The Insurance Act 2015 (the ‘Act’) received Royal Assent on 12 February, 2015 and will come into force on 12 August, 2016. Along with the consumer insurance reforms that came into effect in 2013, it represents the most significant change to insurance contract law in this country for over 100 years.

The legislation is seeking to create a new and fairer balance between policyholder and insurer. The main provisions of the Act give effect, with some modifications, to the recommendations made in July 2014 by the Law Commission and Scottish Law Commission.

The changes will have a significant impact on how insureds and insurers approach policies, creating new duties for insurers and policyholders to comply with.

The Act deals with:
- Duty of disclosure, both before a contract incepts and when amended
- Warranties (including basis of contract clauses)
- Terms not relevant to the actual loss
- Fraudulent claims by insureds
- Good faith
- Amendments to the Third Parties (Rights Against Insurers) Act 2010

It is important to note that (with one or two exceptions), the Act sets a default regime and allows insurers to contract out of important elements of the Act for non-consumers as long as it is done in a ‘transparent’ manner.

IN MORE DETAIL
The Insurance Act 2015 reforms the law in relation to non-consumer policyholders.

A ‘consumer’ in this context refers to insureds who are individuals that purchase insurance which is unrelated to their trade, business or profession.

The Act applies to both business and consumer insurance, although the new duty to make a fair presentation only applies to business insurance contracts with the consumer equivalent dealt with under the Consumer Insurance (Disclosures and Representations) Act 2012.

Reinsurance and retrocession
Contracts of reinsurance and retrocession are treated as contracts of insurance at common law and are non-consumer insurance contracts for the purposes of the Act. In such contracts, the party purchasing the insurance (the insurer or the reinsurer) is the ‘insured’ for the purposes of the Act, and the party providing the insurance (the reinsurer or the retrocessionaire) is the ‘insurer’.

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1 Technical provisions not specifically addressed in this note
HOW THE ACT APPLIES

The new law, rather than being a rigid code, sets out principles to be followed, with the aim of being sufficiently flexible to cater for the smallest business to major corporations.

The Act applies to England, Wales, Scotland and Northern Ireland, but in respect of Northern Ireland there is a modification relating to road traffic legislation, so in practice any policy which is subject to the law and jurisdiction of these territories will be governed by the Act.

The Act will not apply retrospectively, so will only apply in the following way:

- The new duty of fair presentation and the new effect of a breach of the duty of good faith would apply only in relation to contracts of insurance entered into on or after 12 August, 2016 and to variations agreed on or after 12 August, 2016 in respect of contracts agreed at any time.

- The new law on warranties, terms not relevant to the actual loss and fraudulent claims will apply only in relation to contracts of insurance entered into on or after 12 August, 2016, and to variations of such contracts.
THE DUTY OF FAIR PRESENTATION
FOR NON-CONSUMERS

The Act updates and replaces the existing ‘Duty of Disclosure’, the duty on non-consumer policyholders to disclose risk information to insurers before entering into an insurance contract.

The Act brings much-needed clarity around what information a purchaser of insurance has to provide to the insurer, which of their staff is responsible for doing that and to whom they have to provide it.

The new duty is now described as a ‘duty of fair presentation’, effectively requiring non-consumer policyholders to undertake a reasonable search of information available to them, and defining what a policyholder knows or ought to know.

It is important to note that ‘entering into an insurance contract’ includes not only the main policy and each renewal of it, but any variations or amendments. Each time a contract is varied, the duty arises afresh in relation to that variation.

WHAT IS A ‘FAIR PRESENTATION’?

A fair presentation of the risk is one that meets the following criteria:

1. Disclosure of every material circumstance which the insured knows or ought to know, or failing that, disclosure which gives the insurer sufficient information to put a prudent insurer on notice that it needs to make further enquiries for the purpose of revealing those material circumstances.

2. Disclosure in a manner which would be reasonably clear and accessible to a prudent insurer.

3. Every material representation as to a matter of fact is substantially correct, and every material representation as to a matter of expectation or belief is made in good faith.

The duty on non-consumer insureds to volunteer information is therefore being retained, albeit in a different way, unlike the position for consumer policies.

The Law Commissions were critical of the practice of unnecessarily complex presentations and ‘data dumping’, where important information could be hidden within a mass of other material. This results in the requirement that, disclosure must be ‘in a manner which would be reasonably clear and accessible to a prudent underwriter’ (section 3(3)(b) of the Act).

