Claims Conditions- the Next Step in the Reform of Insurance Law?

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I. Insurance Law Reformed (and Not)

The Consumer Insurance (Dbisclosure and Representations) Act 2012 and the Insurance Act 2015 were the most significant statutory changes to insurance contract law for more than a century. Those reforms- led by Law Commission- are starting to be enforced by the courts.[1] But whilst those statutes remade many fundamental principles, they were not comprehensive. The focus of this short piece is an area which has not been subject to statutory restatement (either in the Victorian codification that gave us the Marine Insurance Act 1906 or the recent changes): the claims condition. As with many of the 'reformed' areas of insurance contract law, these involve duties on the insured that are of considerable commercial significance to insurers. There is a legitimate interest in these duties being met. The question is whether- as with the statutory reforms- the rules might be redesigned with a proportionate remedy.

II. Claims Conditions- An Introduction

Claims conditions exist in most forms of insurance contract. They are present in consumer contracts and commercial policies and in property insurance and liability cover. An area of particular social significance is the effect that the claims condition can have in limiting insurer liability for claims brought against the insured by third parties who have suffered personal injury.[2] In those circumstances, the third party's chances of gaining compensation is reduced. Most liability insurance policies include a specific contractual duty to give notice of likely future claims. This is often supplemented by clauses requiring the insured to co-operate during the claims process, by the provision of relevant documents or access to the site of any physical accident. These operate in the period between two legally significant moments: (1) the insured acting in a way that gives rise to potential liability to a third party and (2) the resolution of a claim by the third-party against the insured. The insurer's liability under the insurance contract

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[1] For example, in *Scotbeef Ltd* v *D&S Storage Ltd* [2024] EWHC 341 (TCC) and *Delos Shipholding SA* v *Allianz Global Corporate & Specialty SE, The Win Win* [2024] EWHC 719 (Comm).
[2] By way of the Third Parties (Rights Against Insurer) Act 1930 and, more recently, the 2010 Act of the same name.

only arises at the second point in time,[3] but it has a significant commercial interest in having prior knowledge of the impending claim and access to information about the insured's conduct in order to limit its future potential liability.[4] In this respect, the claims condition in liability insurance contracts raises legally distinct issues compared to a first-party liability insurance contract. This short piece is focused on the liability insurance context.[5]

Unlike large parts of insurance contract law (for example, the insurance 'warranty'), claims conditions do not build upon the scaffolding of a statutory codification.[6] The effect of the clauses is determined by their wording, properly interpreted. Despite the recent reform of insurance law, and a consistent level of litigation, very little has changed in this area. It is one of the last great areas of 'common law' insurance law not subject to the statutory reform (especially in respect of remedies of breach) that characterised much of the 2015 Act. What follows is broken into three main sections. Part III reviews the current legal position. Part IV shows the limited effect of recent statutory and regulatory controls on claims notification clauses. Part V offers a potential model for reform.

III. Claims Conditions- the Issues

The insurance claims conditions litigation is well developed and tends to centre around a cluster of common themes. These can be summarised as:

For notification clauses:

(a) The trigger: the circumstances in which notice must be given.

(b) The time frame: how quickly notice must be given.

(c) The remedy: the consequences of late notice.

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[3] See *Bradley* v *Eagle Star* [1989] AC 957, 966 (HL) confirming the approach taken in *Post Office* v *Norwich Union* [1967] 2 QB 363, 373-374 (CA): 'the insured only acquires a right to sue for the money when his liability to the injured person has been established so as to give rise to a right of indemnity. His liability to the injured person must be ascertained and determined to exist, either by judgment of the court or by an award in arbitration or by agreement. Until that is done, the right to an indemnity does not arise'.

[4] For example, *Bankers Insurance* v *South* [2003] EWHC 380 (QB), [34]: 'Clearly these clauses are important to insurers. Non-compliance by the insured can hopelessly prejudice the insurers' right of subrogation and chance of recovery from another party'.

