ASPECTS OF INSURANCE LAW

REPORT OF THE CONTRACTS & COMMERCIAL LAW REFORM COMMITTEE

REPORT OF THE CONTRACTS & COMMERCIAL LAW REFORM COMMITTEE ON ASPECTS OF INSURANCE LAW

To: The Minister of Justice

Introductory

1. The Committee has been called upon to consider and report upon the large topic of the law governing contracts of insurance. The present report is confined to five specific problems in respect of which there is in our view a strong case for early corrective legislation. We have not overlooked our obligation to consider insurance law in a more general way, and we intend to issue further reports. But it seemed to us that action in respect of the particular matters to which we refer should not be held up by the need for a wider study.

2. A draft of this report was issued as a working paper with a view to stimulating comment and criticism, and was circulated to all parties thought to have an interest in the proposals. In response to our request for comment and criticism, submissions were received from the various parties whose names appear in the appendix. The Committee desires to record that the submissions of all parties displayed a most constructive and helpful approach with the result that the Committee has been considerably assisted.

3. It is the view of the Committee that in respect of each of the five matters covered in this report, insurers (and this term is intended to include underwriters who are not incorporated) commonly draw insurance contracts in a manner that is so potentially unfair to the insured that legislative interference is necessary. It must be kept in mind that the detailed terms contained in an insurance policy (which is of course the contract

document) are not negotiated; nor indeed are they necessarily known to the insured until he receives his policy document, which may not be until some time after the contract has come into existence. Where, for example, the policy is held by a mortgagee it may never come into the hands of an insured at all; and if it does come into his hands he is unlikely to appreciate all its nuances of meaning.

4. It is sometimes contended by insurers in opposing reforms of the type which we recommend that insurers rely on the strict wording of their policies only when it is morally defensible for them so to do, and that in ordinary cases they do not rely on technicalities. Whether or not this claim is factually correct, such a situation is plainly unsatisfactory since it permits the insurer to be judge in his own cause. As the English Law Reform Committee once observed "the ease with which a technical defence may be found means that in many cases an insurer is in a position to substitute his own judgment of the claimant's bona fides for that of a court" (Fifth Report (1957) Cmnd 62 para. 11). In such circumstances the legal advisors of an insurer are obliged to point out that a technical defence is available and it may then be difficult for the officers of the insurer to disregard such advice. We are also conscious that, in contradistinction to the many reputable insurers carrying on business in New Zealand whose fairness and integrity in dealing with their policyholders are not in doubt, there are some insurers who are not reluctant to adopt a harsh or unconscionable attitude. We consider it imperative for legislation to be introduced to cover their activities. Reputable insurers will, needless to say, have nothing to fear from such legislation.

Immaterial Mis-statements

5. The common law, as an exception to the general rule that permits one party negotiating a contract to remain silent on matters that would adversely influence the other party (caveat emptor is an application of this general rule), requires a person negotiating a contract of insurance to act with the utmost good faith uberrimae fidei and to disclose all material facts. This rule affords insurers some protection, but it is of course confined to matters of which the insured had knowledge. To enlarge their protection insurers usually pose a number of specific questions in a proposal form and require the insured to warrant that his answers are true and that they form the basis of the contract of insurance. The effect of this is that a wrong answer however innocently given, and however immaterial to the assessment of the risk it may be, entitles the insurer to avoid the contract. (The law is well established. See E.R.H. Ivamy General Principles of Insurance Law (2nd ed. 1970) 132, R.A. Hasson The "Basis of the Contract Clause" in Insurance Law (1971) 34 M.L.R. 29, and K.C.T. Sutton The Contract of Insurance (1972) 5 N.Z.U.L.R. 123).

