In this note, we are looking at some of the more practical issues and concerns that arise from the recently passed Insurance Act 2015 (the ‘Act’), which is due to come into force on 12 August 2016. A description of the Act and its significant provisions is set out in our last Technical Insight, ‘The Insurance Act 2015 – New Legislation’.

Although the Act has yet to come into force, it is worth considering now how best to deal with the new laws, in order to plan ahead. A number of insurers have indicated to Willis Towers Watson that they intend to treat the Act (or elements of the Act) as being effective immediately (or at least earlier than 12 August). This early adoption may be simply by way of that underwriter deciding of its own volition to apply the principles of the Act to all policies (whatever the policy terms actually say) and/or to incorporate express terms reflecting the new Act into new and renewed policies. If that is not the case with your underwriter, policyholders may also wish to consider asking underwriters to agree to adopt elements of the Act early.

This note does not offer specific guidance on individual risk classes.

**Will the act apply to your contract?**

The first practical question is: will the new Act apply to your contract of insurance or reinsurance? The Act will apply to your contract of insurance if your contract is subject to the laws of England, Wales, Scotland or Northern Ireland. A properly drafted contract will always expressly set out the law and jurisdiction applying to it. If the law selected is that of England, Wales, Scotland or Northern Ireland, then the Act will apply to:

- contracts of insurance entered into on or after 12 August 2016; and
- variations to contracts of insurance entered into on or after 12 August 2016, whenever the original contract was entered into.

The parties are also free to agree that the Act will apply earlier than 12 August 2016, that it will not apply at all or that only some provisions of the Act will apply or will apply in a modified way. The freedom to contract in whichever terms suit the parties remains – see our previous note for the legal requirements and restrictions on ‘contracting out’.

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**Important note:**

Remember the Act applies equally to reinsurance. For ease of reading, references in this note will generally be to ‘insureds’, ‘insurers’ and ‘insurance’, but the ideas and principles discussed will also be relevant to reinsurance. Some specific points for reinsureds are noted at the end.

As a general consideration, it is worth remembering that the Act has the overall effect of improving the insured’s position as regards the insurer (or the reinsured’s position as regards the reinsurer). The insured’s duties are clarified and are a little less onerous. The penalties for breach of any of those duties are ameliorated. The legal remedies available to the insurer are no longer just a choice between paying the entire claim and paying nothing – a middle ground has been introduced. So, while there is much talk of new duties on the insured, these are – overall – lesser duties.
Some overseas underwriters may have been happy with English law as it was prior to the reforms, as it resembled their own local laws regarding, for example, duties of disclosure, warranties and remedies available. Local law regarding insurance in some countries will in many cases have been based closely on English legal principles. Following the reforms to English insurance law, there is now the possibility that such overseas underwriters may be less comfortable with English law and may seek to change the choice of law and jurisdiction from England, Wales, Scotland or Northern Ireland, in order not to be subject to the forthcoming changes.

The benefits of the Act will therefore not be available if an underwriter insists the choice of law and jurisdiction is changed from England, Wales, Scotland or Northern Ireland.

**Making a fair presentation**

The outgoing regime was based upon the notion of a duty of utmost good faith, which in turn required an insured to disclose voluntarily (and without being asked) every material circumstance about the risk and not to misrepresent material facts.

The duty of disclosure remains, with the onus largely on the insured to volunteer information, and with a slight amelioration in that the insurer must ask questions where they have been given sufficient information to be put on notice that they need to ask additional questions, as well as a requirement on the insurer to interrogate their own records for relevant information, such as previous claims records.

It is important to recognise that there are limitations to both these ameliorations of the duty of fair presentation. A Court might not agree that sufficient information has already been given to put the insurer on notice that it should ask questions. The insurer might have already made a reasonable search of its own records and still not discovered the information it already has regarding the risk. There seems little point in risking an accusation of non-disclosure.

It would be very unwise therefore for a prospective insured not to disclose obviously material information based upon any assumption that the insurer either already has sufficient information to be put on notice that it needs to ask further questions or that the insurer has the information already in its own records. It is worth bearing in mind that when approaching a new insurer to underwrite some or all of a risk or where you have both leading and following insurers on a policy, not all insurers will have the same information within their own records (if any) regarding the risk you are proposing.

**Important Note:**

The Act has not changed the test for what constitutes a material fact-

_a circumstance or representation is material if it would influence the judgement of a prudent insurer in determining whether to take the risk and, if so, on what terms_. The Act sets out some non-exhaustive examples of material facts:

(a) special or unusual facts relating to the risk,

(b) any particular concerns which led the insured to seek insurance cover for the risk,

(c) anything which those concerned with the class of 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.

