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Briefing note March 2017

Damages for Late Payment of Insurance Claims: Time for change

May 2017 heralds a long-awaited change to the law on the payment of insurance claims, with the introduction of a remedy in damages where claims are paid late. The change follows hot on the heels of the Insurance Act 2015, which has led to many insurers revisiting their policy wordings, and to insureds considering how they collate and present information to insurers. This time it is the handling of claims which will come under scrutiny.

Need for a new Remedy

The change is brought about by section 28 of the Enterprise Act 2016, which introduces a new section 13A into the Insurance Act 2015 (the Act). It will result in a term being implied into insurance contracts entered into after 4 May 2017 that the insurer "*must pay any sums due in respect of the claim within a reasonable time*". The change in the law was made because under the current law- exemplified in the leading case of *Sprung v Royal Insurance (UK) Ltd*- an insured's only remedy in the event that an insurer is late paying a claim is for interest on the sum paid. The government felt this could cause real hardship to insureds- in Mr Sprung's case the insurers' delay in paying out a valid claim after damage at his factory put him out of business. The delay therefore caused him to suffer considerable extra losses, which were irrecoverable. For policies issued after May 2017, insureds in Mr Sprung's position will be able to claim that such a delay is a breach of the implied term, and therefore claim damages for any additional losses they suffer.

Scope of the Change

The Act makes sensible propositions about when it should apply, but lacks specific guidance on how any particular case should be handled:

- The Act doesn't provide any clear definitions of what is "reasonable time", and that is likely to be a key battleground in any claims brought under this provision.
- The Act does give a list of examples of things which may need to be taken into account, for this purpose, namely the type of insurance, the size and complexity of the claim, compliance with any relevant statutory or regulatory rules or guidance and factors outside the insurer's control.
- The Act also makes it clear that merely not paying a claim while a dispute is continuing will not be enough to show a breach of the implied term, but the conduct of the insurer when handling the claim will be a relevant factor.

Practical Effect

It therefore remains to be seen how this will affect insurers' claims handling processes in practice

- Investigating insurance claims can take time, particularly for complex or high-value claims, and the reasons for that may not always be obvious to the policyholder.
- The threat of damages for late payment might result in faster payments in some instances, but we also expect to see insurers taking a more careful approach to documenting their claims handling and explaining it to insureds.
- When the Law Commission originally proposed the change, some insurers expressed concerns that they would be subject to speculative claims.

Settlement of Disputed Claims

One key feature of the right to claim damages for late payment is that it can be exercised up to a year after a claim is paid. This creates a potential area of concern for insurers, who will not be able to close their files after they have paid out with the comfort that all their potential liabilities have been discharged. It is possible for the insured and the insurer to agree to exclude the right contractually at the time of making payment, and so one consequence of the Act may be an increase in insurers asking insureds to sign releases or settlement agreements as a condition to making payments. Unless the wording of a policy states otherwise, insurers have no right to insist on insureds signing such documents, although it is common practice to do so. It may well be that the practice of asking insureds for such releases becomes standard once the Act takes effect- although insureds should always consider carefully before giving up rights in this way.

Contracting Out

Finally, it should also be noted that it is possible to contract out of these new provisions for non-consumer insurance, provided that the breach is not deliberate or reckless, and provided that the transparency requirements under the Act are met. The transparency requirements require that the term is clear and unambiguous as to its effect, and that the insurer has taken sufficient steps to draw the disadvantageous term to the insured's attention. The question for any insured asked to agree to such a variation is essentially a commercial one, but the justifications for contracting out are less obvious than they are for many of the other provisions of the Act. Whereas the other Act provisions mitigate the remedies available to insurers in the event of an insured failing in its obligations, this is a provision concerned with compensating an insured where an insurer's claims handling has been so slow that the delay itself causes additional loss to an insured. Insureds would be well-advised to consider carefully before agreeing to contract out of this right, as that effectively means they are agreeing to bear the financial consequences of any unreasonable delay by insurers.

For more information on the changes brought about by the Insurance Act 2015 please click here

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