6. The injustice of this is obvious. It has perhaps never been more clearly expressed than in the following famous passage from the judgment of Fletcher Moulton L.J. in Joel v. Law Union and Crown Insurance Company (1908) 2 K.B. 863, 885:

> "Insurers are thus in the highly favourable position that they are entitled not only to bona fides, but also to full disclosure of all knowledge possessed by the applicant that is material to the risk. And in my opinion they would have been wise if they had contented themselves with this. Unfortunately the desire to make themselves doubly secure has made them depart widely from this position by requiring the assured to agree that the accuracy and not only the bona fides of his answers to various questions put to him by them or on their behalf shall be a condition

> of the validity of the policy. This might be reasonable in some matters, such as the age and parentage of the applicant, or information as to matters connected with his family history, which he must know as facts. Or it might be justifiable that these conditions should obtain for a reasonable time - say during two years - during which the company might verify the accuracy of statements which by hypothesis have been made bona fide by the applicant. But insurance companies have pushed the practice far beyond these limits, and have made the correctness of statements of matters wholly beyond his knowledge and which can at best be only statements of opinion or belief, conditions of the validity of the policy. For instance, one of the commonest of such questions is, "Have you any disease?" Not even the most skilled doctor, after the most prolonged scientific examination, could answer such a question with certainty, and a layman can only give his honest opinion on it. But the policies issued by many companies are wholly invalid unless this and many other like questions are correctly - not merely truthfully - answered, though the insurers are well aware that it is impossible for anyone to arrive at anything more certain than an opinion about them. I wish I could adequately warn the public against such practices on the part of insurance offices. I am satisfied that few of those who insure have any idea how completely they leave themselves in the hands of the insurers, should the latter wish to dispute the policy when it falls in. In the case of the question to which I have referred, if it can be shewn - even by the contemporaneous examination of the medical referee of the office itself - that the insured had at the time some disease, the policy is void. The disease may have been unknown, and even undiscoverable; it may have been transient, and have had no effect on his future life, or on the cause of his death. These things are immaterial. If the company choose to dispute the policy and establish a single inaccuracy in these statements, which are thus made conditions, the policy is void, and usually all that has been paid thereon is forfeit".

We add one more quotation from a judgment. It is from the decision of Swift J. in Mackay v. London General Insurance Company Limited (1935) 51 Ll.L.R. 201

at P. 202 -

> "I am extremely sorry for the plaintiff in this case. I think he has been very badly treated - shockingly badly treated. They have taken his premium. They have not been in the least bit misled by the answers which he has made. They would never have refused to give him his policy if they had known everything which they know now. But they have seized upon this opportunity in order to turn him down and leave him without any indemnity for the liability which he incurred.
>
> But I cannot help the position. Sorry as I am for him there is nothing that I can do to help him. The law is quite plain".

In our view the law should be changed.

7. Several comments received from the insurance industry made reference to the fact that the cases cited above came before the courts many years ago. It was also said that the strictures of the judges in those cases had no relevance to the general conduct of the insurance industry in New Zealand today. We think it relevant in the light of such comments to refer to a recent decision where a judge of the New Zealand Court of Appeal was constrained to say in a case involving a most reputable insurer:

> "At the outset it is right to emphasise that in this case there is not the slightest suggestion of any lurking suspicion of the sort that sometimes might seem to be required to justify a resort to the fine print of an insurance contract. As the Judge found and the insurer freely concedes (the insured) is a thoroughly honest, hard-working woman who has had the misfortune to be hit in her small business by a sudden and unexpected calamity. Thus there is no unspoken argument here for the strained and technical defences which have been put up against her claim. They depend entirely upon the apparent commercial advantages which seem to arise from the insurance company's construction of its legal rights under the policy. It is an attitude unlikely to command much sympathy".
> (See (1972) N.Z.L.R. 504 at 505)

8. No alteration has been made in the United Kingdom to the law on this subject, although in 1957 the Law Reform Committee recommended that "notwithstanding anything contained or incorporated in a contract of insurance, no defence to a claim thereunder should be maintainable by reason of any mis-statement of fact by the insured, where the insured can prove that the statement was true to the best of his knowledge and belief" (1957 Cmnd 62 para. 14(2)). In Victoria in 1936 legislation was enacted in relation to contracts of insurance (Instruments (Insurance Contract) Act 1936 S.2) which in the case of life insurance has been replaced by s.84 of the Life Insurance Act 1945-65 (Commonwealth) and in the case of other contracts of insurance by the Instruments Act 1958 (Victoria) s.25. The Commonwealth provision is as follows:

