

Pre-contractual disclosure:

What is the scope of an insured's pre-contractual duty of disclosure at common law and under the ICA?

Common law:

- *There is no CL requirement for pre-contractual disclosure in relation to contracts generally.
- *Pre-contractually, utmost good faith operates as a legal mechanism to achieve a true and fair agreement for the transfer of risk by requiring insurer and intending insured to exchange material information about the risk before entering into an insurance contract, and again before renewing, extending or varying it (Prepaid Services v Atradius).
- *Utmost good faith requires each of them to:
 - voluntarily disclose to the other info known to them which is material to the risk to be transferred; and
 - not to misrepresent info material to the risk to be transferred.
- Info known to an intending insured includes info:
 - They actually know and that they would have known if they had not wilfully shut their eyes to the truth (Economides v Commercial Union)
 - Their relevant agent knows i.e. what their insurance broker knows, even if the broker acquired that knowledge before the agency relationship commenced; is known by the insured's employee or by an agent appointed by the insured to arrange the insurance or manage its subject matter.
- Info known to an intending insured does not include info they do not know even if: in the ordinary course of business they ought to know it or they would have become aware of it if they had made some inquiries for the purpose of discovering it.
- Intending insured will discharge the duty if they make a fair presentation of the risk to the insurer (Iron Trades Mutual Insurance). The fairness test is objective, it does not depend on what an insured thinks is fair.
- Insurer cannot waive an insured's obligation to make a fair presentation, but it can limit the scope of the obligation by waiving its need for certain info (Wise Underwriting).
 - It can do so by specifically informing the intending insured that it does not require specific info, or as a consequence of the range of questions asked in a proposal for insurance or of the answers to them (Schoolman v Hall).
 - Meaning of the insured's answer is to be determined objectively, considering the Q and answer – what a reasonable proponent would fairly have understood it to mean and the answer by reference to what that reasonable person would fairly have understood it to convey (Condogianis v Guardian Assurance).
- If intending insured gives an incomplete or vague answer to a question in a proposal, the fact that a reasonably careful insurer would follow up but the insurer

did not, might lead a court to conclude that there was a fair presentation of the risk, or the insurer waived the need for further disclosure on that issue (Wise Underwriting).

- Even if the fact is material, intending insured is not required to disclose a fact that the insurer ought to know:
 - From publically available sources of info such as media.
 - Because it insures a particular industry and the fact relates to practices of that industry or is well known by persons in that industry, and
 - Because it insures a particular class of business and the fact relates to the risks that affect that class of business.
- Unless a policy contains an express term to the contrary, an insured is not obliged to disclose changes in the risk that occur during the insurance period (material or otherwise) (Ferrcomm v Commercial Union).
 - Policy will not cover the changed risk if it takes the risk outside that which was in the reasonable contemplation of the parties at the time the policy was issued (Ansari v New India).
- Pre-contractual duty of disclosure arises in relation to:
 - An agreed variation of the risk during the period of insurance. Any remedy for a breach of the duty of disclosure or for misrepresentation in relation to the variation is limited to the variation; it does not affect the original contract (Mercandian Continent)
 - Renewal of an insurance contract. Unless informed otherwise, an insurer is entitled to assume that the answers in the original proposal for the insurance apply to the renewal (Alexander Stenhouse; Mercantil Mutual Insurance v Gibbs)
- *A breach of the duty of disclosure can be innocent, negligent or fraudulent.
- *Whether a party has not disclosed or has misrepresented a material fact is a question of fact (WA Insurance Company v Dayton).

What is a material fact?

- *Determining whether a fact is material is a two-staged process (Akedian Co v Royal Insurance):
 - (1) Court must decide whether, in the circumstances (including the knowledge, practice and conduct of the insurer), the non-disclosed or misrepresented fact would have reasonably influenced or affected the insurer as a prudent insurer, in deciding whether to accept the risk, and if so, on what terms, even if a prudent insurer would have made the same decision had it known the fact (WA Insurance Co v Dayton).
 - *A fact can be material even if it would not have had a notionally decisive effect on the mind of a prudent insurer (Pan Atlantic Insurance v Pinetop).
 - *Barclay Holdings v British National Insurance: held that a fact is material if its effect on a prudent insurer's mind is something more than the effect produced by the info which the insurer would have been generally interested to have. If, though interested to have it, such info

would not, in the end, have determined for reasonably prudent insurer the acceptance or rejection of insurance, the setting of the premium or attachment of conditions,, there is not such effect on the mind as requires disclosure by the insured.

- *The info, although of interest is not material. As such, it is not info which the insured must disclose.
- *Sola Optical Australia: HCA held that a fact is material to the P's case if it is both relevant to the issue to be provided in the P is successful in obtaining an award of damages, and is of sufficient importance to be likely to have a bearing on the case.
- If Sola Optical (non-insurance case) can be applied to pre-contractual disclosure in the insurance context, a fact will be material if it is:
 - (a) relevant to a prudent insurer's decision whether to accept a risk and if so on what terms; and
 - (b) of sufficient importance to be likely to have a bearing on prudent insurer's decision.
- *A prudent insurer is a hypothetical insurer that knows its business and carries it on carefully, without exceptional timidity or boldness (Pan Pacific).
- *(2) The court must decide whether the non-disclosed or misrepresented fact was material to the actual insurer. This is tested by asking whether the fact induced the actual insurer to accept the risk on the terms it did (Pan Pacific Insurance v Pinetop).
 - Just because a fact influenced an insurer to accept a risk on the terms it did, does not give rise to a presumption that the insurer was actually induced by the non-disclosed or misrepresented fact to accept the risk on the terms it did (Assicurazioni Generali v Arab Insurance).
 - For inducement the fact must be effective, but not necessarily the only cause of the insurer accepting the risk on the terms it did (Assicurazioni Generali v Arab Insurance).
- Making a finding about actual inducement involves the court speculating on what an insurer would have done if it has known the non-disclosed or misrepresented fact before it accepted the risk. That may involve the court considering an insurer's practices and procedures and the decisions the particular underwriter who accepted the risk has made in the past in similar circumstances (Alkedian Co v Royal Insurance).

