Comments of City of London Solicitors Company, Insurance Law Committee regarding the Law Commissions' Issues Paper 1 – Non-Disclosure and Misrepresentation

(Review of Insurance Contract Law)

These comments represent preliminary views and opinions of the Insurance Law Committee of the City of London Law Society. The members of the Committee are Ian Mathers of Allen & Overy (Chairman); Martin Bakes of Herbert Smith; Christian Wells of Lovells; Michael Mendelowitz of Barlow Lyde & Gilbert; Stephen Lewis of Clyde & Co; Geoff Lord of Kennedys; Kenneth McKenzie of Davis Arnold Cooper; James Bateson of Norton Rose; Martin Mankabady of Lawrence Graham; Maxine Cupitt of CMS Cameron McKenna; Richard Spiller of Kendall Freeman; Paul Wordley of Holman Fenwick & Willan; Glen James of Slaughter & May; Terry O'Neill of Clifford Chance; and Victoria Sander of Linklaters.

1. We are grateful to the Law Commissions for the opportunity to attend the seminar relating to Issues Paper 1 which was kindly hosted by Beachcroft Wansbroughs on 21st September 2006. We applaud the decision to produce Issues Papers on particular topics in the course of the review and to seek views prior to publication of a Consultation Paper. We are mindful of the fact that whilst the Issues Paper seeks views on a number of matters, you have indicated that you do not wish, at this stage, to receive detailed responses to the Issues Papers. Whilst, therefore, we are taking a close interest in the review, we have limited our discussions so far to obtaining preliminary comments from members of the committee about the Issues Papers. We thought that, nonetheless, it might be of interest to you to be made aware of those preliminary comments and in this note, we set out comments made in relation to Issues Paper 1.

2. So far as the tentative proposals relating to consumer insurance contracts are concerned, the committee, in general, supports those proposals. There were three matters raised by members of the committee which we would like to pass on to you. These were as follows:

    a. A number of members questioned whether the test for fraud should include the requirement at paragraph 6.39(2) of the Issues Paper, i.e. that the insured must know that the statement was material to the insurer (or realised that it might be material and did not care whether it was or not) in addition to the requirement in Clause 6.39(1) that the insured must know that the statement was untrue (or realised that it might not be true and did not care). It was felt that, in relation to the question of fraud, knowledge of materiality should not be required and that if the consumer insured tells a lie (or is reckless as to whether he or she is telling a lie) the insured should bear the risk of materiality. It should be sufficient that the fact is indeed material – and the insured's ignorance about whether or not it was material should not matter. The same point should also apply in respect of business insureds, although it was not dealt with expressly in the Issues Paper – although it would appear to be implicit in paragraph 7.73 that it is envisaged by you that the test for fraud in relation to business insureds should include this requirement.

    b. Some members of the committee had reservations about there being no residual duty of disclosure in cases of consumer insurance. They felt that the changes proposed in relation to the test of materiality and the remedy for non-disclosure and misrepresentation would provide sufficient protection to consumers. In essence, the proposed change would excuse

the conduct of an insured who knew of facts which he or she realised were important but chose not to bring them to the insurer's attention. This is "sharp practice" as identified by the Law Commission in 1980 and, today would still be regarded as "sharp practice".

c. Some members of the committee were doubtful about the suggestion that the Court should have discretion to apply a proportionate remedy where the policyholders fault was "minor" and other insurers would have accepted the risk (see paragraph 6.72). It was felt that this would add an unnecessary complexity to the law. It would involve difficult decisions about what was "minor" and what a sufficient body of "other insurers" might be. It was felt that it would be simpler for the position to be determined by reference to the position of the actual insurer and that the matter would be best left to the Court to decide whether to believe the actual insurer's evidence as to what its reaction would have been had there been full disclosure and/or no misrepresentation.

Otherwise it was considered that the proposals seemed generally to reflect FOS practice which had already achieved a significant measure of acceptance on the part of insurers. There was support for the proposed changes to the test of materiality and to the remedies available to insurers (including the concept of proportionality). For completeness we should mention that a few members of the committee expressed concern about the practicability of determining materiality by reference to the position of the reasonable insured.

3. Our impression was that the section of the Issues Paper dealing with business insurance was more equivocal than that which dealt with consumer insurance. In many respects, echoing this, the discussions relating to business insurance were of a more general nature than those relating to consumer insurance. At this stage, we would draw your attention to the following points that were made:

a. We noted that so far as the duty of disclosure was concerned, you proposed significant differences between consumer insureds and business insureds; in particular, you tentatively concluded that there should be no residual duty of disclosure so far as consumer insureds were concerned, whereas the general duty of disclosure should be retained in relation to business insurance. Some members of the committee expressed the view that having reached the tentative conclusion that the duty should not be retained in consumer cases, it might be said to be illogical to retain the general duty in relation to business insurance. Some members commented that in many areas of business insurance, insurers carried out a very significant amount of due diligence (for example surveying property when underwriting commercial property policies). It could be argued that, ultimately, it may become a question of price, i.e. whether business insureds generally should be prepared to pay a larger premium in order to reduce the uncertainty which inevitably results from there being a general duty of disclosure and, in this regard, the position in relation to business insurance was no different to consumer insurance. Other members of the committee supported the retention of the duty of disclosure for the same reasons as set out in 2b in addition to the reasons given in the Issues Paper.

b. In relation to paragraph 7.71 of the Issues Paper, in which you indicate that you welcome views on whether the remedy for negligent misrepresentation should be proportionate, some members of the committee expressed firm views that the remedy of avoidance should be retained. They felt that it should be retained to encourage business insureds to provide

accurate information and that the remedy was more in line with the general legal position as regards misrepresentation.

c. In addition, some members of the committee expressed the view that in cases of business insurance, the practical application of the proportionate remedy is likely to be significantly more difficult than in cases of consumer insurance. There will be much greater scope for argument about what the insurers would have done had there been full disclosure and/or was misrepresentation.

d. Most members of the committee agreed that MAT insurance and reinsurance should be treated in the same way as business insurance.

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