CITY OF LONDON LAW SOCIETY

INSURANCE LAW COMMITTEE

Minutes of a Meeting held at the offices of Lawrence Graham at 5pm on Tuesday 10th June 2008

Present:

Ian Mathers (Chairman) – Allen & Overy
Martin Mankabady – Lawrence Graham
Martin Bakes – Herbert Smith
John Farrell (for Geoff Lord) – Kennedys
Jonathan Goodliffe (for Michelle Bramley) - Freshfields
Beth Dobson (for Glen James) - Slaughter & May
Michael Mendelowitz – Norton Rose
Richard Spiller – EAPD
Terry O'Neill – Clifford Chance
Kapil Dhir (for Paul Wordley) – Holman, Fenwick and Willan

In attendance:

David Whear – Norton Rose
Robert Purves – 3 Verulam Buildings

Apologies for absence:

Anna Tipping – Linklaters
Christian Wells – Lovells
Kenneth McKenzie – Davies Arnold Cooper
David Wilkinson - Dewey & LeBoeuf

1. The Chairman thanked Martin Mankabady for hosting the meeting and introduced Robert Purves, who had been Chief Counsel, Insurance and Prudential Policy, at the FSA prior to his recent move to 3 Verulam Buildings. He had kindly agreed to talk to the Committee about some issues he had been involved in at the FSA.

Robert thanked the Committee for the opportunity and focused his talk on the FSA's approach to Treating Customers Fairly (TCF) and DP08/2 Transparency, disclosure and conflicts of interest in the commercial insurance market. As to TCF, his main message was that while the FSA had begun this initiative by targeting organisational internal culture and practices, with a view to ensuring that firms were taking account of the need to treat customers fairly, more recently they appeared to be moving more towards examining practical outcomes for consumers in terms of contractual and service standards. This approach, if continued, could result in the introduction of sub-principles without going through the usual procedures for Handbook material. It could be difficult for firms and their legal advisers to determine the content of those principles or how their own practices measured up.

As to transparency, the discussion paper followed an FSA review of commission disclosure in 2006 and a further review by consultants in 2007. Although the consultants had come down against mandatory disclosure on cost-benefit grounds, the FSA considered that there were nevertheless several interrelated issues that ought to be addressed, namely (1) current FSA rules already required disclosure to business clients on request, but any such disclosures were often unclear and incomplete; (2) the problem was compounded by a lack of understanding by clients as to the status of intermediaries and what steps they

might take to "search the market"; and (3) while the 2007 review had concluded that customers typically did not seek disclosure or make use of the information when disclosed, such information might be employed more generally e.g. by other intermediaries, so as to improve competition in the market. DP08/2 scheduled some illustrative rules to mandate commission disclosure, but in Robert's view there were some legal questions to be considered. The Insurance Mediation Directive contained no such rules and any that the FSA introduced could accordingly be considered "super-equivalent" and open to criticism on that ground, although it was possible that the position might change as the result of a review of the Directive which was currently being mooted; having regard to the 2007 review, it was not clear that mandatory disclosure could be justified on grounds of consumer protection; and there could be difficulties in enforcement across boundaries, particularly in the case of e-commerce.

In discussion, Terry O'Neill suggested that the FSA's paper might be seen more as a signal to the industry to come up with solutions of its own. Richard Spiller thought that the FSA should tread rather carefully, because brokers were able fairly easily to transfer mandates offshore and any unwelcome rules could encourage them to do so. He also pointed out that the question of distinguishing financial incentives based on an intermediary's overall performance from commission and other incentives related to particular transactions could be one of some difficulty.

2. Approval of minutes

The minutes of the meeting of 11th March were approved.

3. Membership

David Wilkinson's membership of the Committee was approved. The Chairman reported that Maxine Cupitt had reluctantly decided to resign due to work commitments. He had also asked James Bateson whether he was still interested in attending but had not heard back.

4. Insurance Contract Law

The Chairman drew attention to the Law Commission's Update 14 which contained a link to their summary of responses to their consultation paper on non-disclosure, misrepresentation and breach of warranty in relation to consumer insurance, together with a promise that a summary in relation to business insurance would follow. It seemed that their proposals for consumer insurance had received a soft ride and would generally be maintained. The main exception had been for their proposal that intermediaries should normally be treated for the above purposes as agents for the insurer unless they conducted a fair analysis of the market. These proposals had received considerable resistance (including from the Committee) and the Commission would be re-thinking their position. David Whear, who had led the Committee's response on the position of intermediaries agreed and Martin Mankabady said that recent remarks by David Hertzell indicated that the Commission may start again from the current position, under which intermediaries are normally treated as agents for the insured. Martin Bakes said that otherwise perhaps the most noteworthy point was that the Commission appeared to be inclined to fast track their proposals for consumer insurance, perhaps partly because they were more likely to gain early approval and partly because the main basis for criticising the current law was its treatment of consumers. This could have the downside that any proposals for business insurance would have to await a later opportunity for legislation and, separated from the proposals for consumer insurance, might not get the necessary backing. Richard Spiller suggested, however, that the debate so far indicated that there could be considerable difficulty in getting agreement on business insurance and there might be merit in proceeding with legislation on the proposals for consumer insurance and seeing how they bed down. David Whear and Martin Mankabady pointed to the difficulty which still had to be faced in defining a consumer and in particular dealing with the position of small businesses. There was also a discussion as to whether the position of brokers might depend upon whether the Commission maintained their initial proposals to make any rules for business insurance optional, since that was unlikely to reduce the broker's exposure. It was agreed that the Committee should await the Commission's summary of responses on business insurance before deciding whether to submit further comments.