Although it remains unnecessary to disclose matters which diminish the risk (for example, a building has security alarm protection), this may still be a useful disclosure to make if it encourages the underwriter to accept a risk or to reduce premium. In such cases it would become a material representation.

**Important Note:**

In regards to fair presentation of the risk, it is important to understand that although the new Act goes to greater lengths to help define disclosable knowledge, the new duty of fair presentation is not more onerous than the duty of disclosure under existing law.

In the vast majority of cases, disclosure which properly meets the extensive requirements of the outgoing law, will also meet the requirements of the new Act. Although ‘senior management’ is now specifically named as a relevant source of knowledge for the purposes of disclosure under the new Act, this would have almost certainly also been the case under the old law.
If, having received the initial risk presentation, one underwriter requests more information, the prudent approach would be to provide that additional information to all insurers approached in relation to the particular risk.

A word of caution on extensive disclosure: do not fall foul of the prohibition on data dumping. A presentation of material information must be fairly made and the dumping of enormous data sets on an underwriter with no attempt at making that information clear and accessible (by indexing, categorising, filtering etc.) will probably not be fair. Again, if this is an issue, try to agree with the underwriter how best to present information – what filters are to be used, which data highlighted etc. Consider also summarising the key material facts at the beginning of the presentation, taking care to ensure that this is in itself a fair summary of the risks and not misleadingly positive. Willis Towers Watson experts can advise on how to present data in a clear and accessible manner so that material information can be identified by the underwriter with reasonable ease.

**Knowledge**

In preparing for disclosure, the process of gathering information within a large corporation can be a complex task. Under the Act, there is an obligation on the insured to carry out a ‘reasonable search’ to discover material information. This is intended to be a flexible enough standard to allow for the many different types and sizes of commercial insured that will be governed by this rule of disclosure, however that flexibility incorporates vagueness.

When there are hundreds or thousands of employees, at what point may an insured stop searching or stop asking questions? The new Act makes it clear that the material knowledge of senior management, and those responsible for the insured’s insurance (including their brokers), will be disclosable. Under the Act, ‘senior management’ includes those individuals who play significant roles in the making of decisions about how the insured’s activities are to be managed or organised.

However, the insured is still required to reveal what it ought to know, which means that the insured must make reasonable enquiries – which must, at least in part, mean enquiries of those within the organisation (and relevant agents external to the organisation) likely to hold information material to the risk being insured, not just enquiries of senior management or those responsible for the insurance.

**Important Note:**

Two possible ways of reducing uncertainty as to the fairness of the presentation of the risk:

1. Disclose the information anyway; or
2. Tell the underwriter that you are not going to disclose certain information (indicating the type of information – for example, ‘We are not disclosing claims made prior to January 1, 2010 and none made later than June 30, 2015’) and seek the underwriter’s agreement that this is acceptable. If the underwriter agrees to the limitation on disclosure, they cannot later complain.

The golden rule remains: if in doubt about whether a circumstance may be material, declare it, but do not data dump. Treat the ameliorations to the insured’s duty of disclosure (knowledge the insurer already has or the disclosure of partial data to the insurer sufficient to indicate that they may need to ask further questions to elicit all material information) as potential defences to later claims of insufficient disclosure, rather than principles to guide the extent of your disclosure.

**Further Consideration:**

Here are some areas for further consideration concerning reasonable enquiries made by the insured in order to reveal what it ought to know:

- Do you have internal obligatory reporting procedures, systems and controls in place which make it more likely that material information will be identified and reported to senior management and/or those responsible for arranging insurance cover?
- Have you properly documented those procedures so as to ensure that you can later demonstrate that a reasonable search was made?
- Are you confident as to the list of senior managers and those responsible for arranging insurance is complete and up to date?
- How much time are you allowing for these enquiries to be made in advance of policy placement? As you have to make a reasonable search, you must allow a reasonable period in which to complete that search. A Court is not likely to have much sympathy with an insured that failed to collect and disclose material information because it left its enquiries until the last minute.
- Procedures also need to incorporate time for requests for more information from underwriters, to ensure your response is compliant and to allow for timely placement of your policy.
A note on broker’s knowledge: the knowledge of a broker working for you that has been acquired by the broker while acting for another client will not be deemed to be the knowledge of the insured. However, as under the previous law, knowledge acquired by the broker in the course of acting for your company will be deemed to be your knowledge and will be disclosable.

Willis Towers Watson can assist you in considering the enquiries that might be made in the circumstances of your particular insurance but also consider the following options (although these will not be available for all classes of cover, being perhaps more suited to specialised risk classes):

1. agree with or, at the very least, inform the underwriter the extent of the searches you have made and that further searches are not required or will not be made;

2. define in the contract exactly whose actual knowledge within or external to your particular organisation is relevant and disclosable for the purposes of the policy. Many contracts of insurance already include such provisions, where this is an issue for the insured.

