

BELRIM - Insurance Act 2015

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Brussels, 16th June 2016

Insurance Act 2015

Agenda

1. **The issue**
2. The legislation
3. Implementation
4. Q&A

Insurance Act 2015

The issue

- There has been growing concerns with claims being challenged by insurers under English law
- Mactavish analysis identified:
 - 45% of large losses were challenged by insurers
 - The average time to settlement of the disputed losses was three years; and
 - The sum obtained was on average 60% of the sum claimed.

Insurance Act 2015

The issue cont .../

- The concerns arose from a combination of:
 - Poor risk analysis and disclosure by policyholders; and
 - Poor law which protected insurers
- The prime causes of dispute were:
 1. Coverage (as a result of poor risk analysis and coverage design by the policyholder)
 2. Quantum arguments
 3. Breach of policy conditions
 4. Non disclosure and misrepresentation.

Insurance Act 2015

The issue cont .../

- Government intervention was necessary as the English judges could not easily develop the law (as they normally would in a common law system) as the 1906 Marine Act is very clear and both consumer and commercial disputes were going to arbitration rather than the courts
- The overriding objective of this legislation is to professionalise placement:
 - First, to require the policyholder to properly investigate their risk and comply with policy conditions
 - Second, to change the law so that it is more fair to policyholders who have made reasonable efforts to comply.

Insurance Act 2015

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Insurance Act 2015

The legislation - Duty of Fair Presentation (1/2)

- Question of substance and form
- Insured must:
 - Disclose all “material circumstances” it knows or ought to know or, failing that,
 - Provide sufficient information to put underwriter on notice to ask further questions
- Insured may not “data dump”
- Insured knows what its senior management, persons arranging insurance (e.g. broker/risk manager/finance director/proprietor) know and ought to know what would reasonably have been revealed by reasonable search.

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The legislation - Duty of Fair Presentation (2/2)

- Insured does not have to disclose a circumstance if insurer knows it, ought to know it or is presumed to know it. That means:
 - Insurer knows what is known to underwriters/agents - not senior management
 - Insurer ought to know what should have been passed on to underwriters or what it holds in its systems provided it is “readily available”
 - Insurer presumed to know common knowledge and what underwriters writing that class of business should know.

Insurance Act 2015

The legislation - Insurer's remedies

- “Deliberate or reckless breach” – insurer can avoid policy and keep premium
- All other breaches:
 - If the insurer would not have written the risk – avoid and return premium.
 - If the insurer would have imposed additional terms/additional limits – these are imposed from inception and/or
 - If the insurer would have charged a higher premium – claim is reduced pro-rata (average)
- NB. No “innocent non-disclosure”.

Insurance Act 2015

The legislation - Warranties & similar terms

- Basis clauses abolished – cannot contract out
- Warranty becomes suspensive condition – cover is suspended but breach can be remedied and cover restored
- Insurer cannot rely on warranty or other risk mitigation term if insured shows non-compliance “would not have increased the risk of the loss which actually occurred in the circumstances in which it occurred”
- Does not apply to a term which defines risk as a whole.

Insurance Act 2015

The legislation - Contracting out

- Cannot contract out of basis clause provision or if policyholder is consumer (warranties/fraud) unless favourable to consumer
- If a term places a business policyholder in a worse position then insurers must:
 - Take sufficient steps to bring term to policyholder's attention; and
 - Ensure term is clear and unambiguous
- Flexible test. More required for SME/direct sales than for broked or sophisticated market.

Insurance Act 2015

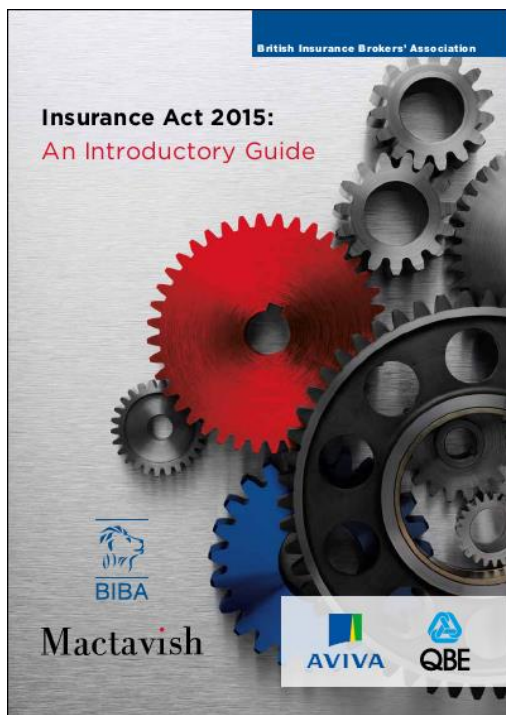
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Insurance Act 2015

