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Impact of the Insurance Act 2015 on London Market Brokers

The Insurance Act 2015 introduces a number of changes to English insurance law which are likely to have a significant impact on the conduct of (re)insurance brokers in the London market. This article will review some of those changes and the new exposures that brokers will face as a result of their introduction.

The Insurance Act will change UK insurance law, including English insurance law, as it applies to contracts, or variations to contracts, entered into after 12 August 2016.[1] The Act will apply to contracts of reinsurance as if they are contracts of insurance. The placing of (re)insurance contracts that are subject to any other law will not, in theory, be affected by the Insurance Act, but in practice it will be very difficult for any broker to adopt different processes depending on the law of any individual policy that it is arranging. Accordingly, it is likely that the changes introduced by the Insurance Act will have to be adopted by brokers across the board when dealing with their clients and the placing of business in the London market.

Section 3(1) of the Insurance Act imposes a duty on the (re)insured to make a fair presentation of the risk to the (re)insurer. The duty of fair presentation is little different from that under current law in that it requires the (re)insured to disclose every material circumstance which it knows or ought to know, but in a number of respects the burden which the Insurance Act imposes on the broker will be greater than under the current law.

Firstly, the Act requires the (re)insured to make disclosure in a manner which would be reasonably clear and accessible to a prudent (re)insurer. Paragraph 47 of the Explanatory Notes accompanying the Act[2] makes it clear that this requirement is focused on eliminating "data dumping" by the broker at the time of placing. Insureds and reinsureds will now look to their broker to prepare information in a form that is accessible to the underwriter. The Explanatory Notes warn that the presentation should not be "overly brief or cryptic". The failure to satisfy these requirements may result in the presentation not being a "fair presentation" with the consequence that the underwriters may be entitled to avoid or have other remedies contained in the Act for failure to make that fair presentation. Inevitably, insureds and reinsureds will look to their brokers if there is a failure in this regard.

One of the more difficult areas of English law concerns the circumstances in which a corporate entity is fixed with knowledge. The Insurance Act ousts the current law (which fixes the (re)insured with knowledge of its "agents to know" and what in the "ordinary course of business" it ought to know[3]) and introduces a new regime. What a corporate insured (or reinsured) knows for the purposes of disclosure to underwriters will arise in two ways:

- the actual knowledge of those individuals involved in the senior management of the (re)insured or in arranging the insurance or reinsurance (eg a risk manager, the broker, or a reinsurance manager) will be the (re)insured's knowledge;[4] and
- what could be discovered by a reasonable search of information available to the corporate (re)insured will also be the (re)insured's knowledge.[5]

These concepts can be simply stated, but the detail is likely to give rise to some difficulty for brokers advising their corporate clients on what they have to do to comply with the Insurance Act's requirements. For example, the (re)insured's senior management is defined to mean *"those individuals who play significant roles in the making of decisions about how the insured's activities are to be managed or organised."*[6]

Paragraph 55 of the Explanatory Notes says that *"in a corporate context, this is likely to include members of the board of directors but may extend beyond this, depending on the structure and management arrangements of the insured."*

Brokers will be expected to advise on which people need to be asked. As can be seen from the definition and the Explanatory Notes, identifying the right people may not be an easy task.

Identifying those individuals who are responsible for the (re)insured's (re)insurance may also give rise to some difficulty. It is obvious that a risk manager, or the individual placing broker, will fall into this category of person. However, there may be others in both the (re)insured's organisation and in the broker's organisation who may be deemed to be involved in arranging the (re)insurance, for example an individual at the broker who collates risk information on a general basis which is used to arrange the (re)insurance. All these individuals will have to be identified to ensure that what they know is catered for in the placing information given to underwriters.

"Reasonable search" of information

One of the main changes brought about by the Insurance Act will be the introduction of the concept of the (re)insured having to conduct a "reasonable search" of information available to it for the purposes of making a fair presentation of the risk. This is a new requirement as the current law does not require the (re)insured to conduct a search for information.[7] No doubt the broker will be asked to advise on how that search is to be conducted and who should be asked. The Act is imprecise as to what will satisfy the requirement of a reasonable search. If the broker or the (re)insured get it wrong, then there is a risk that the presentation will not be a "fair" one such as to satisfy the duty set out in the Act. For example:

- The search has to be of information available to the (re)insured. This includes *"information held within the insured's organisation or by any other person"*.[8] If the (re)insured is part of a larger group, is that larger group the "organisation" whose information has to be searched, or is it limited to the information held by the (re)insured itself? This will be highly relevant to a captive buying reinsurance: does the Insurance Act require it to search the information of every company in its group in order for the presentation to reinsurers to be fair?

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– Information held by "any other person" is also subject to search. The examples given in the Act of "any other person" are *"the insured's agent or a person for whom cover is provided by the contract of insurance"*.[8] Paragraph 57 of the Explanatory Notes states that *"the reasonable search may extend beyond the insured itself to other persons, where such a search would be reasonable in the circumstances and where information is available to the insured."* Paragraph 8.90 of the Joint Law Commissions' (JLC's) Report published in July 2014 suggests that any other person may include suppliers, lawyers and accountants. Is a retailer now expected to ask its suppliers whether they have any material information to pass on to it for the purposes of the retailer arranging, for example, its liability insurance?