Contracting out/contracting in

We have not been advised by any underwriter that they intend to contract out of the Insurance Act reforms as a matter of general policy, but there will certainly be individual cases where this happens to a greater or lesser extent. Some underwriters have indicated that they will seek to apply the principles of the Act prior to August 2016, both in terms of changing their wordings to incorporate early adoption and (in some cases) applying the Act to their claims handling processes regardless of the contract wording. An example of the latter would be to ignore an ability under existing law to terminate cover altogether for a breach of warranty but instead merely to suspend cover, allowing the insured to remedy the breach.

One major insurer has advised that they intend to substitute the proportionate reduction of claims remedy in the Act, for payment of the additional premium they would have required in return for full payment of claims. In most, but not all situations, this might be seen as more favourable than the Act.
Early adoption – improving on the new laws

While early adoption of the Act as it currently stands is likely in itself to improve the position of most insureds, it is worth considering whether or not to enhance or clarify some of the principles and remedies set out within the Act when drafting and negotiating early adoption policy terms. Consider the following potential improvements (with the first two being more appropriate for specialised risk classes):

1. Define Relevant Knowledge: As mentioned above.

2. Agree the Extent of Enquiries Made for the purposes of disclosure, as discussed above.

3. Improve on the remedies that may be imposed by the underwriter: For example, where, following a non-deliberate and non-reckless non-disclosure of material facts, an insurer would still have entered into the contract of (re) insurance, but would have charged a higher premium, under the new Act the underwriter would be entitled to reduce proportionately the claims it pays. So, if the underwriter would have charged double the premium it in fact charged, it can halve any claims paid. It would be prudent for some insureds to agree instead that the insured will have the option to pay the additional premium and receive full payment of claims.

A further consideration, where your policy is divided into distinct sections providing distinct covers (for example, a section exclusively covering business interruption and a section covering third party liabilities), would be to seek to restrict the remedy available to the underwriter to affect only the distinct section of cover affected by any non-disclosure, misrepresentation or breach of condition. So, for example, it might be provided that only claims within the section of cover affected by a non-disclosure may be proportionately reduced, rather than all claims under the policy as a whole.

The downside to this, however, might be that the proportionate reduction of such claims would be greater than it might have been had the increase in premium that would have been charged been taken as a percentage of the whole policy premium, rather than the premium for the affected section. For example, a policy has cover in two sections, A and B, for each of which £50 in premium was charged. Say a negligent misrepresentation was made in relation to section B, which would have meant the underwriter would have charged an additional £10 for section B cover had the misrepresentation not been made. Under the Act as it stands, claims under both sections A and B would be reduced to 90.9% (100 divided by 110). If the remedy is applied to section B claims only, 100% of section A claims would be paid, but 83.3% (50 divided by 60) of section B claims would be paid. Consider which of these approaches is more likely to be advantageous to you.

4. Add a requirement for a direct causative connection between a breach of a term (including a warranty) and the loss claimed, before allowing the underwriter to reduce its liability in reliance on that breach. At present, the new Act has improved the previous legal position by requiring a relevant connection between a breach of any term the underwriter has imposed to reduce the risk of a particular loss of a particular kind and the actual loss that occurred, in the circumstances in which it occurred. To avoid any penalty as a result of the breach of such a term, the insured must show that non-compliance with the term could not have increased the risk of the loss which actually occurred in the circumstances in which it occurred. That is not the same as a requirement to show a lack of causative connection between the breach that occurred and the loss claimed for under the policy. For example, a policy has a requirement for a particular kind of window lock to be installed. This is installed on one side of a building, but not the other. A burglary takes place, the building being broken into via the windows with the correct window locks installed. Clearly, there is no causative connection between the lack of window locks on some windows and the burglary that took place, as the building was not entered via the inadequately protected windows. But, using the Act’s wording, did the lack of window locks at least increase the risk of a burglary loss? This is arguable either way, so the insured’s position would be improved by amending the legal position to require a causative connection between the breach of a term and the loss that actually occurred before the insurer can rely on that breach to reduce a claim or not pay the claim at all.

5. Limit the way that any additional or replacement term to be imposed by an underwriter (following non-disclosure of material facts) can apply: Insurers are allowed under the Act retrospectively to apply terms that would have been included in the policy had proper disclosure been made at the outset. Make it clear that any term that the insurer seeks to apply retrospectively is not to be a ‘disadvantageous term’ as described in section 16(2) of the ‘Contracting out’ provisions of the
Act. So, for example, this would prevent the insurer imposing a warranty that was not merely suspensory, but discharged the insurer from all liability from the date of breach – otherwise an insurer might argue that you had already breached the warranty they would have applied and that, in consequence, the whole policy was voidable.

