROACH: REVERSING THE DECISION IN *SPRUNG*

10.13 (1) We are not persuaded that the correct characterisation of an insurers duty is to prevent the loss from happening. It is, rather, to pay an indemnity equal to the insured loss sustained by the insured which is, we believe, quite clearly reflected by the terms of most current insurance policy wordings.

(2) We agree that late payment should entitle an insured to damages for foreseeable losses beyond an award of interest. In our view this is best achieved by the implication of a term into the contract of insurance to the effect that payment should be within a reasonable time of the occurrence of the loss. As to what is reasonable that is something that the courts are better placed to grapple with. As an aside a question will arise as to commencement of the limitation period: as English Law stands commencement is from the date of the loss which is a known and certain position. A failure to pay will necessarily be later in time. Rather than have two separate dates for commencement of limitation it is our view that there should be one and that it should be the date of loss as being a certain and known date. There was some support amongst our number for the Scottish system.

(3) See 10.10 above – the parties should be free to contract as they see fit.

10.14 Properly and carefully drafted legislation is preferable to achieve clarity.

Impact of reversing *Sprung*

10.15 See 10.11 and 10.12 above. Our impression is of a serious volume of claims by aggrieved insured in the event that reforms as advocated by the Issues Paper are put in place.

DAMAGES FOR CONSUMERS' DISTRESS, INCONVENIENCE OR DISCOMFORT

10.16 In cases of unreasonable refusal to pay claims, as distinct from late payment cases, and where the insurance is personal to the insured (travel, health etc) and is not business related then an award of this kind is reasonable in principle.

10.17 Awards of this kind are better left to the courts.

10.18 Awards should be proportionate to the value of the claim

24 June 2010

Its contents should not be taken as legal advice in relation to a particular situation or transaction.

THE CITY OF LONDON LAW SOCIETY
INSURANCE COMMITTEE

Individuals and firms represented on this Committee are as follows:

Geoff Lord – Kennedys, Chairman
Martin Bakes – Herbert Smith
Emily Benson – Barlow Lyde & Gilbert
Jonathan Goodliffe - Freshfields
Charles Gordon – DLA Piper
Catherine Hawkins – Berrymans Lace Mawer
Glen James – Slaughter & May
Stephen Lewis – Clyde & Co
Francis Mackie – Edwards Angell Palmer & Dodge
Martin Mankabady – Mayer Brown
Kenneth McKenzie – Davis Arnold Cooper
Michael Mendelowitz – Norton Rose
Terry O'Neill – Clifford Chance
Richard Spiller - Edwards Angell Palmer & Dodge
Christian Wells – Hogan Lovells
David Wilkinson - Kennedys
Paul Wordley – Holman Fenwick & Willan