The Insurance Institute of Manchester

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The New Class 2015-2016 Report 2: The Insurance Act 2015

The Effect on Brokers

The Insurance Act 2015
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Meet The New Class

During the summer of 2015, the Insurance Institute of Manchester was inundated with applications from candidates eager to achieve a place on 'The New Class 2015' programme, lead by Stephen Bridge ACII from the council. Sixteen successful candidates were selected to participate in a tailored training programme, sponsored by LV=, to help them develop both themselves and the industry.

Under the guidance of institute vice presidents, Fintan Griffin ACII and Karen Cartridge Dip CII, the teams engaged in soft skills sessions including public speaking, report writing and project management. The group, split into two teams, had to then utilise these skills to create a report based on the implementation of the Insurance Act 2015, for release August 2016.

The following report has been created by 'Team Fintan' focusing on the effect on brokers.

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Katie Heathcote – Marsh Ltd
Gemma Mullins - Thompson Brothers Insurance Consultants Ltd
Tom Rolph - HSB Engineering Insurance
Clare Warrington – LV
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Introduction

"My thoughts around the act are that brokers need to be getting ***more involved*** *with this and not burying their head in the sand, assuming the changes are only going to impact insurers.*

Management need to ***accept these changes*** *and engage with staff to effectively alter working practices in a way that gets the best* ***result for clients****, whilst making sure that insurers are happy with the process.*

Specialist brokers who really understand their clients businesses are going to find this much easier than general brokers with no knowledge of the client or how they operate. Engagement from key insurers' partners is needed with this process and will remain vital to keep good relationships in place.

Consideration needs to be given to ***how information is provided to the client*** *on the act, how they are able to review the submission made to insurers on their behalf and how we evidence this. This is likely to vary between departments due to the number of insurers traded with, type of clients and complexity of their businesses."*

Katie Jackson ACII, Bollington Insurance Brokers 2016, IIM President

Background to The Insurance Act 2015

Insurance law has largely developed from The Marine Act 1906. In this Act the principle of utmost good faith was developed. This has dominated how insurance has operated for over 100 years.

Under this Act insured parties were required to disclose every circumstance that they knew, or ought to have known, so an insurer could decide on a premium, or if they wanted to underwrite the risk at all. This meant insured parties had to predict what to disclose without much guidance. This also extended to brokers acting on behalf of insured parties.

In 2006 the Law Commission was asked to consider if the existing insurance law regime in the UK was still fit for purpose. It was found that it was not as there is distrust and a lack of confidence in insurance companies. The 1906 Act gave insurers wide-ranging opportunities to avoid insurance policies at any sign of wrong doing by the customer.

Recent Acts of parliament have led to there being significant changes in the way disclosure is dealt with. The first of these acts being the Consumer Insurance (Disclosure & Representation) Act 2012. This covered consumer insurance bought by individuals only and made them exempt from the duty of disclosure. This Act does not affect commercial customers meaning the principle of utmost good faith continued to apply.

The Insurance Act 2015 was developed to develop disclosure for commercial customers. This comes into effect on 12th August 2016. This Act seeks to modernise the way the insurance industry operates and improve how the public and customers view it.

The Act will make it harder for insurers to avoid claims as a result of technical breaches by the insured, as well as clarifying and specifying what information is to be known or presumed.

Key areas the Act relates to:

- Duty of Fair Presentation
- Warranties
- Fraud

Fair Presentation

From the 12th August 2016, the Insurance Act 2015 will replace and take over the Marine Act which has not evolved since 1906. Part of the Act will focus on the disclosure requirements of material facts for commercial clients. Currently the duty is on the customer to disclose all material facts however the new Act will extend this principle and bring in a new duty called ‘duty of fair presentation'.

What is a fair presentation?

This is defined in the new Act as a presentation which:

a. Is reasonably clear and accessible to a prudent insurer
b. Does not try to hide or sugar coat important information which should be brought to their attention
c. Does NOT data dump
d. Extends the duty to disclose all material facts to the intermediary, making it a joint responsibility

Why is it good?

- Under the old Act, insurers could easily hide behind the safety net of the wording ‘disclosure of all material facts’ and throw out claims on the grounds they were not made aware of something. Customers were expected to be inside the mind of the insurer. As we all know, this is a complicated industry and many customers may struggle to understand what to disclose and what not to disclose
- An intermediary (broker), given their expertise and experience, can advise customers on what is to be disclosed and what is not

Why is it bad?