> "A policy shall not be avoided by reason only of any incorrect statement (other than a statement as to the age of the life insured) made in any proposal or other document on the faith of which the policy was issued or reinstated by the company unless the statement -
>
> (a) was fraudulently untrue; or
>
> (b) being a statement material in relation to the risk of the company under the policy was made within the period of three years immediately preceding the date on which the policy is sought to be avoided or the date of death of the life insured, whichever was the earlier".

The current Victorian statute provides as follows:

> "No contract of insurance (other than a contract of life insurance) shall be avoided by reason only of an incorrect statement made by the proponent in any proposal or other document on the faith of which such contract was entered into revived or renewed by the insurer unless the statement so made was fraudulently untrue or material in relation to the risk of the insurer under the contract".

These are the only relevant Australian statutes, though it is to be noted that a New South Wales judge has recently urged the adoption in his state of the Victorian provision (Kazacos v. Fire & All Risks Insurance Company

(1970) 92 W.N. (N.S.W.) 397 at p. 404 per Taylor J.).

9. It will be seen that under the Australian statutes and under the terms of the English committee's recommendation a mis-statement may avoid if it is either fraudulent or material. Our working paper expressed the view that there was no reason why a mis-statement however fraudulent should avoid a policy if it was in relation to a matter that was immaterial. Without exception insurers took the strongest objection to this proposal. At the time the working paper was prepared some members of the Committee also had serious misgivings but it was agreed that, since the Committee's proposals were being put forward simply as a working paper, we would await the receipt of comments before endeavouring to reach a final conclusion. The Committee now finds that it is evenly divided. We have therefore thought it desirable to record the arguments expressed on both sides.

10. Those in favour of the proposed reform point out that there is no logical reason why an immaterial mis-statement (whether fraudulent or not) should give the insurer the right to avoid a policy. If the mis-statement is immaterial then it cannot have been relevant to the insurer's judgment. The members of the Committee who favour this view point out that the definition of materiality contained in the draft bill annexed to this report gives insurers a large measure of protection.

11. The members of the Committee who do not favour the reform agree with the representations received from the insurance industry to the effect that it is of paramount importance to maintain the principle of uberrima fides in insurance contracts and that if an insurer can discharge the heavy onus of proving fraud in any respect, this should entitle the insurer to avoid the policy. In this regard the Life Offices' Association drew attention to the decision in Carter Bros. v. Renouf (1962) 111 C.L.R.

140 and commented that the facts of that case (which do not appear fully in the report) make it clear that while a fraudulent statement may not be material either at the time or at all, it may lull the insurer into a state of mind where he does not pursue enquiries into matters which may turn out to be very material.

12. Members of the Committee are unanimous in commenting that in part the difficulty stems from the unsatisfactory questions which are asked in some insurance proposals. The Committee is also unanimously of the view that it is reasonable (subject to our recommendations in the case of policies of life insurance) for insurers to protect themselves against mis-statements that are material, however innocent they may be. This seems to be the approach of various North American provisions. The Ontario statute for example (Insurance Act R.S. Ont. 1970 c. 224 s.98) a forerunner of which was considered by the Privy Council in Mutual Life Insurance Company of New York v. Ontario Metal Products Co. (1925) A.C. 344 at p.350) provides that except in relation to certain classes of insurance a mis-statement may avoid a policy only if it is material.

