

Duty to take reasonable care not to make a misrepresentation to an insurer

Recommendation

Recommendation 4.5

Part IV of the Insurance Contracts Act should be amended, for consumer insurance contracts, to replace the duty of disclosure with a duty to take reasonable care not to make a misrepresentation to an insurer (and to make any necessary consequential amendments to the remedial provisions contained in Division 3).

Existing law

An insured is required to disclose matters known to the insured that are relevant to the insurer's decision of whether or not to accept the risk and, if so, on what terms (Insurance Contracts Act, section 21).

A modified duty of disclosure applies to "eligible contracts of insurance" (section 21A).

"Eligible contracts of insurance" under the Insurance Contracts Regulations 2017 are:

- motor vehicle insurance;
- home buildings insurance;
- home contents insurance;
- sickness and accident insurance;
- consumer credit insurance; and
- travel insurance.

Under the modified duty of disclosure, the insurer may request the insured to answer specific questions relevant to the risk, and if the insurer fails to do so in relation to a relevant matter, the insurer waives the insured's duty of disclosure in relation to that matter.

When answering a question, the insured should disclose each matter known to them and that a reasonable person in their circumstances could be expected to disclose in relation to the question.

Summary of proposed reform

There will be a new duty on consumers to take reasonable care not to make a misrepresentation when entering into, varying, extending or renewing a consumer insurance contract.

This duty replaces the existing duty of disclosure.

The new duty applies only to contracts of insurance (including general and life insurance contracts) obtained for the insured's personal, domestic or household purposes.

This new duty is limited to responding to specific questions asked by the insurer, including that the insured confirm or update information previously given to the insurer when entering into, varying, extending or renewing an insurance contract.

Comments

- The reforms expand and replace the current disclosure regime for eligible contracts of insurance to all general and life policies (including group life policies) that are sold to consumers for their personal use. This means that the general duty of disclosure for these types of insurance will be replaced by a regime that only requires the insured to take reasonable care not to make a misrepresentation. Insurers will need to adjust their application processes accordingly.
- The most significant effect of these changes is that insurers will need to assess, when considering claims, whether any misrepresentation that has been made has involved a failure to take reasonable care on the part of the insured. In doing so the insurer will be required to have regard to "all relevant circumstances" which is to include factors such as the type of insurance applied for, how it was applied for, the target market involved, the quality of the materials provided by the insurer, the clarity and specificity of the questions asked and how clearly the insurer explained the consequences of answering questions.
- This new assessment process is likely to pose implementation challenges for insurers and an increased compliance risk given the separate introduction of the new claims handling as a financial service laws and the position that insurers will now be subject to the enhanced civil penalty regime if they are not seen to discharge their obligation to act efficiently, honestly and fairly in making assessments of reasonableness of care under the new disclosure standard. At the very least, the new disclosure regime will make it harder for insurers to rely on pre-contractual misrepresentations made by their insureds and easier for insureds to challenge insurers' decisions to reduce or avoid liability for claims through bodies such as AFCA.