Implementation Challenges

- BIBA/Mactavish Guide: Part One (Introduction)
- Critical summary of what the Act **does**



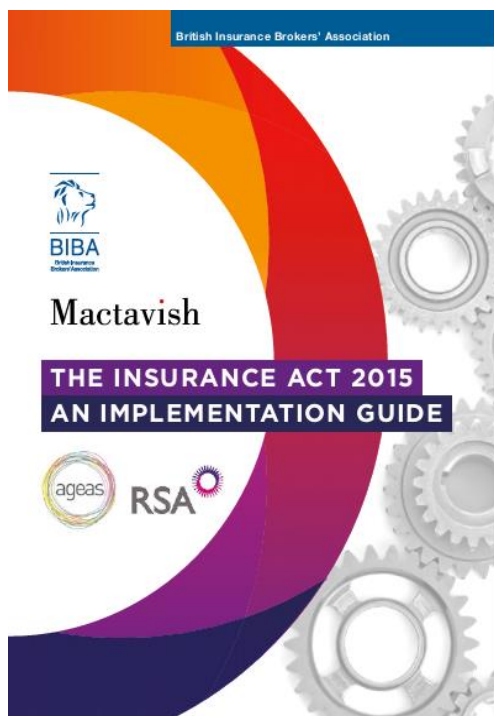
BIBA/Mactavish – Introductory Guide:

- Explaining the key changes within the Act
 1. Duty of Fair Presentation
 2. Warranties & Conditions
 3. Fraudulent Claims
 4. Contracting Out
- What insureds need to consider
- Support brokers should seek from insurers
- Broker toolkit

Insurance Act 2015

Implementation Challenges

- BIBA/Mactavish Guide: Part Two (Implementation)
- Critical guidance on what each party **needs to do**



BIBA/Mactavish – Implementation Guide:

- Challenges of implementation
 1. Devil in the detail
 2. Fair Presentation & Reasonable Search
 3. Warranties & Conditions
 4. Contracting Out
- Implementation measures: a blueprint for customers, brokers and insurers
- Broker toolkit updated

Insurance Act 2015

FERMA - Changes in UK Insurance Law

- FERMA/Mactavish Introduction to the Insurance Act 2015 for European businesses



FERMA/Mactavish – IA 2015 Introduction:

➤ Key aspects of the Act

1. The duty of Fair Presentation
2. Warranties and other conditions
3. Third parties rights and remedies for fraud
4. Contracting out

➤ Key considerations for European businesses

Agenda

1. Recap of the Duty of Fair Presentation
2. Sample challenges: understanding the nuances of the Act
3. Sample solutions: focus on Duty of Fair Presentation
4. Enterprise Act 2016
5. Open discussion

The Duty of Fair Presentation

Customer Knowledge

What **MUST** be actively disclosed

Knowledge of senior management

Knowledge of the insurance team, including brokers

Information reasonably revealed by a reasonable search

A fair presentation of the risk requires clear and accessible disclosure, without material misrepresentation, of:

Every material circumstance which the insured knows/ought to know:

Or, failing that,

Sufficient information to put a prudent insurer on notice that it needs to make further enquiries to reveal those material circumstances.

Customer Knowledge

NOT required to be disclosed

Information held by the insurer and accessible to the underwriter relevant to the risk

What an insurer writing this type of risk would reasonably be expected to know

Common knowledge

Key Point 1 – Senior Management

- “Senior management” is defined as “*those individuals who play significant roles in making decisions about how the insured’s activities are to be managed or organised*”
- Those key words “to be” are very significant. It may be that it is not management or organisation of the activities themselves that count - it is decisions as to how activities are “to be” managed or organised. That suggests a higher level of management
- That may include influential investors, private equity / hedge fund investors, JV partners, influential non-executives, etc. It has been defined as a matter of influence to capture shadow directors.

Key Point 2 – Controlling Mind or Will

- The senior management definition is aimed at including the controlling mind or will of the organisation
- If the board know (or any member of the board knows) material circumstances, these should be disclosed
- It should be no excuse that the board concealed information from their risk manager or broker.

