

## BRIEFING

# Damages for the late payment of insurance claims: the final frontier

In July 2014 the Law Commission made recommendations in four areas of insurance law. Most of these were incorporated into the Insurance Act 2015, which was given royal assent on 15 February 2015.

However, the provision relating to the late payment of insurance claims was criticised by the insurance industry and deemed too controversial to write into law at the time. Parliament promised to revisit the issue at a later date and now, by clauses 20 and 21 of the proposed Enterprise Bill 2015, it has done exactly that. If passed, the new act will introduce amendments into the Insurance Act 2015 which will enable policyholders to claim for damages caused by the unreasonable delay in payment of a valid insurance claim.

### The need for change

The change is long overdue. Currently, and for reasons to do with the convoluted development of insurance law in England and Wales, where a valid insurance claim is made the policyholder is only entitled to the sum owed under the policy plus interest. There is no remedy for additional losses caused by an unreasonable delay in payment by the insurer.

The Law Commission was particularly concerned about the vulnerability of small businesses in these circumstances. SMEs are often highly geared and therefore extremely exposed to commercial pressures when negotiating the settlement of their insurance claims.

The Law Commission also noted that the law of England and Wales is out of step with the law in other jurisdictions, including Scotland, where there is a legal obligation for insurers to pay out within a reasonable time period. The current law also contradicts the stance taken by the Financial Ombudsman Service (FOS) and the FCA, which require the fair and prompt handling of claims.

### The implied term

The proposed provision would imply a term into every insurance contract. The term would place insurers under a duty to pay policyholders with valid claims within a reasonable time.

The definition of a 'reasonable time' will depend upon the circumstances of the particular claim, and will be determined by the following factors:

- The size and complexity of the claim;
- Compliance with any relevant statutory or regulatory rules or guidance;
- Factors outside the insurer's control.

Insurer conduct throughout the claims process will also be considered and a defence will be available if "reasonable" grounds exist for disputing a particular claim. What is reasonable in this context has been left deliberately open, but clearly insurers will be allowed ample time to investigate legitimate areas of concern.





If there has been an unreasonable delay in making a payment, in order to claim additional financial loss the policyholder must also show that:

- It has a valid claim;
- The insurer is responsible for unreasonable delay. The insurer must have had sufficient time to carry out a full investigation, including time to seek information from third parties;
- The policyholder has suffered actual loss in addition to the loss claimed under the policy. This would never be presumed and must be established in each case;
- The loss was caused by the unreasonable delay;
- The loss was foreseeable, in that it was within the 'reasonable contemplation' of both parties at the time the contract was made;
- The policyholder took all reasonable steps to mitigate its loss, including (if possible) borrowing money for repairs where necessary.

It is not possible to contract out of the implied term in consumer contracts. It will however be possible to contract out of the late payments provisions in commercial contracts, provided the transparency requirements in section 17 of the Insurance Act 2015 are met. These state that the insurer must draw attention to the disadvantageous term before contracting, and ensure the relevant term is clear and unambiguous in its effect. Any attempt to contract out of the provisions will be void if the insurer delays the payment deliberately or is reckless as to the delay.

### The effect on SMEs

Late payment has little effect on big businesses, which usually have sufficient cash-flow to withstand delays in payment and, perhaps more importantly, the power to negotiate with insurers on equal terms. At the other end of the scale, consumers and 'micro-enterprises' (i.e., those that employ fewer than 10 staff and have an annual turnover of less than 2 million euros) can complain to the FOS and obtain compensation of up to £150,000.

Accordingly, the new provisions aim to protect small businesses with no access to substantial financial resources or to the FOS. The implied term gives insurers an incentive to deal with these claims in a timely manner that is sensitive to the risk felt by small businesses at this crucial time.

The Government Impact Assessment states that the majority of insurers are already compliant with the proposed term and therefore doubts that insurers will seek to contract out of the implied provision in practice. That might be an overly generous view. Arguably the main reason why the provisions will be adopted is because the alternative is so unattractive: an insurance policy which expressly states that the insurer does not agree to pay valid claims within a reasonable timeframe is hardly the most marketable commodity.

The Enterprise Bill 2015 had its first reading in the House of Lords on 15 September 2015 and the second reading is due to take place on 12 October 2015. Should it pass through Parliament and obtain royal assent, it will come into force one year after it is passed.

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