- More onus is on the broker now, the safety net insurers once had is merely replaced with another
- Unfairly disputed claims due to non-disclosure can now be blamed on the broker, meaning potential Professional Indemnity (PI) claims and loss of business due to customer-broker relationship breakdowns

Brokers need not worry

- This Act, although it appears to be a bit scary for the brokers, really only emphasises the work brokers and insurers are already doing:
  - Brokers have presentation templates they use to provide insurers with information surrounding existing and new business cases
  - Brokers already have annual reviews with their clients to discuss any changes to the risk
  -Brokers have relationships with insurers which builds trust between the two parties, meaning each has an interest in getting the risk on cover right

- Insurers assist the brokers with proposal forms and will ask questions to gather more information upon receipt of risk presentations

- If it does get to the point whereby a claim is disputed as a result of non-disclosure, brokers have the support of their own PI insurance, it will be up to the insurers or the customers to prove the broker did not fulfil their role
- Customers also have the support and backing of the Ombudsman which has had great success in the past assisting customers with disputed claims

"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."

Willis Technical Insight Document

Fraud

"There are still some players who don't behave in the manner they should…
The Insurance Act should stop people behaving in that way"

David Williams, Technical Director, Axa

In relation to fraud the new Insurance Act 2015 applies to both the consumer and commercial contracts of insurance. It sets out best practice for both insurers and brokers with fraudulent claims.

Within the Act it states that insurers are not liable for any part of a claim that is tainted by fraud. The insured only needs to be fraudulent in one area of the claim for the whole claim to be avoided.

Under the Marine Act, insurers would have to void the policy from inception and give all monies back. However under the new Insurance Act 2015 insurers may void the policy from the time of the fraudulent act and not inception. They may also keep all the premium paid and avoid all future claims.

For insurers this is a great addition to the Act. On the other hand for brokers there is a risk of being left with a bad debt, whereby they have settled their account with the insurer but have allowed the insured to pay over a finance agreement. The insured then stops paying once they have been voided. This leaves the broker out of pocket. It will then be up to the broker to pursue the insured to recover their monies owed.

Whether the broker is left out of pocket or not will depend on the terms agreed with the insurer in the Terms of Business Agreement (TOBA). Within the TOBA there could be an agreement whereby the debt is written off if the broker is unable to collect the monies owed in this circumstance.

Another drawback is if an insured has submitted multiple fraudulent claims then it is up to the broker and insurer to prove that all claims are fraudulent if they can prove that only the last claim is fraudulent then all other claims remain valid and paid.

Warranties

A warranty is a term in a contract that must be complied with by the insured. Warranties will still be included in policies; however the Act has changed how insurers deal with breaches, this is demonstrated in the scenarios below. This puts new responsibility on the broker in terms of information gathering, representation and disclosure to insurers.

Key Points – Current Law

Under the current law, a breach of warranty automatically discharges the insurer from liability from the date of breach, whether or not the breach is connected to the claim, resulting in the insurer no longer being responsible for the risk. Even if the breach of warranty was unconnected to the loss and can be remedied, the insurers can void the contract as the onus is on the insured to be compliant with the warranty throughout the policy period.

Insurance Act 2015

The Act no longer allows the insurer to avoid paying a claim when the breach is unconnected to the loss.

When there is a breach of warranty this will suspend the insurers liability from the date of breach up until it can be remedied. The insurer will therefore not be liable for any losses during this time. The new Act however will not allow insurers to use the 'basis of contract' term, meaning they can no longer contract out. This is demonstrated in the scenarios below:

Scenario A

A client, New Class Motors has an alarm warranty in place on their property policy and the following claims are made:

- The alarm is broken and the client fails to notify insurers
- The insured suffers a theft claim

Marine Act: the claim would not be covered and the insurer could avoid the policy from the date of the breach.

Insurance Act: the claim would still be declined, however the policy would not be avoidable and, once remedied, full cover would resume. This gives the policyholder time, when the insurer is off risk, to remedy the breach. If it can be remedied, the policy will resume cover from the date the breach is remedied.

Scenario B

A client, New Class Motors has an alarm warranty in place on their property policy and the following claims are made:

- The alarm is broken and the client fails to notify insurers
- The insured suffers a flood

Marine Act: the insurer could avoid the claim due to the breached warranty.

Insurance Act: no longer allows the insurer to avoid paying a claim when the breach is unconnected to the claim. Therefore the claim would be paid as the warranty was not connected to the loss. This is enhanced position for the insured as there now needs to be a connection between the loss and the breach. However, it is the insured's responsibility to satisfy insurers that the breach was immaterial to the loss.

