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The Insurance Act (2015)

and considerations for charities…

What is the Insurance Act?

Insurance law is ancient, deep rooted into our marine heritage, many centuries prior. However, since the turn of the twentieth century, one of the most fundamentally important pieces of insurance legislation has been the Marine Insurance Act 1906. It has governed much of the relationship between insurers and policyholders but it has also been in need of a facelift.

The Insurance Act 2015 represents a step change in legislation. It is designed to reform how insurance contracts are governed in the UK. The act makes some fundamental changes to principles that have underpinned insurance law and some of these updates might have an impact upon your charity. They will certainly change how Ladbrook act as a conduit between our charity clients and insurers. As an insurance broker, we always act as an agent of our charity clients in all activities, we will be advising our clients on a one to one basis, as appropriate.

While officially titled The Insurance Act 2015, it is a slightly misleading title as while it achieved Royal Ascent in 2015, it comes into force in August 2016.

This paper outlines some of the key changes that the Insurance Act introduces and discusses the impact on charities.

What does the Act do?

Disclosure

There are several areas that are effected by the act but some of the biggest changes impact disclosure. One of the key objectives in the legislation is to address unfairness in this area.

Disclosure as it currently stands places the burden on the policyholder to ensure that the insurer has the relevant information they need to correctly underwrite cover.

When the Insurance Act 2015 comes into force, there are some subtle but important changes to disclosure. Charities will still be obligated to disclose any facts that the charity knows (or ought to know) that would influence an insurer. However, this obligation is now found to be met if the charity has provided information which reasonably should have prompted the insurer to ask more follow-up questions.

While this still allows for some interpretation, it seems certain that the intention is to make the burden of disclosure, more evenly applied to both client and insurer.

However, **It is expected that a charity would make reasonable steps to consider and search for such information too.** We will examine what this means in more detail when considering the impact of the act on charities.

The changes to disclosure are very important. This is because the duty of disclosure has a very important role. In legislation dating back to the eighteenth century, case law was created that means if a policyholder (whether fraudulently or not) conceals the facts of a risk, then the insurer may subsequently void their policy. This was further cemented into place in 1906 as part of the Marine Insurance Act released that year. Voiding a policy means that the insurer can pretend the contract never existed and remove themselves from all subsequent obligations.

Consequences of Misrepresentation

Changes are also being made to how insurers can deal with misrepresentation. As stated the current law enables insurers to make policies void following misrepresentation. This is even the case in situations where they would have accepted the risk if they knew all facts at the inception of the policy.

To date, insurers have been able to void cover simply because some elements of the risk was presented incorrectly. Often a discrepancy might be found during a claim, *a time where one might argue*, unfair insurers might be financially motivated to void a policy and avoid a claim.

For example an unscrupulous insurer might refuse to pay for a property theft following a break in, if the charity had incorrectly stated the nature of the roof construction of the property. In this example, the disclosure was not necessarily relevant and not even fraudulent, yet it opens the door for insurers to make a policy void. Again in this example, you might consider that the insurer might have a point if the roof construction was perhaps non-standard and would have initially led to them declining to offer cover at all.

However, if the insurer would have insured the charity and choose to void a policy due to this mis-representation, then one might argue it is an unfair situation for the charity.