5. Rome I

The Chairman noted that this Regulation had been adopted by the Council on 6th June, and HMT had issued a consultation paper on the question whether the UK should opt in. Subject to any views to the contrary, he proposed to circulate a draft response proposing the answer yes, on the basis that (1) the main objections which the Committee had voiced to earlier drafts of the Regulation, notably the court's discretion to apply overseas mandatory laws, had been substantially removed; and (2) the specific provisions for direct insurance were now confined to a codification of the rules in the insurance Directives, with a requirement that they should be reviewed in 5 years time. He understood that the Financial Law Committee would be taking a similar line, subject to a reservation as to the requirement to review the position regarding the effect of assignments on third parties in two years time. Martin Bakes noted that the Committee had earlier queried the exclusion from the Regulation of "obligations arising out of dealings prior to the conclusion of the contract" and wondered whether that could take out rules governing contractual non-disclosure and misrepresentation. The Chairman said that he had understood from an answer given by HMCS in a stakeholder meeting where he had raised the point that the exclusion was aimed at an institution which the Germans called "culpa in contrahendo" and provided for damages for pre-contractual misbehaviour. Claims of this nature (which might include, so far as the UK is concerned, damages for deceit) fell within Article 12 of the Rome II Regulation and the exclusion appeared to be designed to make this clear. He had understood that the exclusion would not apply to contractual remedies for non-disclosure misrepresentation or breach of warranty. He also noted that a recital (10) had been added to help make this clear. Admittedly the terms of the exclusion might still be construed more widely. That would presumably mean that in England the common law would apply. But while it would detract from the unifying effect of the Regulation, he doubted that it would be a reason for the UK not to opt in.

6. EU Draft Common Frame of Reference

The Chairman drew attention to the note of a meeting he had attended with Professor Hugh Beale, one of the architects of this draft. Hugh had taken pains to emphasise that this draft was most likely to be useful as a source of comparative information on EU contracts laws and not as a basis, at least in the foreseeable future, for an EU uniform law, save conceivably as an optional instrument like the UN Convention on contracts for the international sale of goods. It was not yet clear how the draft would be taken forward by the Commission nor whether the Principles of European Insurance Contract Law which had been submitted by the Innsbruck Group would be incorporated.

7. Part VII transfers

The Chairman noted that HMT had made some modifications to the amendments they had proposed to Part VII, notably to ensure that the express provision to enable the court to transfer outward reinsurance contracts and override default provisions did not prejudice their wider power to make consequential provisions. Glen James had written to support this modification, subject to some points on wording. Beth Dobson said that in addition the letter approved a modification to ensure that the power of the court to override default provisions extended to retained contracts but questioned whether outwards reinsurers whose contracts were to be retained under the scheme as well as those whose contracts were to be transferred should be notified of the proposal. Richard Spiller questioned whether that should usually be necessary, but the Chairman thought there might well be cases where a reinsurer's exposure could be affected by a change in structure of the retained business. Richard understood that the three statutory instruments proposed by HMT to implement their modifications had now been laid, though only one had been published [*Chairman's note: the other two have since been published and all three circulated to the Committee.*]

Jonathan Goodliffe noted that there were various other difficulties in the operation Part VII, some of which related only to the drafting of that part of the FSMA, such as the relationship with Gibraltar, but others had more to with the Directives, notably the provisions for regulatory consents. There could be value in the

Committee raising these difficulties in the appropriate quarters with a view to further amendments. It was agreed that he should liaise with the Chairman and bring any proposals to the Committee.

8. Inherited estates

The Chairman drew attention to a change in FSA rules proposed in CP08/11 under a proprietary with-profits insurer would no longer be allowed to charge compensation costs (e.g. for mis-selling) to the inherited estate, on the ground that this would incentivise such insurers to maintain proper systems and controls. Glen James had kindly agreed to look at this paper and recommend any response which the Committee should make, but would welcome any input. The Chairman said that the only thought which had occurred to him was that the paper did not appear to make a case for the present position, which might be that policyholders should expect to take at least part of the costs associate with the operation of the with-profits fund, even including operations which resulted in the insurer incurring legal liabilities.

9. Solvency II

The Chairman reported that he had been in touch with the ABI to ascertain whether they intended to resuscitate their Legal Working Group which had looked at the draft Framework Directive, but it seemed that they thought time was not yet ripe. Jonathan Goodliffe thought that indeed there was not much a Legal Group could do until further policy agreements had been reached, notably on the role of group supervision.

10. Lloyd's

The Chairman said that he had earlier reviewed the regulatory reform order on which HMT were consulting and had opined by email that there was nothing for the Committee to comment on; and had received no thoughts to the contrary. Richard Spiller queried whether anyone knew whether there was a definite date for bringing forward the order, since it could assist some transactions otherwise affected by the divestment provisions; but apparently not.

11. Recent court decisions

John Farrell said that the full judgment in *Seele Austria v Tokio Marine* which the Committee had considered at its last meeting was now available and he would forward it to the Chairman together with an article he had written on the case. Michael Mendelowitz said that he understood leave to appeal to the House of Lords had been given in *Wasa v Lexington*, also discussed then, and he drew attention to a very recent judgment by Christopher Clarke J in *Lexington v Multinacional de Seguros* [2008] EWHC 1170. This effectively upheld the judgment in *Kosmar v Trustees of Syndicate 1243* which had again been discussed at the March meeting.

12. Items for future attention

Jonathan Goodliffe understood that the Ombudsman's report into Equitable Life was expected to be published soon and would be likely to be of interest to the Committee.

13. Next meeting

The next meeting will be held at 5.00 pm on 23 September at the offices of Allen & Overy.