



*The need to promote confidence in the financial services sector and to develop a positive image of the insurance industry has never been greater. Doing so requires a delicate balance between strict application of the law and consideration of the principles of equity and fairness.*

*Neil Ashcroft, Marketing Director, Centriq Insurance, explains...*

Globally, in the wake of the financial crisis, the emphasis is shifting towards protecting the rights of consumers, particularly in the financial services industry. Unfortunately, the latter is increasingly regarded with distrust on the part of consumers, which sometimes springs from claim settlement decisions that are perceived to comply with the letter, but not with the spirit of the law.

The principles which underlie contracts of insurance originate largely from English law, and our courts continue to apply English law in their rulings, with little or no reference to our subsidiary Roman-Dutch common law of insurance, despite the fact that English law is increasingly regarded as out of keeping with the needs of a modern consumer driven society.

An example will illustrate the point. Under English law, the courts have consistently held that there is no need for any causal connection between an insured's breach of a clause in an insurance contract and the insured's loss. In other words, the breach does not have to cause or even contribute to the loss in order for the insurer to repudiate liability, on the basis that the contract was void due to the insured's breach of any one of the conditions of the contract.

If this interpretation of the law is strictly applied, it means that a vehicle theft claim can be repudiated on the basis that the vehicle was not roadworthy at the time of the loss. Although there is no causal link between the breach and the loss, the legal position is simply that the contract is null and void because the insured breached a condition of the contract.

There are many other examples of this type of strict application of English law, which has understandably created much scepticism amongst consumers. This is particularly true in light of the fact that English law, in this respect, is at variance with Roman-Dutch law and other modern civil law systems in Europe. It is also at variance with our own common law, based on Roman-Dutch law, and the principles of dignity, respect and fairness enshrined in our Constitution.

The position of other modern civil law systems in Europe is illustrated by the following example provided by Professor JP van Niekerk from UNISA during his presentation at the Ombudsman for Short-term Insurance's industry workshop held last year.

*'In Forsikringsaktieselskapet Vesta v JNE Butcher, Bain Dawes Ltd & The Aquacultural Insurance Service Ltd, a storm caused damage to an insured fish farm in Norway, resulting in most of its stock of trout and salmon escaping. The primary Norwegian insurer settled the insured's claim against it and had paid for the loss, but when it sought to recover on its reinsurance, the English reinsurers denied liability for the loss, relying on the undisputed fact that the insured had been in breach of a warranty in the original policy, which stipulated 'that a 24-hour watch be kept over the site,' and that 'failure to comply with any of the warranties will render this policy null and void.'*

Van Niekerk explained that under Norwegian law, which governed the Norwegian Insurer, 'the breach of warranty did not render the policy null and void, despite the express words of the policy [Norwegian law by virtue of s 51 of its Insurance Contracts Act 1930 not allowing parties to contract out of the causal requirement], because the breach was irrelevant to the loss.' Therefore, a 24-hour watch could not have prevented the loss of fish caused by the storm. However, under English law, which governed the reinsurance policy issued by the reinsurers to the Norwegian insurers, 'the breach of warranty, whether relevant to the loss or not, rendered the reinsurance policy null and void.'

Due to the often harsh and/or inequitable outcomes resulting from the strict application of insurance law, which in South Africa is largely based on English law, the principles of equity and fairness have been introduced. One of the major steps towards greater protection of consumers in the insurance industry was the establishment of the office of the Ombudsman for Short-term Insurance.

As the Ombud, Brian Martin, explained at a recent workshop: "Following upon the introduction of the Financial Services Ombudsman Schemes (FSOS) Act in 2002, all Financial Services Ombudsman Schemes are obliged to apply principles of equity and fairness in their determinations, in addition to the law. Consequently, in this sense, the application of principles of equity is now a legal requirement in South African Law, insofar as Ombudsman Schemes are concerned."

According to the Ombud, "equity" refers to the fact that a decision regarding a claim settlement "should be fair and reasonable, having regard to all the facts and circumstances of the matter and should be readily understandable by lay persons without any specialist knowledge of insurance".

Returning to the earlier example of the vehicle theft claim that is repudiated because the vehicle was not roadworthy at the time, the application of equity would require “due consideration whether the breach by an insured of any policy provision or term is material in relation to the loss giving rise to a claim and the nature and extent of any prejudice which may be occasioned to the insurer through non-compliance with the provisions of the policy”.

Insurers should, in rejecting claims based on non-disclosure, for example, first establish sufficient facts to prove that the exact terms of the policy in question have been breached and that their assessment of risk has been compromised as a result of the non-disclosure.

In addition, so as not to fall foul of the provisions of section 53(1)(a) of the Short-term Insurance Act, 1998, which limits an insurer’s right to reject claims based on non-disclosure to instances where the non-disclosure “*is likely to have materially affected the assessment of risk,*” the wording of the policy should match the wording of the section and should not be watered down elsewhere in the policy.

The statutory test of materiality, i.e. would a reasonable, prudent person consider that the information constituting the non-disclosure should have been disclosed so as to enable the insurer to form its own view concerning the effect of the information on the assessment of the risk or the premium charged, should also be the only standard applied.

While equity is a requirement in terms of the Ombud’s determinations, increasing focus on consumer protection means insurers would do well to apply the principles of equity and fairness in their own claim settlement decisions. This should not only be done to limit the number of consumer complaints submitted to the office of the Ombud, but also to help build and endorse a positive image of the insurance industry.