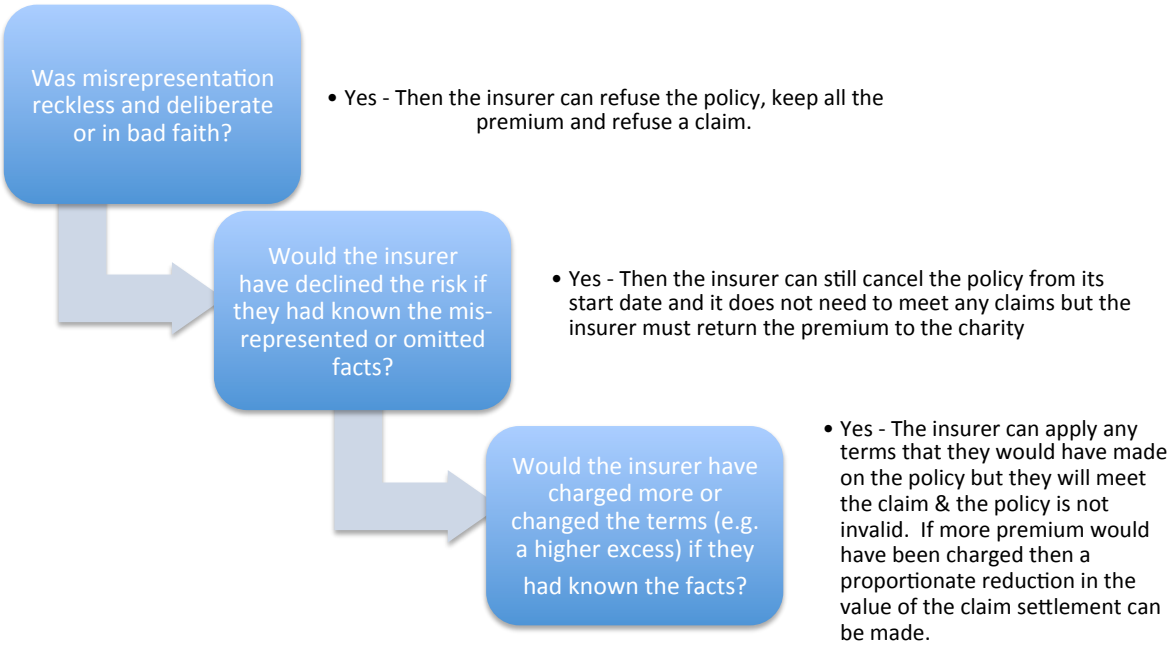
If you have ever been in a situation where an insurer is trying to avoid a claim, you will know it can be a stressful and infuriating business. It is our experience that most insurers (certainly the ones we work with!) are reputable and want to give good service in the event of a claim. Still, differences between the actual risk and 'what the insurer believes the risk to be', can lead to delays or in the worst cases, reduced payments or even voided policies.

Knowing how important this is, we always work with our clients to ensure all aspects of their organisational activities are represented and the risk details are up to date at each renewal. This often is helped by a visit to the client premises and a comprehensive presentation to insurers.

The consequences of misrepresentation are set to change too with the introduction of The Insurance Act 2015 and it will create fairer outcomes for customers.

Some things will not change. Following the introduction of the act, if a misrepresentation or omission is made and is deemed to be **reckless or fraudulent**, the act enshrines an insurer's right to act as though the policy never existed. This means that they can still, in those circumstances, refuse to pay a claim and furthermore, they can now retain all of the premium too in these circumstances.

However, if the breach was a little more innocent, then the outcome will now reflect that. The following chain broadly determines the outcome.



Changes to Warranties

In insurance law, a warranty is a promise, normally made by the policyholder, and included as an essential part of the contract. Not fulfilling the warranty or promise falsity renders the policy void. A typical warranty might concern maintenance of equipment or aspects of building security.

Some insurers have at times used 'Basis of Contract' clauses within their insurance policies. These clauses turn any information provided by the charity into warranties, so that any change (even if trivial or immaterial) can render a policy void. Thankfully, under the new act, 'basis of contract' clauses will be abolished for organisations, having already been abolished for consumers under the Consumer Insurance (Disclosure and Representations) Act 2012.

A warranty is a contractual term in a policy and must be kept to at all times. For example, it might be a warranty that the alarm on a property has to be in operation when the property is not occupied. Historically, a breach of such a warranty has also allowed an insurer to walk away from any liability, even if the warranty itself is not at all connected to the loss.

That changes with The Insurance Act 2015. If a warranty is breached by a charity then the subsequent liability on the insurer will not be discharged as it currently can be. Instead liability will be suspended.

If, during this suspension, the client can resolve the breach, then cover is back in force. So for example, imagine a policy which has a warranty in force that commits the charity to activating a burglar alarm overnight. Now imagine that the charity refurbishes the property and removes the burglar alarm. In this situation, the insurer can suspend cover for theft (see relevance in the next paragraph!) but only until the charity has replaced the alarm.