[5] The academic commentary on claims conditions is broadly supportive of some form of proportionate remedy, at least as an option. See eg J Birds, 'Innominate terms in insurance contracts' [2006] JBL 545; J Lowry and P Rawlings 'Innominate terms in insurance contracts' [2006] LMCLQ 135 and J Davey 'Insurance claims notification clauses: innominate terms & utmost good faith' [2001] JBL 179. The leading orthodox account of the current position is R Merkin and O Gurses 'The Insurance Act 2015: rebalancing the interests of insurer and assured' (2015) 78 MLR 1004.

[6] The modern insurance warranty regime is found in s. 10 Insurance Act 2015, replacing s. 33 Marine Insurance Act 1906.

For claims co-operation clauses:

(a) The breadth of the duty to co-operate at the claims stage, and especially, the duty to maintain and share relevant information.[7]

(b) The remedy for non-compliance.

Each of these elements is determined by a process of contractual interpretation. There is no statutory framework for such clauses, unlike basis clauses or insurance warranties. As a matter of general contract law, this process considers the wording of the clause and wider document and the commercial context in which the agreement occurred.

The wordings vary,[8] but a notification clause might (for example) require notice of 'an event likely to give rise to a claim'[9] with notice 'as soon as reasonably possible'.[10] A claims co-operation clause might (additionally expect) 'any further information we may reasonably require; any assistance to enable us to settle or defend a claim'.[11] The remedy for non-compliance depends on the classification of the term, and this generates considerable litigation. The orthodox explanation is that such clauses are innominate terms,[12] unless otherwise stated. Despite this classification, the remedy granted has been (invariably) damages to reflect the prejudice caused to the insurer as a result of late notice or non-compliance, rather than termination (a potential remedy for innominate terms).[13] The standard alternative classification

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[7] One issue is what documentation should be preserved for potential use by an insurer. The High Court in *Cuckow* referenced (in some detail) the decision of HHJ Peter Leaver QC in *Widefree Limited* v *Brit Insurance Limited* [2009] EWHC 3671, [100] (QB): 'If an insured knows, or should know, that evidence or information is or might reasonably be required by his insurers and does not retain it, that insured runs the risk of being unable to satisfy the condition precedent'.

[8] See, for example, *Kajima UK Engineering Ltd* v *The Underwriting Insurance Company Ltd* [2008] EWHC 83 (TCC): "The Insured shall give written notice to the Underwriters as soon as possible after becoming aware of circumstances which might reasonably be expected to produce a claim or on receiving information of a claim for which there may be liability under this insurance. Any claim arising from such circumstances shall be deemed to have been made in the Period of Insurance in which such notice has been given".

[9] On which see *Zurich Insurance* v *Maccaferri* [2016] EWCA Civ 1302, [16] and the discussion of *Layher Ltd* v *Lowe* [1996] EWCA Civ 1231 and *Jacobs* v *Coster (t/a Newington Commercials Service Station)* [2000] EWCA Civ 3042.

[10] 'As soon as possible' has been treated generally as equivalent to 'as soon as reasonably possible', taking into account the wider context. See *Verelst's Administratrix* v *Motor Union Insurance Company Limited* [1925] 2 KB 137.

[11] This wording was used in *Cuckow v AXA Insurance Plc* [2023] EWHC 701 (KB).

[12] *Cuckow*, at [94], assumed that unless the term was a condition precedent, the only remedy for breach would be for damages.