However, the Act states that a ‘fair presentation’ does not have to be made in a single document or oral presentation. This is intended to recognise that the insurer may need to ask questions about the information in the initial presentation in order to draw out the information it requires to make the underwriting decision, so there may be a series of exchanges. All information which has been provided to the insurer by the time the contract is entered into will therefore form part of the presentation to be assessed for the purposes of considering whether or not the presentation is fair.
The insurer's knowledge?
It is not necessary to disclose matters of which the insurer is already aware or is deemed to be aware, nor any matter which diminishes the risk. The Act creates a positive duty of inquiry for the insurer. Clause 5(2) sets out two types of information which an insurer 'ought to know' and is therefore deemed to know:

- The first, in clause 5(2)(a), is information which an employee or agent of the insurer knows and ought reasonably to have passed on to the underwriter. This is intended to include, for example, information held by the claims department or reports produced by surveyors or medical experts for the purpose of assessing the risk.

- The second category, clause 5(2)(b), is intended to require the relevant underwriter to make a reasonable effort to search such information as is available to them within the insurer’s organisation, such as in the insurer’s electronic records.

An insurer will also be presumed to know things which are common knowledge, or which an insurer offering insurance of the class in question to insureds in the field of activity in question would be expected to know in the ordinary course of business.

Whose knowledge is relevant?
In a large corporate entity, whose knowledge counts? Under the Act, when deciding what an insured knows, what matters is the knowledge of senior management (which will include the board of directors, but also those who play significant roles in the making of decisions about how the insured’s activities are to be managed or organised) and of those responsible for arranging the insurance.

What knowledge?
The Act sets out what an insured ought to know. An insured must carry out a reasonable search for information, with what is reasonable depending on the size, nature and complexity of the business. The insured will be deemed to know what 'should reasonably have been revealed by a reasonable search' (section 4(6) of the Act) and so information held by non-senior management (but by those who, say, perform a managerial role) may still be imputed to the insured where it would have been reasonable for the insured to seek out that information. Relevant information held by any other person (even those outside the company, such as the company’s agents or beneficiaries of cover) will also be imputed to the insured if a reasonable search should have revealed that information.

The Broker’s knowledge?
The insured’s knowledge specifically does not include confidential information acquired by the insured’s agent (for example, its broker) through a business relationship with someone other than the insured who is not connected with the insurance. It will include knowledge the broker has obtained through its relationship with insured.

IN MORE DETAIL

What does the insured know?
The law has always, as a matter of fairness, determined that an insured knows not only what it actually knows but also information to which it has knowingly turned a blind eye (i.e. not enquiring because the insured knows the answer will be damaging). The insured is also taken to have known what it ought to know and this idea is developed by the Act.
REMEDIES

Importantly, the Act introduces an entirely new system of proportionate remedies where the duty to make a fair presentation has been breached. The remedy of avoidance for a breach of the duty of utmost good faith is abolished, although the ability to avoid will be retained in some cases where the insured breaches the duty to make a fair presentation in relation to disclosure/misrepresentation – see below.

REMEDIES FOR MATERIAL NON-DISCLOSURE OR MISREPRESENTATION

Avoidance: Deliberate or reckless breaches

If a qualifying breach was deliberate or reckless, the insurer:

(a) may avoid the contract and refuse all claims, and
(b) need not return any of the premiums paid.

For example, an insured deliberately conceals known and material information from its presentation of the risk and does not even provide sufficient information to put the insurer on enquiry, making it an unfair presentation. This entitles avoidance but with no obligation to return premium.

Proportionate Remedies: non-deliberate or non-reckless breaches

In all other cases (even where the insured has made an innocent mistake), the following proportionate remedies will apply, all being based on what the insurer would have done had it known the true facts:

1. If the insurer would not have entered into the contract on any terms: the insurer may avoid the contract and refuse all claims but must in that event return the premiums paid.

2. If the insurer would have entered into the contract but on different terms (other than terms relating to the premium): the contract is to be treated as if it had been entered into on those different terms if the insurer so requires, even if the insured would never have accepted such terms.

3. In addition, if the insurer would have entered into the contract but would have charged a higher premium (whether the terms relating to matters other than the premium would have been the same or different): the insurer may reduce proportionately the amount to be paid on a claim.

In sub-paragraph (3) above, ‘reduce proportionately’ means that the insurer need only pay on the claim X% of what it would otherwise have been under the terms of the contract (or, if applicable, under the different terms provided for by virtue of paragraph 2, because 2 and 3 can apply together). The calculation is as follows:

\[ X = \frac{\text{Premium actually charged}}{\text{Higher Premium}} \times 100 \]

Any breach for which the insurer has a remedy under the Act against the insured is referred to as a ‘qualifying’ breach.
WARRANTIES AND OTHER TERMS

Under the current law, breach of a warranty in an insurance contract automatically discharges the insurer from liability completely from that point onwards, even if the breach is remedied.

An insurer may avoid liability even if the breached term was entirely unrelated to the type of loss occurring which was actually suffered (for example, a warranty to maintain a working burglar alarm would be unconnected with a flood to the insured premises caused by extreme weather conditions).

Under the new Act breaches of warranty can be cured; all warranties will become ‘suspensive conditions’ (section 10 of the Act). This means that cover is suspended for the period during which the warranty is not complied with. Furthermore, this means that an insurer will be liable for losses that take place after a breach of warranty has been remedied, assuming that a remedy is possible.