6. **Limit continuing duties of disclosure**: Where there is condition in the policy that introduces a continuing duty of disclosure (for example, an alteration condition in a property policy about any increase in the risk of damage), restrict the remedies open to the insurer for breach of this condition to be no worse than the remedies available had the non-disclosure been made prior to entering into the contract.

Willis Towers Watson, along with other organisations such as AIRMIC and underwriters themselves, has drafted clauses making provision for early adoption, either exactly in line with the Act or with improving modifications. Contact your local Willis Towers Watson office on what might be available to you.

### Straddling two regimes

Whether or not you and your insurer are early adopters of the new regime or are waiting for the in force date of 12 August 2016, depending on the commencement date and length of your policy, you may find your cover is subject to two regimes.

For example, a policy is entered into on 1st January 2016 for one year. The new Act comes into force on 12th August 2016. Unless the parties have agreed otherwise, the new Act will not apply to the policy as it was entered into prior to 12th August 2016. However, if the parties to the policy agree a variation to the policy after 12 August 2016 (for example, they agree to extend the policy by two months and include a new warranty regarding fire sprinklers), the new regime will apply to the variation, regardless of the fact that the main policy is not subject to the Act. So, a duty of fair presentation will have applied in relation to the contract to vary the existing policy, but not to the main policy. The remedies available to the underwriter in respect of any breach of duty or term under the variation will in some instances be less harsh than those available for breaches of the duty of disclosure under the main policy or breaches of any of its terms.

It may therefore be worth considering, if a policy is significantly varied after the Act's in force date, to harmonise the regime applying to the cover as a whole – perhaps agreeing to apply retrospectively the new Act to the main policy, as well as to the variation of it, as though it had been in force at the time the main policy was entered into.

### Specific cautions for reinsureds

**Failure to seek additional information**: Under the new Act, an insured might give the insurer only sufficient information so as to put the insurer on notice that they ought to ask further questions to elicit further material information. Let's imagine that the insurer fails to ask such additional questions and was therefore unaware of a material circumstance affecting cover. As it made no follow up enquiry, the insurer is not able to rely on the insured's failure to present that material information. A claim is then payable in full by that insurer.

At the time the insurance was arranged, assume the insurer purchased facultative reinsurance for the risk. As the insurer was unaware of the non-disclosure of material information by the insured, despite being put on notice by the partial information actually disclosed, the insurer cannot in turn disclose that material information to its facultative reinsurer. A claim is made on the facultative reinsurance and the reinsurer declines payment on the basis that the insurer ought to have known the missing information and failed to disclose what it ought to have known.

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2 There may well be defences against such an argument.
Reinsureds at risk of such an argument may wish to consider excluding from their reinsurance cover any ability on the part of the reinsurer to rely on a non-deliberate and non-reckless failure on the part of the reinsured to seek (and therefore disclose to its reinsurer) further information from an insured.

Early Adoption Dangers: A reinsured deciding to be an early adopter of the principles of the Act in relation to its inward insurance liabilities needs to consider carefully how they achieve this, if they wish to avoid endangering their reinsurance cover. If the principles of the Act are applied early by the reinsured to their reinsured insurance liabilities without there being any provision in the insurance policies incorporating the relevant principles of the Act, the reinsured is applying the Act voluntarily. If the consequence of such voluntary early adoption, unsupported by any legal obligation, is that claims are paid that need not have been paid either at all or in full, a reinsurer may consider this an ex gratia (voluntary) payment. It is unusual for ex gratia payments to be recoverable under reinsurance.

In order to apply the principles of the Act early and safely, preserving the availability of reinsurance for any increased claims payments that result from such early adoption, consider ensuring that the insurance policy terms are amended (in advance of a claim) to make a voluntary early adoption into an adoption by which the insurer is contractually bound. However, whether entirely voluntary or not, always consider the potential effect of any such changes in underwriting policy in the light of your actual reinsurance contract wording – for example, would it amount to a ground for special termination by the reinsurer?

Conclusion and next steps

As the insurance market and, ultimately, the Courts start to consider how to interpret and apply the new Act, uncertainties will be gradually resolved and no doubt new issues will emerge. During this period of settling in and adjustment, Willis Towers Watson will be working with both clients and markets to try to ensure a smooth transition.

Please raise any specific issues or concerns that you have regarding the new insurance regime with your Willis Towers Watson contact. Different clients will require different, tailored solutions.

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2 Obviously, this is only relevant before the Act is in force on 12 August 2016.
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