Key Point 3 – Disclose Breaches of Conditions

- Since, under the old law, a breach of warranty would discharge all insurer liability, disclosure of facts relating to a breach of warranty by the customer (as at the time of contracting) was generally not required
- The new Act makes warranties suspensory (i.e. the insurer is again liable once the breach is rectified, where the breach is capable of being rectified), which is obviously of benefit
- However, facts relevant to the insured's propensity to breach a warranty (or, indeed, any condition tending to mitigate risk) might now be material for the purpose of fair presentation. This would be a demanding departure from current practices.

Key Point 4 – Clear & Accessible

- If information isn't clear and accessible we may see a new trend of insurers asking for information to be re-presented. Otherwise the insurer may waive their rights
- LMA / IUA guide: *“The central change brought about by the introduction of proportionate remedies is an increase in the importance and complexity of inducement. The actual underwriter will, in certain cases, have to prove that he was induced to a much finer degree ... The importance of keeping thorough underwriting notes and records will become even more important, since often these will indicate which matters particularly influenced the underwriting decision, and as to the way in which the underwriter thought about the risk.”*

Key Point 5 – Reasonable Search

- LMA / IUA guide: *“Knowledge that should be revealed by a “reasonable search” is probably a broader category than knowledge the insured ought to know “in the ordinary course of business” (although this is far from certain, and remains to be seen). That is because the express language of the Act does not delimit the potential repositories of information which is to be subject to a reasonable search. The information does not need to be in the possession or control of the insured”*
- *“This means that the scale and scope of a reasonable search is likely to vary even within the same class of risk depending upon, for example, the sum insured, since it may well be reasonable to require a wider search where the sum insured is significantly greater.”*

Key Point 6 – Reasonable Search & 3rd Parties

- Reasonable search potentially encompasses any third parties who hold information about the insured, whether or not they are involved in procuring the insured's insurance. The limit depends on how far it is reasonable for the search to extend
- Policyholders may therefore have to make enquiries of agents such as brokers, lawyers and technical advisors who may hold information relevant to the risk
- Which agents should be included in the search will vary depending on the circumstances and the type of insurance. An insured's solicitor may have information relevant to a professional indemnity policy but not a building and contents policy.

Key Point 7 – Beneficiaries of Policies

- The Act states that a reasonable search should include information available to the insured's organisation or "*held by any other person (such as the insured's agent or a person for whom cover is provided by the contract of insurance)*"
- In some cases, particularly in a Directors' and Officers' insurance or similar liability context, or where a group of companies and contractor interest are being insured, this requirement may become very demanding if there are a large number of potential beneficiaries
- We expect the Courts to apply caution by class of insurance.

Key Point 8 – Terms Tending to Reduce Risk

- The Act presents contracting parties and Courts with a new challenge. They will have to determine whether a term concerns loss of a particular kind or loss at a particular time or location, or whether it defines the risk as a whole. If the latter then section 11 does not apply
- If section 11 applies, the insurer cannot rely on non-compliance if the insured shows that it “**could not** have *increased the risk of the loss which actually occurred in the circumstances in which it occurred.*”
- In the event of a claim the changes may result in more protracted negotiation (as opposed to straightforward repudiation of a claim or a rapid settlement negotiation based on the insurer’s contractual rights).

Key Point 9 – Post Loss Conditions Precedent

- Despite the Act, there is still potential for “technical” defences
- “Post loss” conditions precedent to liability requiring, for example, notification within specified periods are still enforceable
- A technical breach of such conditions can still result in the loss of claims (e.g. notification outside the specified time limit, even if no prejudice is caused).

Key Point 10 – Contracting Out Example

- The Act doesn't require the insurer to say that something is actually contracting out. And it isn't obliged to explain to the customer, if it has explained to the broker
- An insurer writing “LMA 5260/5258” may suffice
- LMA 5258 – would mean that even if a warranty breach is rectified the policy remains invalid (contracts out of all s.10)
- LMA 5260 – could mean that even an irrelevant breach of a warranty or condition precedent might invalidate the whole policy or avoid liability for a claim (contracts out of s.11).

