

Consultation on Insurance Contract Law: Post Contract Duties and other Issues

Memorandum from the Financial Ombudsman Service

20 March 2012

1. The Financial Ombudsman Service welcomes the opportunity to respond to the consultation paper.
2. We write specifically in relation to the proposals concerning damages for late payment and insurers' remedies for fraudulent claims - detailed in chapters 1 and 2 of the consultation paper respectively.

About us

3. The Financial Ombudsman Service was established by law to resolve individual disputes between consumers and financial businesses – fairly, reasonably, quickly and informally. We can look at complaints about a wide range of financial matters – from insurance and mortgages to investments and credit.
4. If we decide that a business has treated a consumer fairly, we will explain why - but if we decide that the business has acted wrongly and the consumer has lost out – we can order matters to be put right. We are completely independent and impartial and decide each case by reference to what is fair and reasonable in all the circumstances.
5. In considering what is fair and reasonable we are required to take into account the relevant law and regulations, rules and guidance, the provision of relevant documents and good practice in the industry. Although we are required to take into account the relevant law – we are not bound by it.
6. In the majority of cases, however - our approach is based on what we know the courts would be likely to do in similar circumstances. For example, many of the disputes we settle turn on well-established points of contract law and our approach would generally mirror that of the law in these cases.
7. However, in some areas – for example, in insurance – good industry practice has developed separately from the law. In circumstances where such good practice has developed separately we may very well depart from the strict requirements of the law in deciding what would be fair and reasonable in the circumstances.
8. We therefore welcome the Law Commission's decision to focus on the law in this area, and we have welcomed the dialogue we have had with the Commission in their preparation of these proposals.

Summary

9. The approach we take to complaints concerning damages for late payment and insurers' remedies for fraudulent claims already broadly reflects good industry practice

in this area. However, this approach has developed separately from the law and our approach in such cases departs from its strict requirements.

10. Our preference is for our decisions to be based on the law and for our decisions on what is “fair and reasonable” to coincide with the law. It would make it much easier to justify our decisions if they were consistent with the legal position and it would also provide a greater level of certainty for both consumers and businesses.
11. The proposal within the consultation will effectively consolidate our current approach and that of good industry practice into primary legislation and therefore we broadly agree with the proposals motioned. This is a strong endorsement of our current approach and we welcome the fact that the proposals recognise this.

Damages for late payment

12. We have already been applying a remedy of damages for late payment for some time and there is also broad acceptance within the industry about the approach we take. However, this approach is inconsistent with the current legal position in the case of *Sprung*¹.
13. We can also award compensation for distress or inconvenience although the amount involved is usually modest – up to £300. Exceptionally, we may award more than £1,000. However, the current legal position in the *England*² case seems to suggest that such awards would not be available.
14. The current law is not only inconsistent with our own approach but it also runs contrary to recognised industry practice. If there is a general consensus that the law is unfair and out of line with accepted industry practice - which the consultation seems to suggest - then we consider there to be a strong case for reform in this area.
15. We therefore agree with the proposal that insurers should be under a statutory duty to pay valid claims within a reasonable time and that failure to do so should result in damages for any foreseeable losses incurred. We also consider that interest should run from the date of the breach rather than the date of the loss – and that the limitation date should run from this date as well for the sake of simplicity.
16. We also broadly agree with the other proposals set out in the consultation paper concerning damages for late payment including that damages for distress and inconvenience or discomfort should be available. We also consider that legislative reform would be desirable in this area to implement these proposals.
17. The proposals set out within the consultation would bring the law more in line with our own approach to such cases and would eliminate current inconsistencies. This in turn would provide a greater level of certainty both for consumers and businesses in terms of the approach we were likely to take.

Insurers’ remedies for fraudulent claims

18. We broadly agree with the proposals set out in the consultation paper concerning insurers’ remedies for fraud.

¹ [1999] 1 Lloyd’s Rep IR 111

² [1999] 2 All ER (Comm) 481

19. In particular we agree that those who commit fraud should forfeit the whole claim to which the fraud relates and any claim where the loss arises after the date of the fraud - although previous valid claims should be unaffected. This mirrors our current approach to the issue and we welcome the fact that the proposals reflect this.
 20. However we do have some concerns as to whether the costs of investigating proven fraud should be recoverable by the insurer. We have no jurisdiction to make binding awards on consumers to pay damages - so this is not a remedy we would be able to apply in practice.
 21. It seems to us that the investigation of claims is an integral part of an insurer's business. In law, consumers are not compensated if a legitimate claim is declined in bad faith, so it strikes us as unfair and unbalanced for insurers to be entitled to such damages where consumers are not.
 22. Also complaints concerning fraudulent claims in co-insurance is not an issue we encounter very much of in practice. However, the fact that we do not receive many complaints concerning the issue does not mean that we can safely say that it is not a widespread problem.
 23. The approach we take to such an issue is that, if a joint policyholder provides evidence that the fraud was not carried out on their behalf or with their knowledge, we consider that the innocent policyholder's share of the claim should be paid whilst the share of the fraudulent party should not.
 24. We agree with the proposal that a fraudulent act by one or more group members should be treated as if the group member concerned was a party to the contract. The current law provides no remedy for the insurer in such circumstances and we would welcome the proposal provided that it does not prejudice innocent group members.
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