Therefore, for example, if an insured breaches a warranty that roof structures will be inspected every six months, that breach will be ‘remedied’ if the roof is inspected after seven months, and so coverage will be suspended for only one month in such circumstances. A loss resulting from a cause that would have been prevented if an inspection had taken place will not be covered if it occurred in that one month suspensive period.

IN MORE DETAIL

Relevant connection between breach and loss claimed:

In addition, the Act (under section 11 ‘Terms not relevant to the actual loss’) now requires a relevant connection between the breach of any term (including warranties) the underwriter has imposed to reduce the risk of loss of a particular kind and the actual loss that occurred, in the circumstances in which it occurred.

So, even if a roof inspection warranty (or indeed a roof inspection condition precedent) was not complied with, if it has no connection with a subsequent claim for an electrical fire, the insurer cannot rely on the breach of roof inspection warranty to avoid liability for that fire claim. The onus is on the insured to demonstrate the lack of any relevant connection. A direct causal link between the breach and the actual loss is not required.

However, this does not apply to terms which ‘define the risk as a whole’. An insured, for example, having a term which restricts the use to which insured property can be used to commercial use as opposed to private use (which term might be argued to reduce the risk of losses more usually associated with residential properties) is unaffected by this requirement. A property within the portfolio used residentially would therefore continue to be excluded from cover, regardless as to whether or not this use had any connection with the actual loss occurring.
**ABOLITION OF ‘BASES OF THE CONTRACT’ CLAUSES**

Basis of the contract clauses will be prohibited (as is already the case now for consumer contracts) and it will not be possible for business insurers to contract out of this particular change (section 9 of the Act).

These clauses purport to have the effect of converting pre-contractual information supplied to insurers into warranties. Thus any provision in a proposal form which purports to convert answers in the proposal into a warranty will be ineffective.

**INSURERS’ REMEDIES FOR FRAUDULENT CLAIMS**

The Act provides the insurer with clear statutory remedies when a policyholder submits a fraudulent claim. If a claim is tainted by fraud, the policyholder forfeits the whole claim, they cannot recover the part of the claim that would genuinely have been payable.

The Act also provides that the insurer may refuse any claim arising after the fraudulent act and can serve notice that it is treating the contract as terminated from the date the offence was committed. However, previous valid claims arising prior to the fraudulent act are unaffected.

The insurer need not return premium following notice of termination based upon the submission of a fraudulent claim.

**Group insurances and fraudulent claims.** The Act makes special provision for situations in which a member of a group insurance policy (i.e. a policy arranged by one insured for a number of insureds, such as a Group of companies) makes a fraudulent claim.

Where this happens, the insurer will have a remedy against the fraudulent member but it will not affect the other members or the insurance policy as a whole – cover will remain in place for the other ‘innocent’ beneficiaries. If an insurer wants to contract out of this provision, it must comply with the transparency requirements to bring that to the attention of the group company beneficiaries.

**GOOD FAITH**

The Act removes the remedy of avoidance of the contract for breach of the duty of good faith in section 17 of the 1906 Marine Insurance Act (which applies to all types of insurance, marine or not), and any equivalent common law rule. See above for the replacement remedies for qualifying breaches.

**CONTRACTING OUT**

For non-consumer insurance, the provisions of the Act are intended to provide default rules. However, parties are free to agree contract terms which are less favourable than those in the Act, provided that the insurer satisfies two transparency requirements. This ability to contract out is not true of consumer insurance contracts. An insurer will not be able to use a contractual term to put a consumer in a worse position than they would be in under the terms of the Act.

**IN MORE DETAIL**

**What are the transparency requirements for contracting out?**

Where insurers do intend to opt out (and hence include a ‘disadvantageous term’), they must take sufficient steps:

- To draw it to the insured’s attention before the contract is entered into, and
- The disadvantageous term must be ‘clear and unambiguous as to its effect’.

What is sufficient to meet the above two requirements will depend on the characteristics of the insured and the circumstances of the transaction (where and how is the contract made).

**What cannot be contracted out?**

The contracting-out provisions will not apply to settlement agreements or the prohibition in respect of basis of the contract clauses.
CONCLUSION
The Act provides a new framework for business insurance contracts and as with all new legislation it will be for the Courts to interpret the new law.

While it is likely that a period of uncertainty will ensue after implementation of the new law, it does appear that the Act goes some way to redressing the imbalance under the current law between the interests of the insured and insurers.

Willis will continue to work with the government and our partners on any further reforms. We will issue a follow-up to this bulletin once more information has become available, which will cover the practical considerations of the Act. For example, how to make a fair presentation, the benefits and disadvantages of contracting out of the Act (including any alternative arrangements) and a discussion of insurers’ responses to the Act.

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