IA 2015 – Fair Presentation Implementation

Insurance Act 2015 - Areas of focus for policyholders

- Mactavish is working with many clients on FP compliance measures, ranging from fairly obvious “good practice” to some fairly advanced measures (see guide)

Reasonable Search

Clear & Accessible Presentation

“Good Practice”

- Documenting who & what is involved in gathering risk information
- Updating guidance to contributors on their responsibilities under IA 2015
- Tailoring search to specific risk scenarios

- Indexing & signposting
- Emphasising known risk concerns, e.g. new sub-deductible trends

“Added Value”

- Clarifying what “sign-off” means at each level of the business involved
- Reassessing adequacy of sources
- Review of scope of a) involved personnel and b) broker / third party knowledge

- Bespoke guidance to help u/w through wider risk context, e.g. website specifics, risk policy detail
- Ongoing appraisal of operations and risk to identify/flag “unusual” factors

“Market Leaders”

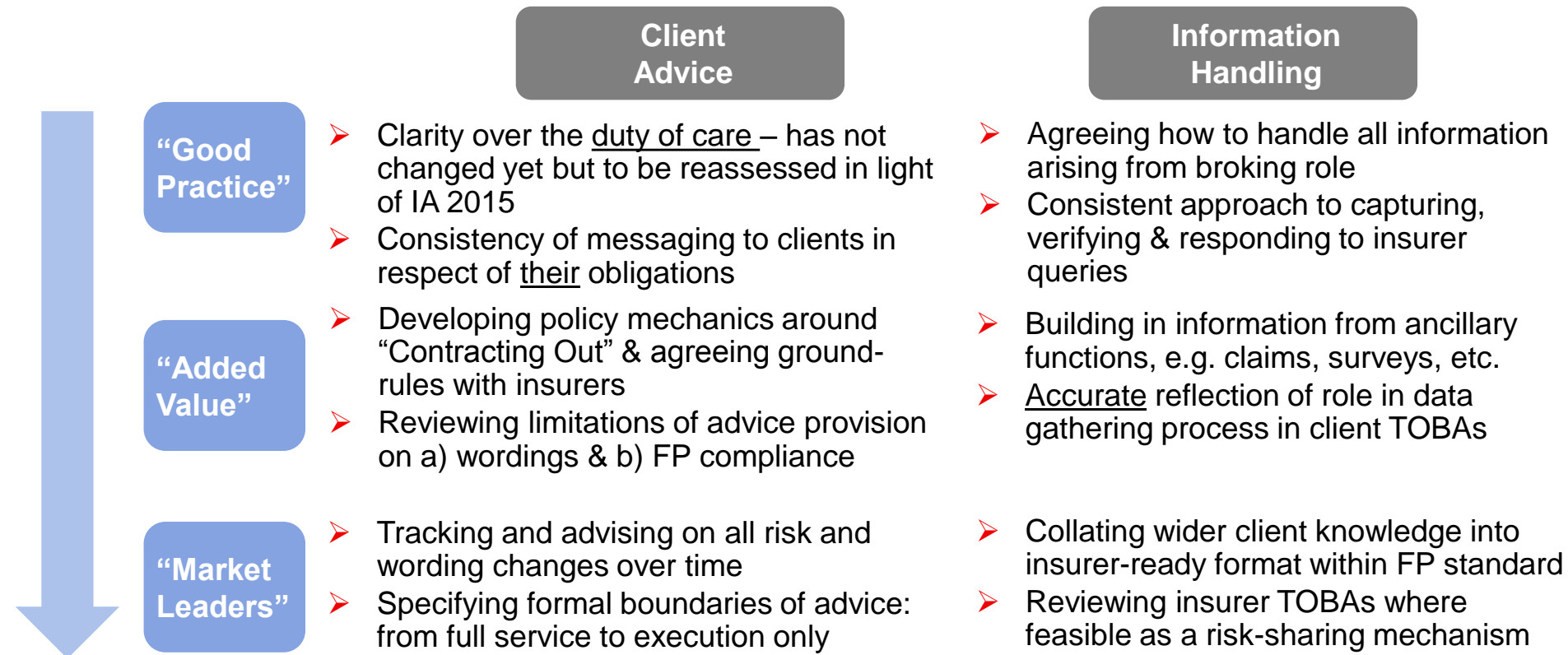
- Bespoke risk enquiries into complex aspects of business beyond the traditional dataset
- Agreeing senior management and/or search limitations with key insurers
- Automating senior “sign-off” within the IT tools used for information gathering