Another important change with The Insurance Act relates to the relevance of a warranty upon a subsequent claim. Critically, the insurer will not be able to decline to continue cover if the charity can demonstrate that there is no connection between the warranty and a claim. It was a critical part of the review conducted by the Law Commission which led to this aspect of the updated legislation. Their conclusion is clear, **that insurers should not be entitled to avoid a claim where the insured's breach did not relate to the loss**. So if the alarm was not operational but the claim relates to an injury to a volunteer who fell over in the charity office, an insurer can no longer decline cover for this liability claim.

This seems to be an eminently sensible step as warranties are designed to create obligations on the policyholder which the insurer might reasonably expect. They certainly should not be used to unfairly avoid a claim for a trivial or immaterial breach.

What Charities Need to Consider

This legislative change happens on the 12th August 2016. It will then relate to all insurance transactions, including mid-term policy adjustments. In my view, the new act makes handling the consequences of breaches and commissions, fairer for third sector organisations and so should be welcomed.

I would highlight that it is still possible for insurers to contract out of these new legal obligations as long as they have made this very clear to the policyholder. Thankfully, none of the charity specialist markets that we work with have indicated any inclination to do so and I cannot conceive of the circumstances in which we would work with an insurance market that wished to avoid these new obligations.

A significant implication of the act is that all charities will need to comply with the new duty of fair presentation at every renewal.

Two key factors need to be considered when planning for your renewal under the new Act, which may not have been appreciated to date:

1. Charities should leave more time for renewal (particularly data gathering) or they could risk failing to comply with their statutory duties and missing the opportunity to benefit from the additional defences that the new law provides.

2. While the new remedies for breach of the duty of fair presentation are clearly more proportionate than the current avoidance-only stance, there still is significant risk that cover will be compromised if insureds fail to provide the information that insurers need. It is also more likely that both the courts and insurers will follow the law as written, because the new regime is now deemed to be fair and balanced between the two contracting parties.

'Reasonable Steps'

One of the biggest considerations for charities is understanding what 'reasonable steps' means in relation to the disclosure of your insurance risk. A charity needs to think about who in the organisation holds important information (management, trustees, even perhaps volunteers). This is the most important thing a charity can do in light of the new legislation.

The Insurance Act there creates much greater specificity about whose knowledge needs to be captured when preparing a presentation of risk for insurers.

Under the new law, it is just as important to disclose important / relevant information known to the charity that would affect how an insurer would treat the risk. The definition of this now extends to information that the charity ought to know.

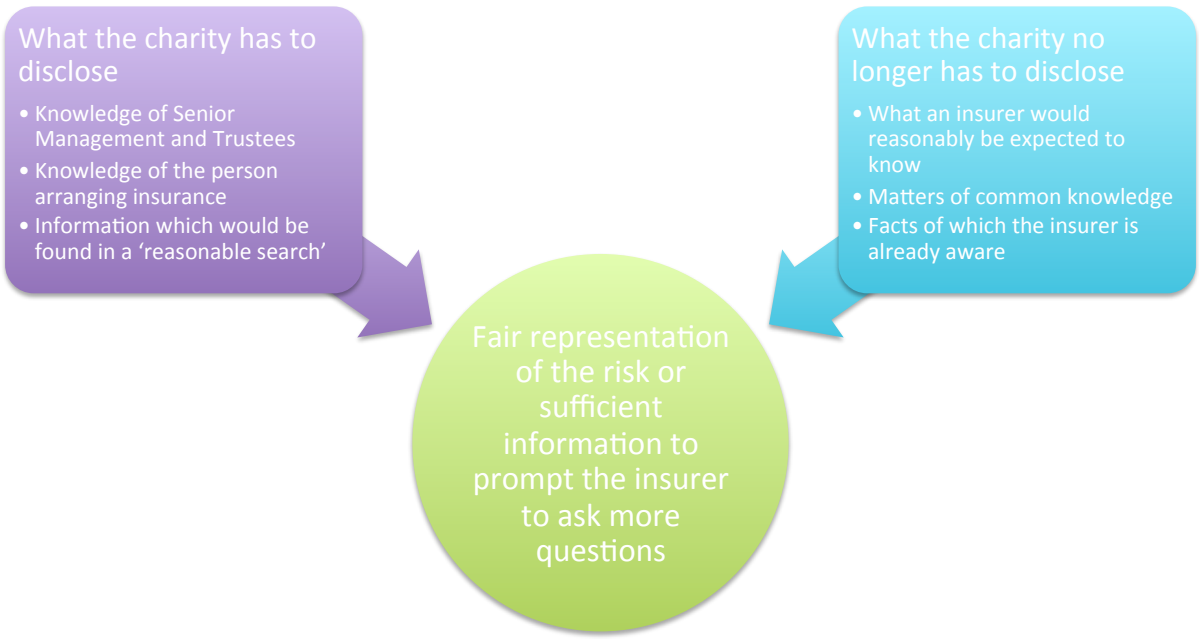
However, this disclosure is subtly different under the new Act because the charity only need disclose enough information to alert an insurer that it needs to ask for further information to uncover material facts.