[13] In the authors' view, this makes them contractual warranties, as no judge has been able to describe a set of circumstances in which breach would terminate the relationship. That is normally a key element in a term being classified as innominate- that both minor and major breaches can be envisaged. This nicety does not matter for the arguments made in this short piece.

is for the clause to be a condition precedent to the insurer's liability for related claims. If classified as a condition precedent then the insurer need not show any prejudice to its position to deny the claim.[14]

Recent case law shows the significance of the classification: *Cuckow* v *AXA Insurance UK PLC*[15] and *Arch Insurance (UK) PLC* v *McCullough*.[16] Each arose in the field of liability insurance, with the insurer denying liability to a third-party claimant on the basis of the insured's (or their representative's) failure to comply with claims conditions. In *Cuckow*, the insurer's defence was that the insured's representative (the insolvency practitioner managing the insured's business) had failed to supply relevant documentation to the insurer at the claims stage.[17] The precise limit of what documents had to be presented was contentious. The High Court paid considerable attention to the classification of the claims cooperation clauses as conditions precedent. The courts have given effect to wording that 'demonstrates a clear intention to give a clause the status of a condition precedent'.[18] The significance of this to the underwriter's liability was recognised, and MacGillivray suggests that any ambiguity is resolved by reading the clause *contra proferentem*, and presumptively against the insurers. In *Cuckow,* the label of 'Policy Conditions' combined with the warning that the insured 'may lose all right to recover under your policy' for non-compliance was considered sufficient to categorise the term as a condition precedent.

However, the phrasing would also describe the effect of a true contractual condition, whereby breach might lead to the termination of the policy. It would also fit with some well-known cases on the innominate term,[19] as the word 'may' might equate to 'if sufficiently serious'. That is, according to the current texts, the default classification for such terms.

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[14] *Pioneer Concrete* v *National Employers Mutual General Insurance Assocn Ltd* [1985] 1 Lloyd's Rep 274: 'as a matter of general contractual principle, it appears to me that [prejudice] cannot be required of an insurer before he relies on a breach of a condition precedent in the policy'.

[15] Above, n 11.

[16] [2021] EWHC 2798 (Comm).

[17] The contract required supply of 'any further information we [the insurer] may reasonably require'. The insurer had requested survey documentation related to the insured's installation of cavity wall installation related to claims stretching back several years, but within the relevant limitation period.

[18] This is derived from J Birds, B Lynch and S Paul *MacGillivray on Insurance Law* (15th ed, 2022), reviewing *Welch* v *Royal Exchange Assurance* [1939] 1 KB 294; *Denso Manufacturing UK Ltd* v *Great Lakes Reinsurance (UK) Plc* [2017] EWHC 391 (Comm) and *George Hunt Cranes* v *Scottish Boiler* [2002] EWCA Civ 1964.

[19] *Schuler AG* v *Wickman Machine Tool Sales Ltd* [1974] AC 235, although the outcome in that case was affected by conflicting clauses on the contractual process for termination following a potentially repudiatory breach, with the possibility of remedial action.

In *McCullough*, the operator of a motorsport facility was aware of a serious accident on the track but had understood that no legal action would result, following what he had seen as reassurance from the family. Nonetheless, the events were seen as sufficiently likely to generate a claim that notice should have been given at or around the time of the injury, and not delayed for almost a year.

The notice clause was viewed as a condition precedent. It was described- along with all other duties of the insured- as a condition to any liability of the company.[20] The full terms of the policy are not included in the judgment, but earlier authority has recognised that an overly inclusive term (such as that above) may not have the generalised effect stated, where the clauses concerned lacks the commercial rationale for treating it as a condition precedent.[21]

IV. Limited (Effective) Regulation Under Current Law

This section reviews the limited ways in which insurance law and regulation controls the insurer's ability to deny a claim on the basis of a failure to give timely notice by the insured. Some are limited to consumer insurance.