- Additional checkpoints to stress-test clarity of information with wider internal audience
- Highlighting specific gaps in information for insurer appraisal

IA 2015 – Fair Presentation Implementation

Insurance Act 2015 - Areas of focus for brokers

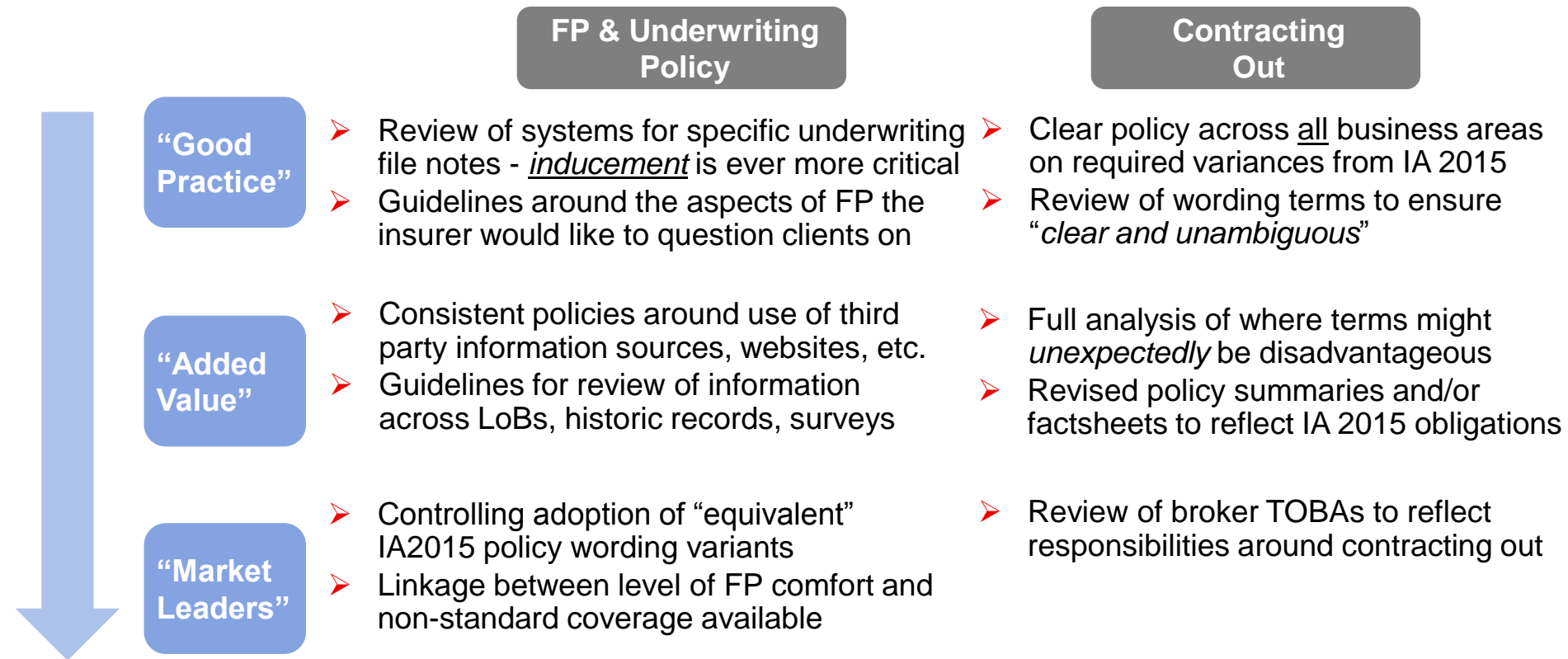
- Mactavish is also working with brokers (often at policyholders' request) and it is clear that operating enhancements should be requested of them by the FP compliant buyer



IA 2015 – Fair Presentation Implementation

Insurance Act 2015 - Areas of focus for insurers

- Corresponding insurer challenges are also detailed in the guide – partly relevant to any AIRMIC buyers with a captive...



IA 2015 – Fair Presentation Implementation

Insurance Act 2015 - Captive Implications

The captive challenge arises from duality of roles – where captives must consider their revised obligations as both buyer and seller:

Captive as insurer: Mitigating Captive Risk



- Ensuring adequacy of u/w enquiries and filenotes as a new Act-driven requirement for 'substance'
- Reviewing captive-driven policy wordings for Act compliance and sufficiently of 'contracting out'
- Ensuring captive access to the full set of underwriting information

Captive as customer: Mitigating Captive Risk



- Potential for unique disclosable knowledge (e.g. low-level claims)
- Develop captive-specific answers to core questions around FP:
 - Captive 'senior management'?
 - Relevant external service providers to the captive with material knowledge?

