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Dear Christina

## **Insurance contract law: Post contract duties and other issues**

This is the Financial Services Consumer Panel's response to the Law Commission and Scottish Law Commission's consultation on changing insurance contract law.

The Panel is broadly supportive of the proposals included in the consultation. In particular, we agree that the insurable interest requirements should be updated to better reflect modern family structures. We also support proposals to allow policyholders to seek damages for late payment of insurance claims. This reflects the wider position in contract law and the reliance consumers and businesses place on the timely payment of insurance claims.

The Panel is not best placed to answer the detailed questions included in the consultation. However, we do have some general observations on three key areas of the consultation: damages for late payment; insurers' remedies for fraud; and insurable interest for life insurance.

### **Damages for late payment**

The Panel supports the case for allowing policyholders to seek damages for late payment of insurance claims. Consumers and businesses rely on insurance to provide cover against financial loss. Where the insurance claim is unreasonably delayed, and leads to further financial loss, we believe it is fair and reasonable to expect the insurer to compensate for this additional loss. We also believe this requirement should be extended to claims that have been wrongfully rejected.

### **Excluding liability for decisions made in good faith**

The Panel strongly agrees that insurers should not be allowed to exclude liability for failing to pay valid claims on a personal lines insurance policy within a reasonable time period. Any such clause would be difficult for consumers to understand and would most likely be included in the lengthy terms and conditions which most consumers struggle to understand.

We can understand the motivation for allowing liability for decisions made in good faith to be excluded for commercial insurance policies. However, we are concerned that this could adversely affect the large number of small firms that do not have the level of 'in-house expertise' to understand the effect of this clause. We would prefer a ban on insurers excluding liability for failing to pay valid claims for all personal lines and commercial insurance policies.

### *Damages for distress and inconvenience in consumer insurance*

Consumers typically purchase an insurance policy to ensure they are protected should the worst happen. This is especially true of non-compulsory insurance products. Yet in some cases, when consumers come to make a legitimate claim, they find the policy does not provide the 'peace of mind' they had anticipated. The Panel therefore strongly agrees that consumers should have the right to seek damages for any distress and inconvenience caused when an insurer breaches the terms of their contract. This could include, for example, failing to handle a legitimate claim in line with the contract and consumer's reasonable expectations.

### *Limitation of actions in England and Wales*

The consultation sets out three potential options to determine when the six year time limit to commence litigation against an insurer for failing to pay a claim commences. The Panel believes consumers should have the maximum opportunity to make a claim. We therefore strongly support option (3) – *to provide that the time runs from when the insurer makes its decision*. It is only at this point that a consumer may realise they have reason to make a claim. We believe it would be unfair if the time, under which a claim should be made, has elapsed before the consumer was armed with the full information to enable them to bring a claim.

We recognise that there may be some uncertainty about when the insurer made its final decision due to the large volumes of correspondence exchanged on the more complex cases, so recommend that the time limit only starts when the final communication on the claim is received by the consumer.

### **Insurers' remedies for fraudulent claims**

Insurance fraud is not a victimless crime, with industry estimates suggesting this adds £50 to the cost of a personal lines general insurance policy. We therefore endorse the current position whereby any policyholder that commits fraud should forfeit the whole claim to which the fraud relates. We consider this an appropriate deterrent to discourage people from committing fraud and, where fraud is committed, a fair sanction.

### *A statutory restatement*

The Panel supports the position set out in the consultation including the clarification that where fraud is committed, this does not affect any previous valid claim. We believe it would be inappropriate to overturn previous claims on the basis of subsequent events, especially where the payment was made much earlier.

However, if as a result of the policyholder's fraudulent actions, the insurer investigates earlier claims and finds that these were also fraudulent, we believe it is important to clarify that the insurer is not precluded from seeking to recover these earlier payments.

The Panel agrees that a policyholder, who has committed insurance fraud, should forfeit any claim on their policy which arises after the date of the fraud. As this makes the policy worthless, we believe the insurer should simply cancel the contract and inform the consumer that they have done so.

### Group insurance

The Panel believes it is appropriate to give insurers the same remedies against a member of a group insurance scheme as if they were an individual policyholder. We also agree that it is essential that the fraudulent actions by one group member do not affect other members.

### **Insurable interest – life insurance**

The Panel supports the proposal to reform the insurable interest requirements. We believe this is essential to ensure insurance policies are able to meet the needs of consumers living in a range of family structures.

### Policies without insurable interest are void but not illegal

The Panel strongly supports the intention to make an insurance policy void, rather than illegal, where there is no insurable interest. We believe there should be greater onus on the insurer to make sure the proposer has an insurable interest in the life of the insured. This risk is currently borne by consumers, yet in most cases they do not have sufficient knowledge of insurance contract law to determine whether their circumstances meet the insurable interest test. Where a proposer has taken out a policy, which has later been found to fail the insurable interest test, we believe all premiums should be returned to the customer and not simply retained by the insurer.

### Insurable interest with economic loss

We favour broadening the definition of insurable interest to allow a proposer to take out an insurance policy on the life of an individual they are economically dependent on. The current legal requirement for the insured to have a legal obligation to the proposer is too restrictive. We therefore agree this should be based *on there being a real probability of economic loss on death of the person insured*. The Panel also believes that insurers and proposers should have freedom to determine the value of the insurable interest, although agrees this should be 'reasonable'.

### Insurance without evidence of economic loss

The Panel supports the proposal to allow parents to insure the life of a child under 18 with any insurer, not just friendly societies. This should enable more providers to offer such policies, thereby increasing market competition for the benefit of consumers.

The Panel appreciates the motivation for capping the sum assured on such policies, due to the risk of moral hazard. While the Panel is not best placed to suggest the level of this cap, we believe it is important to ensure this is updated regularly to reflect the real value of the cap will be eroded over time. We suggest that this could be increased in line with a defined inflationary measure, such as the Retail Price Index (RPI), as is the case with the annual ISA limit. We also recommend that the limit should apply across all policies insuring the child's life. This would help prevent people taking out multiple policies on the same child.

### Cohabitants

The Panel agrees that cohabitants should have the right to insure each other's lives without having to show an economic loss. We believe it is fair and reasonable for these 'couples' to expect the same rights as spouses when taking out life insurance. However, requiring the cohabitants to live in the same household for at least five years seems an arbitrary and high threshold, especially as the cohabitants may have been in a relationship for several years earlier. We suggest it would be more appropriate to set the minimum cohabitation period at six months. This provides a reference point for insurers while ensuring cohabitants' ability to access life insurance is not unfairly or unnecessarily restricted.

Yours sincerely,

Adam Phillips  
Chairman