1) Unfair Terms Legislation

A broadly drafted claims notification clause which was characterised by the contract as a 'condition precedent' to liability was found to be an unfair contract term in *Bankers Ins* v *South*.[22] Buckley J noted that:

> 'a breach by the insured may not prejudice the insurer. Even very late notification, may not necessarily cause difficulties. Thus these clauses may deprive an insured of the benefit for which he bargained or provide the insurer with a bonus, simply because the insured has transgressed procedurally, but without prejudice to the insurer'.[23]

[20] 'Observance of the terms of this certificate relating to anything to be done or complied with by the insured is a condition to any liability of the company…'
[21] See *Cuckow*, [40] and its discussion of *In re Bradley and Essex and Suffolk Accident Indemnity Society* [1912] 1 KB 415.
[22] Above, n 4.
[23] At [34]. As noted above, he did not deny that these clauses had a real commercial purpose but is stating that those genuine grounds for protecting insurers in some circumstances is not a universal justification for the loss of the claim. There is, on this view, the need for a proportional outcome.

The clause was therefore unenforceable against the consumer insured. The current iteration of this rule is found in s. 62 of the Consumer Rights Act 2015. There is no equivalent rule for commercial markets, as the Unfair Contract Terms Act 1977 does not apply to insurance contracts.[24] A vulnerable third party, such as a consumer or employee seeking to enforce a commercial liability insurance policy by way of the Third Party (Rights Against Insurers) Act 2010, would not be able to rely on the Consumer Rights Act, as the contract is a commercial policy.

2) Notice by the Third Party under s. 9, Third Party (Rights Against Insurers) Act 2010

In circumstances where the harm to an injured third party is immediate, obvious, and serious it is likely that solicitors for that claimant will be instructed within a short time frame. Where the insured company is then insolvent, it is possible (under s. 9 of the Third Party (Rights Against Insurers) Act 2010) for the third-party to give notice to the insurer and discharge the duty of the insured to do so.[25] This is far from a comprehensive solution:

(a) The third-party may not be able to identify the relevant insurer (without co-operation from the insured). The statutory regime does assist here,[26] but there may be practical difficulties.
(b) The third-party may not have sight of the specific requirements under which notice is due.
(c) The insured may not be insolvent until after the period in which notice should have been given.

3) Section 11, Insurance Act 2015

Of all the reforms instigated by the Insurance Act 2015, section 11 is the least certain in ambit. It is the authors' view that it does not regulate the enforceability of many liability policy claims conditions, but that may not be universally true.

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[24] UCTA 1977, Sch 1 excludes the operation of ss. 2 and 3 to insurance contracts.
[25] S. 9 states:
'(1) This section applies where transferred rights are subject to a condition (whether under the contract of insurance from which the transferred rights are derived or otherwise) that the insured has to fulfil.
(2) Anything done by the third party which, if done by the insured, would have amounted to or contributed to fulfilment of the condition is to be treated as if done by the insured'.
[26] S.11, Third Party (Rights Against Insurers) Act 2010. There are further measures related to liability insurance in the ICOBS rules governing claims in the liability insurance space.

Section 11 has a series of requirements which, if met, prevent the insurer from relying 'on the non-compliance [with a contract term] to exclude, limit or discharge its liability under the contract'. This has (at least potentially) a significant regulatory effect.

The first requirement is section 11(1) which governs the nature of clauses regulated. The clause broken by the insured must not be a term 'defining the risk as a whole' **and** one which has the function of reducing risk of a particular kind and/or loss and/or at a particular time. The application of section 11 to notification clauses is not straightforward. It was intended to control insurance warranties and suspensive conditions mitigating specific risks in property insurance policies.[27] Many notice clauses appear as a requirement to any claim under the policy and are likely to be treated as defining the risk as a whole. A clear counter-argument (reflecting the decision in *Banker Ins* v *South* above)[28] is that the limits of the risk assumed is conceptually distinct from the technical procedural requirements of submitting a claim. Put succinctly, claims notification clauses might be treated as defining the insurer's liability, but not the risk transferred. Limitation and aggregation clauses, among others, might be considered in the same way.

