

# Faith lift

Imran Benson considers the Law Commission's proposal to review the law of insurance contracts and asks: is this the end of good faith?

## THE LAW ON MISREPRESENTATION AND

non-disclosure is such that swifter, more radical and more consistent change is required.' The Law Commission has 'tentatively' recommended radical changes to the law of insurance contracts, the unabashed purpose of which is to improve the legal position of proposers. This article attempts to summarise some of the more important changes – it focuses on consumer insurance contracts.

Every law student knows that insurance contracts operate on the principle of good faith: a principle that imposes onerous requirements on those seeking insurance. Good faith requires that the proposer reveal all the facts that would affect the mind of a prudent insurer. A fact can affect the mind without being decisive. The insurer who is affected and seeks to avoid the contract will need to show that, but for the non-disclosure (or misrepresentation), the insurer would have contracted either on different terms or not at all.

The Commission believes good faith needs rebalancing. It proposes essentially four key reforms:

- Reform to the test of materiality.
- Abolition of the duty of disclosure.
- Reform to the test for fraud.
- Introduction of the remedy of proportional payment.

### The test of materiality

Materiality is currently judged by reference to the prudent insurer. The Commission thinks that this test is unfair and recommends that materiality should focus on the proposer, not the insurer. In practice, a fact should only be material, if (in addition to inducement) the insurer proves either the actual proposer appreciated its materiality, or that a reasonable insured (judged by the type of policy, the manner of sale and the normal characteristics of its consumer) would have done so.

### Duty of disclosure

The Commission proposes to abolish the residual duty of disclosure and treat an insurer as knowing all 'reasonably identifiable' infor-

mation within their files. It adopts the reasoning of the Financial Ombudsman Service: in an electronic age when it is common to acquire insurance by telephone, text messaging and the internet, it is unfair to penalise consumers for a failure to disclose if no clear question is asked about the risk, or if, somewhere, an insurer had already been given that information. The consequence, however, can seem unfair. If a mother buys household insurance shortly after her daughter's ex-boyfriend threatens the family, she (the mother) won't, unless asked, be obliged to disclose this. If not asked and not disclosed, there is no reason why an insurer could avoid a claim arising out of a burglary.

### Third parties

The Commission also proposes that where an insurer obtains permission to contact a doctor (or other third party), if the proposer reasonably thought that the insurer would use that permission to verify supplied information (medical history), non-fraudulent misrepresentation will not entitle the insurer to avoid. Even if the proposal form warns that an insurer might not contact a doctor to verify information, the Commission suggests an insured could still be able to establish he reasonably believed the insurer would verify. This proposal aims to protect consumers' reasonable expectations; some might ask if it is instead a recipe for increased bureaucracy and expense. In a contract for life insurance, the Commission also asks if life insurers should, when a policy is at least three years old, be able to avoid for non-fraudulent misrepresentation.

### Fraudulent misrepresentation

Since the ability of insurers to avoid is to be largely limited to where fraud has occurred, its definition is important. Fraudulent misrepresentation can currently be established whenever a proposer provides information that he knows to be untrue (or realises that it might not be true and does not care). In addition, the Commission proposes that the insured should also know that the statement was material to

the insurer (or realised it might be material and did not care). The aim of this 'beefed-up fraud' test is to ensure that avoidance for it can only occur where the proposer is morally culpable. The Commission gave the example of a motorist who, on a renewal form, falsely represented that he did not own a second car. He subsequently explained his untrue answer saying he thought the question was merely for marketing purposes. The Commission thought this untruth did not justify a finding of fraud. Under its proposals, this driver's claim would have had to be met.

### Proportional payment

In cases of negligent misrepresentation, the court, it is proposed, should apply a proportionate remedy by asking what the insurer would have done had it known the true facts. If the insurer can show it would have declined the policy in whole or in part, then it will be entitled to avoid to the same extent. If it would have charged a greater premium, it will be required to pay the claim as adjusted proportionately to the under-payment of the premium. Imagine a premium of £500 is charged for a household insurance policy. A claim is subsequently made and it is discovered that the proposer negligently failed to disclose that his live-in boyfriend had four dishonesty convictions. Had this information been disclosed, the premium would have been £700. In these circumstances (generally), the Commission's proposals would require that 5/7ths of the claim be paid.

### Going too far?

In a lengthy, thoughtful, well-written and preliminary paper, the Commission proposes many radical changes to consumer, life and business insurance. Some may think that the proposals, albeit well intentioned, go too far. The Commission has asked numerous specific questions and is holding consultation seminars – there is still time to say so.

Imran Benson is a barrister practising from Hailsham Chambers