Basis of contract

Policies and proposal forms contain a 'basis of contract' clause that states the answers or statements found in the proposal form or policy wording are true and accurate. The new Act will not allow insurers to use the 'basis of contract' term. This means that all warranties need to be agreed between the insured, the broker and the insurer prior to the commencement of the contract.

Prior to the Act if New Class Motors had declared on the proposal that they have a functioning alarm, the insurer would have the option to void the contract if the alarm was not functioning, as this proposal was the basis of contract. This would apply even when the breach was immaterial to the loss. Following the implementation of the Act, the insurer can no longer decline claims on this basis.

In theory, this will be advantageous to brokers as this will remove an element of doubt in terms of the payments of claims. Brokers will need to be vigilant with regards to the checking of policies and warranties and ensuring the client has a full understanding. Brokers must continue to make policyholders aware of conditions precedent as even though the Act has brought about changes, compliance with these has remained the same.

Contracting Out

The Act is likely to have a significant impact on the way insurance business is transacted within the insurance market place. Brokers will need to be particularly aware of implications on their clients and ensure previously mentioned amendments are made clear.

However insurers do have the option to 'contract out' of the new Act for parties of non-consumer insurance contracts, but what exactly does this mean and how will it affect brokers?

By electing to contract out, parties can avoid the requirements of the Act but only where any disadvantageous amendment is drawn to the insured's attention in an understandable and transparent way. This will impact brokers as they will have an immediate responsibility to ensure the client is fully aware of any policy terms contracted out. As such if an insurer was to notify the broker, and the broker subsequently fails to inform the client, the broker could be potentially exposed to a PI claim in the future. There is an industry consensus that brokers will need to be increasingly concise and measured in their communications with their clients or we could see a sharp increase in PI claims within the industry.

Under the new Act, breached warranties must be relevant to a loss for insurers to avoid a claim, whereas at the moment a claim can be declined whether a breached warranty is directly relevant to the loss or not. Insurers may seek to contract out when insuring exceptional and less favourable risks, to ensure all warranties are complied with unreservedly. This is one of the main reasons why the option to contract out has been made available. With the onus being on the client to strictly comply with any warranties; it’s a moot point that insurers may have been able to offer cheaper premiums under the remit of the old Marine Insurance Act. Furthermore, any circumspect broker may request two quotes, one under each Act to see premium differences.

Although in the industry we like to think clients look for the most suitable, comprehensive cover, we know this is not always the case and price plays a huge part in the decision. In a battle to win and retain business, brokers could contract out of the Act purely to offer discounted premiums, which is not necessarily why the option was made available. The underlying intention of the new Act is to avoid any ambiguity and the imposition of unfair interpretations by insisting upon greater disclosure and dialogue amongst parties prior to agreeing any contract.

The Changes

The way insurers respond to fraudulent claims	**The way breaches of warranty are handled**	**The duties in respect of disclosures and the remedies**
How clients gather their information in order to make a disclosure	**Changes in the way in which information is presented to an insurer**	**Changed duty of utmost good faith**

"Organisations will need to ensure they are able to satisfy the new law and that they have adequate and effective internal corporate governance and communication protocols in place"

Nigel Cooper FCII National Public Sector Leader, Aon

"It's far fairer, and I think explaining that to customers is part and parcel of the job we have as an industry."

Nick Smith, UK Underwriting Manager, Aviva UK.

Conclusion: Your 'To Do' List

Management

The Insurance Act comes into effect imminently and so it is vital that brokers incorporate this into their processes and culture of the business from the information gathering process to checking policy wordings. Management should lead from the front and provide training solutions and ongoing technical support and refresher sessions. Innovative solutions should be found for the amendment of processes, documentation and correspondence including Terms of Business Agreements. Around the table discussions on the act should be encouraged to ensure understanding.

Clients

Clients need to understand what is expected of them. This is an opportunity for brokers to strengthen relationships with clients by having a visible presence throughout the changes and guiding them through the next period of insurance and onwards with clear, bespoke and accurate communications. Although there is an obligation on our clients; guidance is key for brokers.

Example:

Ongoing minuted face to face discussions with clients at regular points

Employees

Employee understanding of the act is vital. Not only are employees the main point of communication for clients, they will also present information regarding a risk to insurers. Employees should follow the relevant procedures for presenting and gathering information as well as the escalation process when things go wrong. Employees should familiarise themselves with the brokers unique approach to the act and ensure training opportunities are taken.

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