The new Act also explains whose knowledge counts. It is clearly unreasonable to expect that every material fact known by every volunteer will be accessible to the person responsible for arranging the insurance, but insurers need to have relevant information to accurately price and evaluate the risk. The new Act defines more clearly the information that should be disclosed.

Information known to senior management and the buyers of insurance of course has to be disclosed. It also states that information held by other areas of the charity or any other person which ought to be known if a **reasonable search** is conducted.

The Act also defines the information which the insurer should be able to find rather than expecting your charity to disclose it. These categories are shown in the pale blue box.

The Insurance Act better reflects that insurers will already hold information about the risk, either specifically about your charity or about that type of charity. However, it also responds to the fact that organisations are vastly more complex than they were when the Marine Insurance Act of 1906 was written. In the modern world, information and knowledge about risk might reasonably be held across charities, particularly larger ones.



Summary: Making a Reasonable Search

There is no 'one size fits all' answer to what constitutes a reasonable search for information, as what counts as reasonable is intended to be flexible and will be determined by the size and complexity of your charity. I am interpreting the requirement to consult senior management as to include trustees. As a result, we will be discussing how our insured charities meet that requirement when the act is in force.

Your charity must also take reasonable steps to ensure that your reasonable search extends to any other person who may hold material information. This could apply to information held by your broker, other agents (e.g. advisers, outsourced service providers), key internal colleagues and volunteers and even third parties.

If a policy is being created that insured sub groups, it would be reasonable that they are included in the information gathering stages. The Act only requires the search to pick up what would have reasonably been revealed by a reasonable search: for example, such a search would not necessarily be expected to prompt an admission from a junior employee in the charity of their own negligence.

Another factor we will be considering with our charity clients are the new requirements around the way information is presented. All information needs to be presented to the insurer in a reasonably clear and accessible manner. Not only will too short presentations be unacceptable and not meeting the requirements on behalf of our clients but also 'drowning' an insurer will also mean that fair disclosure has not occurred. In other words, if a policyholder and broker submit an

avalanche of information without indicating some potentially significant information within, then it prejudices the policyholder's position.

About Ladbrook

Ladbrook Insurance is an insurance broker specialising in the third sector. 95% of our clients are not for profit organisations. We believe that the third sector has an increasingly important role to play in society and that the charity and voluntary organisations that make up the sector, need specialist insurance advice.

We believe that our independent, advised and specialist approach is needed in the charity sector. We also embed a strong ethical approach in our culture, designed to compliment the very sector we were created to serve. We are highly personable, each client has a dedicated Account Handler and we are always happy to get face to face with our clients.

Throughout our history, we have insured thousands of charitable organisations engaged in a wide spectrum of social good. Our approach is simple. Knowledge, expertise, an ethical approach and a dedication to the third sector.

About the Author

Tim Larden has worked in the insurance industry since 1997. In 2015, as the founding principal Martin Ladbrook retired, I acquired Ladbrook Insurance.

From 2010 - 2015, I ran the business insurance subsidiary of Endsleigh which specialised in the third sector. During this time, I worked with umbrella groups such as Locality, NUS and Sporta.

I enjoy the challenges of the variety of the third sector. Our clients often work in deprived communities, supporting some of the most vulnerable people in society.

I volunteer at St Paul's Hostel and have run marathons for Whizz Kidz and Meningitis Trust.

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