Insurance Act 2015 - Ellipse's philosophy and practice and what that means for employers

The Insurance Act 2015 comes into effect on 12 August 2016, which means any new policy which starts on or after that date will be subject to the Act, along with any rate review or change to an existing policy effective on or after that date.

It is a major change in insurance law. In fact it is one of the most significant changes to insurance law for over 100 years, and it will affect all non-consumer insurance contracts, including the products Ellipse offers. Its purpose is to bring the law in line with best practice in the insurance market and therefore crucially it reflects all of the things that Ellipse are already doing.

Main changes introduced by the Act

1. The duty of fair presentation

The Act requires that before entering into an insurance contract the customer has a duty to present the risk to the insurer in a fair manner. This means they must tell the insurer about all material facts in a clear and accessible manner and not misrepresent any material facts and if they don't have complete information they must tell the insurer so.

A material fact is something that would influence the insurer's judgement whether or not to offer cover and if so on what terms.

The customer must tell the insurer every material fact that is known, or ought to be known by them, by any of their "senior management" or anyone responsible for insurance within the organisation. This means that they must make a reasonable search of their records and their adviser's records to determine this.

To help employers with this obligation, when establishing a new policy Ellipse provides a pre-populated application form which includes all of the information that we regard as a material fact, for example, information about employees absent through ill health and overseas business travel. They must then check that this information is accurate and complete in accordance with the Act, before presenting it to us. For a rate review or policy change this information is included on the quote/policy change form and/or application form.

2. New remedies for the non-disclosure of material facts

The Act brings in new remedies for insurers in the event of the non-disclosure of a material fact by a policyholder to the insurer. It defines non-disclosure into two different classifications:

- Deliberate or reckless non-disclosure
- Non-deliberate/ not reckless non-disclosure

It is considered deliberate or reckless if the potential policyholder knew they were in breach of their duty of fair presentation or didn't care whether or not they were in breach of this duty. If they are considered deliberate or reckless then the insurer can cancel (avoid) the policy from the start and keep the premium. If they were deliberate or reckless at a rate review the insurer can cancel (avoid) the policy from the rate review date.

For example, an employer approaches Ellipse to insure their 30 employees for a group life benefit of 4x salary, for which Ellipse quotes a premium of £5,000 per annum. Ellipse provides them with a pre-populated application form to sign before cover starts, which shows that there were no employees absent from work as disclosed when the quote was obtained. The employer then signs the form and the policy starts. One month later an employee dies. The employee was a colleague of the director who signed the application form and had been absent for four months receiving treatment for cancer, their benefit is £350,000. The director who signed the application form was aware of the employee's absence, knew it was likely to affect the insurance, but chose nevertheless not to disclose the information when they signed the form. In this case the disclosure is deliberate/reckless and Ellipse would cancel the policy from the outset and no benefit would be paid to the employee's family, although the premium will be refunded.

If it is not deliberate or reckless, the Act allows the insurer to re-assess the risk based on all of the facts. If this would have resulted in the insurer not offering terms, the insurer can cancel the policy from the start, but they must pay the premium back to the policyholder.

Alternatively, if the reassessment would have resulted in the insurer offering terms on a higher premium the Act allows the insurer to reduce the claim amount proportionately. We do not think this is fair to the employee and their family, as they would receive less benefit through no fault of their own.

As a result Ellipse have contracted out of this part of the Insurance Act 2015 (Schedule 1 paragraphs 6 and 11). This allows us, in this scenario only, to charge the higher premium to the employer and pay the claim in full, which is what we will do. This decision to contract out only affects the reassessment of non-deliberate/not reckless non-disclosure where terms can be offered at a higher premium. We feel this is the right approach given the specific circumstances of group insurance cover, which naturally cannot be reflected in legislation designed for all insurance contracts, hence why the legislation allows insurers to opt out of this section.

In the example above, if the non-disclosure was considered not deliberate, Ellipse would reassess the risk based on the information now available, as if it had been provided on the application form. In this case due to the large benefit (£350,000) and small premium (£5,000) Ellipse would not have offered cover had they known, so the policy will be cancelled from the start date and premiums paid returned to the employer. However, if a different employee was absent with a much lower benefit, perhaps £7,000, then Ellipse may have provided terms at the outset but at a higher premium e.g. £6,000. Rather than pay a proportionately lower amount to the employee's family – e.g. £5,833 – Ellipse will pay the full £7,000, but charge the employer the additional £1,000.

3. Fraudulent claims

The Act also clarifies the remedies available in the event of a fraudulent claim.

If the policyholder makes a fraudulent claim the insurer does not have to pay the claim and has the right to cancel the policy and recover any benefit already paid in respect of the claim. This is the process already adopted by Ellipse.

If there is a fraudulent act by an individual employee, for example, they provide false information when completing an individual medical assessment and there is a claim, Ellipse will not pay that claim but cover would remain in place for other employees covered by the policy.

Ellipse's philosophy and practice

As the principles of the new Act are already incorporated into Ellipse's policies and processes, the introduction of the Act means there is no change in how we treat our policyholders.

However, as described above, because the specific terms of the Act with regard to the remedies in the event of non-deliberate/not reckless non-disclosure, in our view, are not in the best interests of the employees covered by our group insurance contracts, we have contracted out of Schedule 1, paragraphs 6 and 11, of the Insurance Act 2015.

In order to contract out of this part of the Act, we must inform policyholders in advance of the policy starting, the rate review date or at any other time when a policy change is made. For new policyholders, the quotation and application form provided will explain why we are contracting out, but advisers may wish to explain this to employers in advance. This guide for employers may be useful. For existing policyholders, we will email their nominated adviser in advance of the rate review date, or date the policy change becomes effective, to notify them of the change.

What this means for employers

As we do currently, we will always ask the employer to provide the information we need to assess the risk. The pre-populated application form lists all the information which we regard as a material fact and the employer has a duty under the Insurance Act 2015 to answer these questions fairly, which includes making reasonable searches of their records (and their adviser's records) to provide us with the information we have asked for.

Therefore employers must take extra care when answering our questions and completing our application form, and advisers should inform them of this duty. If employers do not undertake these searches and provide us with inaccurate or incomplete information, this is regarded as non-disclosure and we will be entitled to implement the remedies described above.