Areas of uncertainty

– It is not clear from the Act whether information is available to the (re)insured only in circumstances where the holder of the information is under a legal duty to pass that information to the (re)insured (for example an agent) or whether "available to" means any information that the (re)insured could reasonably be expected to ask for and obtain. A person covered under the insurance contract (for example a joint venturer of the insured) may not be under any legal duty to pass any information to the insured, but that joint venturer's information may nonetheless be disclosable if a court ultimately finds that it would be reasonable for the search to include that information. Brokers are going to have to advise their clients on what enquiries of whom will satisfy the reasonable search requirement.

The Insurance Act carves out from information that has to be disclosed to underwriters, information that is acquired by the (re)insured's agent (typically a broker) which is confidential and is acquired through a business relationship with a person who is not connected with the contract of (re)insurance.[9] If a broker has highly material information, but that information is not disclosed to underwriters on placing, will it be sufficient that the broker believes that the information it held was confidential, or will a court test whether, objectively, the information was given to the broker confidentially? The broker will have to make this decision in circumstances where there is no current guidance (because no court has had to address this issue).

Another area of uncertainty introduced by the Insurance Act is whether the information that would have been revealed by a reasonable search is limited to the information which the (re)insured found out having conducted its search, or includes information that the (re)insured would have found out had the search been conducted immediately prior to the placing of the (re)insurance.

Section 7(4) of the Insurance Act sets out examples of things which may be material circumstances. They include special or unusual facts relating to the risk or anything which those concerned with the class of (re)insurance and field of activity in question would generally understand as being something that should be dealt with in a fair presentation of risks of the type in question. Both of these matters are going to have to be addressed by brokers in advising their clients on what needs to be disclosed to underwriters. Any failure to give appropriate advice may result in the (re)insurance being impaired or even avoided.

Proportionate remedies for any material non-disclosure or misrepresentation

Under current English law, any failure to disclose a material circumstance may entitle the (re)insurer to avoid the insurance contract ab initio.[10] An important feature of the Insurance Act is the introduction of proportionate remedies for any material non-disclosure or misrepresentation. The (re)insurer will no longer be automatically entitled to avoid the contract of (re)insurance and its remedies may be restricted to what it would have done had there been a fair presentation (eg charge more premium, or insert an exclusion clause).[11] However, the (re)insurer will have a right of avoidance if the failure to disclose is deliberate or reckless. The decision by a broker to deliberately withhold material information because it was considered to have been acquired in confidence, when in fact it was not, may result in the (re)insured losing its (re)insurance as the result of an error by the broker.

One of the significant changes introduced by the Insurance Act is Section 11 which prevents an (re)insurer from relying on the breach of a term (typically a warranty) where the breach *"could not have increased the risk of the loss which actually occurred in the circumstance in which it occurred."* The relevant term has to be one that would tend to reduce the risk of a loss occurring, but not one which defines the risk as a whole. Accordingly, it is going to be important to identify which category of term a particular condition or warranty falls into. (Re)insureds will be looking to their brokers for advice in this regard.

With the exception of "basis of contract" clauses, (re)insurers of business insurance or reinsurance contracts will be able to contract out of the provisions in the Act (for example, the provision concerning breach of an irrelevant term).[12] One of the requirements for contracting out is that the (re)insurer must take sufficient steps to draw any disadvantageous term to the (re)insured's attention. However, if the broker has actual knowledge of the disadvantageous term when the contract is entered into, then this requirement will have been satisfied. It will accordingly fall to the brokers to identify to their clients the terms in the contract of (re)insurance that vary the application of the Insurance Act. If the (re)insured loses cover as a consequence of the underwriter contracting out of the Insurance Act's effect, the broker will need to establish that it drew the (re)insured's attention to the contracting out provision.

Underwriters and brokers have until August 2016 to adjust their practices and standard terms to the new matters required by the Insurance Act. The JLC hope that this will result in the introduction of protocols addressing what will be required for a fair presentation of the risk in particular classes of business. The uncertainties in the Act described in this article suggest that the market is going to face challenges when implementing the legislation. Inevitably, there will be differences of opinion as to how best to address these matters in a way that does not harm market efficiency or generate more uncertainty.

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[1] *Section 22 Insurance Act 2015*
[2] *Explanatory Notes provided by HM Treasury on 16 January 2015*
[3] *See s.18(1) Marine Insurance Act 1906*
[4] *Section 4(3) Insurance Act 2015*
[5] *Section 4(6) Insurance Act 2015*
[6] *Section 4(8)(c) Insurance Act 2015*
[7] *See Australian & New Zealand Bank Limited v Eagle Wharves Limited [1960] 2 Lloyd's Rep 241, 252*
[8] *Section 4(7) Insurance Act 2015*
[9] *Section 4(4) Insurance Act 2015*
[10] *Section 18(1) Marine Insurance Act 1906*
[11] *Section 8 Insurance Act 2015*
[12] *Section 16 Insurance Act 2015*