

Consultation on Insurance Contract Law: The Business Insured's Duty of Disclosure and the Law of Warranties

Memorandum from the Financial Ombudsman Service

26 September 2012

The Financial Ombudsman Service welcomes the opportunity to respond to the consultation.

We write specifically in relation to the proposals concerning the law of warranties, the duty of disclosure and the extent to which a small business should be treated as a consumer.

About us

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.

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.

The rules setting out how we should handle complaints are set out in the Financial Services Authority Handbook in the section called *Dispute resolution: complaints* (DISP). The section specifically setting out our jurisdiction is found in DISP 2: *Jurisdiction of the Financial Ombudsman Service*.

Whether or not a complaint falls within our jurisdiction depends on a number of factors. But generally complaints can be brought by, or on behalf of, customers (or potential customers) who are private individuals or a micro-enterprise (an EU term covering smaller businesses). Complaints from larger businesses do not fall within our jurisdiction.

Warranties

The consultation proposes to abolish basis of the contract clauses, to treat warranties as suspensive conditions and to introduce special rules for terms designed to reduce the risk of a particular type of loss. The proposals cover both business customers and private individual customers.

In considering what is fair and reasonable we are required to take into account the relevant law and regulations, the provision of relevant documents and good industry practice. Although we are required to take into account the law, we are not bound by it. And this is one area where our approach has developed separately from the law.

The proposals put forward by the consultation would bring the law more in line with our own approach and would eliminate some of the current inconsistencies. This in turn would provide a greater level of certainty, both for customers and the insurer, in terms of the approach we were likely to take.

Although we are in broad agreement with the Law Commission proposals concerning the law of warranties - our own approach to terms designed to reduce the risk of a particular type of loss is that breach of such a term should only suspend liability if the breach itself is connected to the loss.

Duty of disclosure

The jurisdiction of the Financial Ombudsman Service covers both private individual and micro-enterprise customers. So the proposals for the duty of disclosure do not, in the main, apply to those customers falling within our jurisdiction.

However the problems highlighted by the consultation: firstly, that the duty of disclosure is too unclear and secondly that the remedy available to the insurer is too harsh, appear similar to those previously encountered with the law for private individual customers. So we recognise the principles underlying the need for reform in this area.

The problems encountered with the private individual customer market ultimately led to reforming the law via the Consumer Insurance (Disclosure and Representations) Act 2012. This effectively consolidated our own approach into primary legislation and we were in broad agreement with the proposal.

Whilst the current consultation covers business customers which largely fall outside of our jurisdiction, we nonetheless welcome the Law Commission decision to focus further on the law in this area. If the law is considered unfair or unclear as the consultation seems to suggest, then we consider there to be a strong case for reform.

Small businesses


The extent to which a small business should be treated as a consumer is an important issue and we welcome the fact that the Law Commission has recognised this by considering the matter further as part of its proposals.

The Financial Ombudsman Service has considered complaints from small businesses for many years. And during this time we have not encountered any significant issues or difficulties in deciding whether a business is a micro-enterprise and therefore falls within our jurisdiction. We have also not encountered any significant issues or difficulties in deciding whether or not such a micro-enterprise should be treated as a consumer.

Our approach in this area depends entirely on the circumstances of the individual case. For example, an 'unsophisticated' sole trader with limited access to professional advice (such as a one man taxi driver) may be treated as a consumer whilst a larger 'sophisticated' enterprise with access to professional advice (such as a law firm) may be treated as a business.

But despite the fact that we have not encountered any significant difficulties in this area - we do recognise that the same cannot necessarily be said for other sectors. Although we can only comment on our own experience, we appreciate the difficulties faced by the Law Commission in issuing its recommendations in this area.

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