Proving a fact was material:

- For the purpose of proving a fact was material, the actual insurer would adduce:
 - (a) expert evidence from an independent reputable underwriter or insurance broker as to how a prudent underwriter would have responded to the non-disclosed or misrepresented fact;
 - (b) evidence in relation to whether it was induced by the non-disclosed or misrepresented fact to write the risk on the terms it did:
 - its underwriting manuals and similar documents for the purpose of showing how it expected its underwriters to approach the risk and the

- processes in place which allocated responsibility within the company for underwriting that list;
 - evidence showing how it dealt with similar risks at about the same period
 - evidence of the decisions the particular underwriter who accepted the risk has made in the past in similar circumstances;
 - evidence from the particular underwriter that accepted the risk of their state of mind in relation to accepting the risk and decisions they made in the past in similar circumstances;
 - if appropriate, evidence from the person the underwriter that accepted the risk reported to.
- A fact is material if a prudent insurer would have delayed making a decision about offering cover if the intending insured had complied with the duty of disclosure, and an investigation by the insurer would have uncovered a fact which would have led to it declining to enter into the insurance contract on the same terms (*Davis v Westpac Life Insurance*).
- *The duty of disclosure requires an intending insured to inform an insurer about facts known to it:
 - That are relevant to the risk of an insured event fortuitously occurring during the insurance period as a result of the intrinsic nature of the subject matter of the insurance.
 - Property insurance: known as **physical hazard** and refers to direct operation of the events specified in the insurance contract on the subject matter of the insurance (it has nothing to do with the history or personal characteristics of the intending insured; generally it can be observed and scientifically measured).
 - That are relevant to moral hazard – refers to a person’s probity, integrity, honesty and morality and the probability that upon obtaining insurance, they will deliberately cause, invent or exaggerate a loss (*Insurance Corporation of Channel Islands*).
 - (other than those relevant to physical or moral hazard) that would influence a prudent insurer in deciding whether to accept the risk and if so, on what terms.
- Although info about an intending insured’s prior criminal activity might be material to the risk transferred, legislation through Australia allows an intending insured to decline to provide info about a spent conviction (*Criminal Records Act 1991 (NSW), s12*); and presents disclosure of info about criminal proceedings involving a child.
- Intending insured must disclose a well-founded rumour (*Strive Shipping Corp*); and an allegation of fraud or serious misconduct even if there is exculpatory evidence (*Khoury v Government Insurance Office; North Star Shipping Ltd*).
- Onus of proof: *insurer seeking to rely on an innocent or negligent non-disclosure or misrepresentation bears the onus of providing every element of it (*Drak Insurance v Provident Insurance*). It must prove:
 - For non-disclosure: that the intending insured did not disclose a fact known to them;

- For misrepresentation: the intending insured made an incorrect representation of fact;
- The fact was material
- It not knowing the fact induced it to enter into the contract on the terms it did.
- To prove disclosure, the innocent party must prove the non-disclosing party knew the material fact (Zurich General Accident and Liability Insurance v Leven).
- Fraudulent: non-disclosure of material fact is fraudulent if an intending insured knew the fact and deliberately concealed it because they believed the insurer might decline the risk, or only accept it on specific terms if they disclosed the fact (Dalgety & Co v Australia Mutual Provident Society)
 - Misrepresentation of a material fact is fraudulent if an intending insured made it (a) without actually and honestly believing it was true, or recklessly indifferent to whether it was true or not (NRG Victory Australia v Hudson); and (b) with the intention of it being acted on (Dr Gregory Moore v The National Mutual Life).

Remedies:

- *For an insurance contract, an innocent party is:
 - entitled to avoid an insurance contract from the beginning for an innocent, negligent or fraudulent breach of the pre-contractual duty of utmost good faith (non-disclosure or misrepresentation of a material fact). Avoidance is available even if the contract has been partly performed;
 - non entitled to damages for innocent, negligent or fraudulent pre-contractual non-disclosure (HIH Casualty v Chase Manhattan Bank). That is because the CL imposes the duty of disclosure as an incident to the relationship between the parties to insurance contract, it is not an implied term of the contract (Khoury v Government Insurance Office).
 - Not entitled to damages for innocent pre-contractual misrepresentation, although the court might order some sort of indemnity;
 - Entitled to damages for negligent pre-contractual misrepresentation
 - Entitled to damages for fraudulent pre-contractual misrepresentation (tort of deceit), including situations where fraudulent non-disclosure amounts to fraudulent misrepresentation. The insurer is entitled to keep the premium already paid.
 - ***Avoidance is usually an adequate and sufficient remedy for an insurer.**
- Availability of the remedy of avoidance for pre-contractual non-disclosure or misrepresentation (a) by an insured has the unfortunate side effect of encouraging insurers to delay spending time and money properly considering or investigating the adequacy of pre-contractual disclosure until after a claim is made on the policy; (b) by an insurer is not likely to be a practical remedy for an insured because avoidance deprives the insured of the only benefit to it of the contract, namely, having claims paid.

- Avoidance is brought about by act of the innocent party operating independently of the court. It is effective immediately upon the innocent party communicating to the other party its decision to avoid the contract (*Brotherton v Aseguradora*).
- If the insurer elects to avoid the contract, it must repay the premium unless the non-disclosure or misrepresentation was fraudulent, and can recover money already paid under the contract.