Even if a notification clause does not define the risk as a whole, it may well have the effect of controlling losses of a particular kind, at a particular location, or at a particular time. Whilst this issue has not yet been litigated, our expectation is that this regulatory oversight will be interpreted narrowly. This would constitute an interference with freedom of contract in a commercial context, and the judicial approach to analogous issues arising under the Unfair Contract Terms Act 1977 has shown a notable reluctance to intervene in many cases.[29] Assuming that a court could be persuaded that a claims notification clause fell within s. 11(1), it is much easier to identify situations where the kind of breach that occurred would not have increased the risk that the insurer incurred. *BAI*[30] is good example of a situation where late notice did not obviously cause substantial prejudice to insurer's position, not least when

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[27] A classic example is *Kler Knitwear* v *Lombard General Insurance* [2000] Lloyd's Rep IR 47 where non-compliance with a sprinkler maintenance warranty would have an obvious commercial purpose effect on the risk of fire, but not wind and storm damage.

[28] Above, n 4.

[29] There is a nuanced position here as shown by a recent decision of the Court of Appeal: *Last Bus Ltd* v *Dawsongroup Bus and Coach Ltd* [2023] EWCA Civ 1297, [45]-[46]. The starting point is: 'In commercial matters where the parties are of equal bargaining power, the parties are free to apportion risk as they see fit without judicial intervention, including by way of exclusion clauses'. There are contrary situations, where regulation does bite.

[30] *McAlpine* v *BAI* [2000] EWCA Civ 40.

considering its response to notification when provided. On the facts, the High Court viewed the contemporaneous factual account provided by a Health & Safety Executive investigation was sufficient to protect the insurer's position in general terms.[31] On this basis, the insurer's decision to deny liability would be subject to regulation, and so it is the application of s. 11(1) that it the real limiting factor.

4) Regulatory Controls under the Financial Services & Markets Act 2000

The Financial Ombudsman Service provides a genuine alternative route (to the courts) in resolving disputes of this kind. It has jurisdiction over a growing range of commercial policies and can make mandatory awards up to £430,000.[32] Its decisions are based on a mixture of the current legal position and what it judges to be 'fair and reasonable'. Whilst it has no formal system of precedent, there is some evidence of a consistent practice in this area:[33]

(1) To treat s. 11 Insurance Act 2015 as routinely applicable to late notification disputes; and
(2) Even where s. 11 was not applicable (because the contract pre-dated the entry into force of the 2015 Act), to require the insurer to show prejudice.

The decision in DRN-1902870 provides a useful example, with some similarities to *McCullough*. In June 2014, a financial services provider received a complaint from a customer, with potential litigation mentioned. Shortly after, the customer confirmed verbally and in writing that it would not be pursuing a claim. This was not notified at the time to the relevant liability insurer. In August 2014, further contact suggested that a claim would be brought. This was notified to the insurer. Legal action was initiated in 2017. The insurer denied cover for a failure to give notice in June 2014. The Ombudsman decision- based on what was fair and reasonable, rather than the strict legal position- turned on whether that failure was prejudicial. It decided: 'it would [NOT] be fair to reject the claim when no steps had been taken at all and the position was exactly the same. Amtrust was able to consider the claim in August 2014 in the same way as it would have done in June'. The presence or absence of prejudice has also

[31] [1998] 2 Lloyd's Rep 694, per Colman J at 703: 'The information and evidence might be less readily available than would otherwise have been the case…' but not 'so substantially unobtainable as to render [the insurer] incapable of taking over and effectively running the defence to the claim'.
[32] https://www.financial-ombudsman.org.uk/consumers/expect/compensation (as of 06/10/24).
[33] In addition to DRN-1902870 considered in the text, see DRN3686641. This aligns with the practice of previous Ombudsmen: see Colinvaux & Merkin, [C-0253] citing IOB Bulletin No.3, 1994, p.7.

been applied as a factor in relation to claims co-operation disputes.[34] This goes considerably beyond the formal legal position, even when the regulatory controls in ICBOS 8 are included in the analysis.[35] In cases of late notice or a lack of claims co-operation classified as a condition precedent, the insurer need only prove breach and not any prejudice to its position.