13. In the circumstances we have left unchanged the provision in the draft bill that a policy should be avoided by reason of a mis-statement only if it is material. In the case of life policies, the draft bill provides that a material mis-statement does not avoid a policy unless made fraudulently or within a period of three years prior to death or avoidance. The time limit in the case of life policies follows the scheme of the Commonwealth statute quoted above and of sections 157, 158 and 159 of the Ontario statute where, however, the period is two years and not three. (See clauses 4, 5 and 6)

14. Several of the submissions received by the Committee contained valuable suggestions concerning possible amendments to clauses 4, 5 and 6 of the draft

bill. The Insurance Council suggested that it was necessary for it to be made clear that contracts of personal accident and sickness fall within clause 5 of the draft bill and not clause 4. It was also pointed out that the phrase "contingencies of human life", although used in the Life Insurance Act 1908, is not a sufficiently precise description in relation to modern policies. The Committee agrees with this submission and after further research is of the opinion that the Commonwealth Life Insurance Act 1945-74 contains a much more satisfactory definition of a life policy. This definition has accordingly been adopted in clause 2.

15. The Life Offices' Association pointed out that clause 4 as originally drafted was too restrictive of the insured's rights in that it related only to a statement made by a proponent. The Life Offices' Association also drew our attention to the provisions of section 83 of the Commonwealth Act which appears to contain a workable and sensible proposal concerning rights of adjustment after discovery of a mis-statement as to the age of a proponent. We are grateful for these suggestions. They have been adopted in the annexed draft.

16. The Insurance Council also commented upon the definition of materiality (See clause 6(2)). In the working paper we referred to the need for an objective test and adopted the provisions concerning substantiality and materiality contained in the Marine Insurance Act 1908. The Insurance Council, whilst accepting the desirability of an objective test, pointed out that there are many factors, such as the age of the driver of a motor car, which an insurer will regard as not sufficiently serious to warrant increasing the risk, but which are nevertheless relevant to the terms upon which the insurance will be granted. The Insurance Council therefore suggested that a statement should be material if it would influence the judgment of a prudent insurer in fixing the premium or determining whether he will accept the risk or determining the precise terms upon which he will agree to accept it.

There may well be no real distinction in this context between the risk and the precise terms of the risk. We do not think insurers would wish to have the right to avoid if knowledge of the truth would have resulted in an insubstantial variation of the terms. We have amended the draft bill accordingly.

17. Finally, in relation to materiality, we mention that State Insurance Office expressed the opinion that the burden of proof of lack of materiality should be upon the insured. On the other hand Mr. Harley, who made helpful submissions as a private individual, suggested that the test of materiality should relate to what a reasonable proponent would regard as material. Mr. Harley's proposals, however, appear to us to have greater relevance to non-disclosure than to mis-statement and we hope to consider problems of non-disclosure in a later report. In relation to mis-statement we consider that the normal rule should apply, i.e. the burden of proof should be on the party seeking to set the policy aside, and that materiality should be defined in relation to what a reasonable insurer would regard as material.

Compulsory Arbitration

18. It is common for insurance policies to provide that any disputes between the insurer and the insured must be arbitrated. Arbitration as a means of determining disputes can undoubtedly have its merits. Matters in issue can be resolved relatively informally and where issues are technical there are advantages in selecting an arbitrator with experience in the relevant field. But motives for insisting on arbitration can be less worthy. An insurer by insisting on arbitration can defeat claims because it is more expensive to pay an arbitrator (or two arbitrators and an umpire) than to employ the services of judges or magistrates who are of course paid by the State; because the processes of appointing

arbitrators and settling references can lead to delay; and because legal aid is not available for arbitrations. Perhaps the main attraction of arbitration for insurers is its relative secrecy, the fact that arbitrations are disposed of in private and not in open Court. In the view of the Committee if insurers wish to contest claims they must be prepared to do so in public and not behind the closed doors of an arbitration. The customers and prospective customers of an insurer are entitled to know how that insurer behaves towards those claiming under its policies, and in particular whether that insurer is in the habit of invoking technicalities to defeat meritorious claims.