Enterprise Act 2016

Enterprise Act 2016 - Introduction

- The Enterprise Act: an add-on to the IA 2015. Incepts 4th May 2017
- Critical benefit for policyholders arising from the 'damages for late payment' provision:
 - Damages available if the client business suffers or fails, if the insurer acts unreasonably in denying or delaying payment of a claim
- However, constituent client obligations will challenge:
 - Have to mitigate loss, e.g. by raising other funding where viable
 - Must demonstrate that damages were foreseeable to the insurer at point of placement
 - Have to contemporaneously record where damages are incurred
- Contracting out – any insurer caps on consequential damages will trigger obligations defined under the IA 2015.

Enterprise Act 2016

Enterprise Act 2016 - Mactavish led negotiation

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17 November 2015

Baroness Neville-Rolfe DBE CMG
Department of Business, Innovation & Skills
1 Victoria Street
London SW1H 0ET

By email: mpst.neville-rolfe@bis.gsi.gov.uk

Dear Baroness Neville-Rolfe

Re Clauses 20 and 21 of the Enterprise Bill 2015 ("Damages for Late Payment of Insurance Claims")

The London Insurance market has expressed concerns about clauses 20 and 21 of the Enterprise Bill and some possible amendments were tabled before the Grand Committee of the House of Lords. These clauses of the Enterprise Bill as they stand now are based on work carried out by the Law Commission and were otherwise widely supported by the insurance market, brokers and policyholders.

In order to address the concerns of the London Market and to assist the future progress of the Bill, Mactavish (a leading firm of insurance governance experts) commissioned an independent opinion from a leading insurance QC.

Counsel generally supported the work of the Law Commissions and the two clauses in the Enterprise Bill. However counsel made two recommendations regarding clause 20. These are:-

1. A sentence at the end of what is to be section 13A(4) of the Insurance Act 2015 to deal with the question of legal privilege; and
2. Subsections (3) and (4) to create a special limitation period for claims for breach of the implied term.

The first recommendation will make it easier to resist speculative litigation and the second will provide insurers with some finality over their exposure and allow them to close their account for a claim without having to make provision for further claims over an uncertain period of time. We have attached the full text of the proposed amendments to this letter. A copy of counsel's opinion is also attached.

Enterprise Act 2016: Mactavish Negotiation

- Damages for late payment legislation
- Removed from IA 2015 but brought back in by the UK Government in the Enterprise Bill
- Described as a line which insurers would not cross
- Mactavish asked to negotiate industry agreement

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Enterprise Act 2016

Enterprise Act 2016 - Market agreement and significance

We are pleased to confirm that these amendments would ameliorate the concerns of London Market insurers and are agreed by all the signatories to this letter who represent the vast majority of the insurers, brokers and commercial policyholders in the UK insurance market. In our collective view both suggestions improve the current draft of clauses 20 and 21 of the Enterprise Bill without altering the substance. On the basis of these proposals, the LMA and IUA would not encourage the tabling of further amendments to clauses 20 or 21 of the Bill. We hope that these amendments will be supported by the Government.

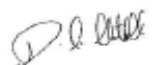
If you would like to discuss anything in this letter further we would of course be happy to do so.

Yours sincerely



Bruce Hepburn
CEO
Mactavish

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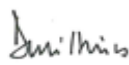


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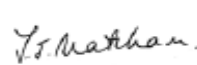
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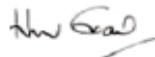
Steve White
CEO
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Association




David Gittings
CEO
Lloyd's Market Association



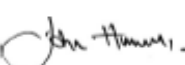
Dave Matcham
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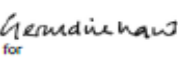
Huw Evans
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Enterprise Act 2016: Mactavish Negotiation

- Mactavish led the negotiation and engaged the top insurance QC in the country
- Legislation amended with widespread market support and signatories
- Landmark success for policyholders
- Achieved Royal Assent on the 4th May 2016 and will come into force on 4th May 2017

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IA 2015 & Fair Presentation Implementation

Panel Q&A