V. What Next?

The claims condition is in a liminal state. The 'innominate term' version provides too limited a remedy. Insurers, even when subject to demonstrable prejudice, might only receive a relatively small reduction in their liability by way of a counter-claim in damages.[36] The condition precedent version provides an absolute defence, irrespective of the prejudice suffered. A fair outcome relies, in some cases, on insurers not enforcing their strict contractual rights. We can do better. The goal here should be to provide a regime that provides insurers with sufficiently protective remedies for breach (beyond the mere award of damages). The current 'condition precedent' regime provides a complete defence to liability, enabling insurers to make any *ex gratia* settlement they choose. A reformed system would seek to provide a suitable middle ground. Parties can then decide to use the proportionate regime, or either of the two existing models, as they see fit. The problem is that the law fails to provide a neutral rule as a starting point for negotiation.

There are bespoke solutions by way of contractual drafting, and these often restrict the duty to provide notice. We have been shown various clauses of this nature. Bespoke clauses create drafting costs and uncertainties before they are enforced by litigation. They do not remove the need for a generalised solution, by the design of a more tailored remedy. The Court of Appeal in *McAlpine* v *BAI* (led by Waller LJ) sought to develop a proportional common law rule for claims conditions.[37] Whilst not completely fleshed out, his model was in the form of a modified innominate term, where serious breach permitted rejection of the claim (rather than termination of the contract):

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[34] On claims co-operation clauses, DRN1330932 discusses the relevance of prejudice to the final decision.
[35] *Komives* v *Hick Lane Bedding Ltd* [2021] EWHC 3139 (QBD).
[36] *Nulty* v *Milton Keynes BC* [2011] EWHC 2847 (TCC).
[37] [2000] EWCA Civ 40

> 'one should consider the possibility that a breach . . . might in some circumstances be so serious as to give a right to reject the claim albeit it was not repudiatory in the sense of enabling BAI to accept a repudiation of the whole contract'.[38]

This was reversed by a subsequent Court of Appeal decision, where Mance LJ persuaded the majority that the particular form of innominate term that Waller LJ imagined was incompatible with the common law of English contract.[39] Given that the common law has tried and failed to create a proportional outcome, consideration should be given to a statutory reformulation. As with the Insurance Act 2015 generally, these would be default rules, and capable of being varied (provided the necessary formalities were met)[40] by contrary agreement. The kind of binary 'off / on' rules for insurer liability that were the stuff of traditional insurance contract law were reformed under the 2015 Act and replaced with a proportional remedy. Claims conditions have been left unreconstructed, unduly in our view, given the significant impact they can have in the context of liability policies. A potential line of statutory development can be taken from the example of s.15A Sale of Goods Act 1979. This limits commercial buyers' ability to reject non-compliant goods where 'the breach is so slight that it would be unreasonable for him to reject them…'[41] and might be repurposed. It has not led to a noticeable uptick in litigation.[42] It does not tilt the balance in favour of any party but simply creates a proportional default around which parties can negotiate. This, in our view, would represent a workable solution for the claims conditions problem and align their treatment with other areas of insurance contract law following the 2015 Act.

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[38] At [26] per Waller LJ.

[39] *Friends Provident Life & Pensions Ltd v Sirius International Insurance* [2005] EWCA Civ 601. This viewed Waller's variant on innominate terms as reliant on a heretical form of partial termination of the contract. This view is not universally accepted. See M Hemsworth (ed.), *The Law of Insurance Contracts*, [26-2G5] 'Partial Discharge: the Wider View'.

[40] Ss. 16-19 Insurance Act 2015.

[41] Sale of Goods Act 1979, s.15A(1)(b)

[42] There have been very few cases on the provision since its introduction some thirty years ago.