19. The Instruments Act 1958 s.28(2) of Victoria and the Insurance Amendment Act, 1968 s.7 of Queensland are examples of legislation giving insured persons relief against compulsory arbitration provisions. Clause 8 of our draft is based on the Queensland enactment. Several of the parties who made comments concerning this clause pointed out that it was now the policy of many New Zealand insurers either not to enforce arbitration clauses or to include such clauses only in relation to the quantum of the indemnity. Indeed certain insurers have for a considerable time been party to an informal agreement with the New Zealand Law Society under which the insurers undertook not to insist upon arbitration other than in relation to quantum. The Committee was aware of these facts, but was also aware that other insurers require all disputes to be dealt with by way of arbitration. We also consider that separating issues of quantum and liability can be inconvenient and expensive.

20. The Committee remains of the view that it is desirable for there to be a degree of uniformity concerning arbitration clauses, but recognises that many insurers believe disputes between an insurer and an insured will not fairly be resolved if determined by a

jury. Although some members do not fully endorse this view, we consider that it would be reasonable for the provision in the draft bill that arbitration clauses shall not bind the insured to be amended to provide that resultant claims between the insured and the insurer are to be heard before a magistrate or, if in the Supreme Court, before a judge alone. This suggestion was made by the Non-Tariff Insurance Association and requires an inferential amendment to the Judicature Act 1908.

Time Limits for Claims

21. In the case of insurance other than life insurance it is reasonable for insurers to impose time limits both for lodging claims and for commencing litigation or arbitration where claims are rejected. Obviously the insurers have to make their own enquiries and to set in train any proceedings to which their rights of subrogation may entitle them. Where time limits for prosecuting claims are imposed by statute, it is usual to permit the Courts to extend the time in cases where the delay is the result of mistake or other reasonable cause and the proposed defendant is not prejudiced by the delay. In our view a similar provision should apply to the time limits imposed by policies of insurance other than life policies. The Instruments Act 1958, s.27 of Victoria supplies a precedent, and in this regard we record that in the draft bill annexed to the working paper a line was inadvertently omitted. This has been corrected in the draft annexed to this report. In the case of life policies we see no justification for permitting any time limit shorter than the period provided by the Limitation Act 1950.

Agency of salesmen and others

22. It is common for the actual filling in of a proposal form to be done not by the proponent but by a representative of the insurer, perhaps a commission agent or a clerk behind the counter of the company's office.

Often such a person does not record the customer's exact words but paraphrases them perhaps to fit the exigencies of space in a printed form or in an effort to shorten what seems a garbled explanation. In this process mistakes can creep in. Insurers understandably prefer to rely on the document and to avoid being drawn into questions as to whether what was written correctly records what was orally stated by the proponent. It is therefore a common term of contracts of insurance that whoever fills in the writing on the proposal form is to be deemed the agent not of the insurer but of the insured. (See the discussion in Ivamy General Principles of Insurance Law cited above, p.494). In the words of one Australian commentator, "It is not easy to reconcile the law in this respect with broad notions of justice and fair play. The insurer is enabled to take advantage of the wrongful act of its employee because pro hac vice he becomes the agent of the proponent" (P.A. Jacobs Insurance Law Reform (1932) 5 A.L.J. 330, 333).

23. Understandable though it may be for insurers to desire that a person who completes a proposal is the agent of the insured, in our view the Courts should be free to endeavour to get at the truth of such matters when they arise. Indeed in some recent cases the Courts appear to have reached this position. See e.g. Stone v. Reliance Mutual Insurance Society Limited (1972) 1 Lloyds Reports 469. The law, however, is obscure and the cases conflicting. We therefore consider that persons employed or retained by the insurers should when completing proposal forms and like documents and generally in relation to the negotiation of a contract of insurance always be regarded as agents of the insurer not the insured. The English Law Reform Committee came to a similar conclusion. Its recommendation was that "any person who solicits or negotiates a contract of insurance shall be deemed for the purposes of the formation of the contract, to be the agent of the insurers, and that the knowledge of such

person shall be deemed to be the knowledge of the insurers". (1957 Cmnd 62 para. 14).

24. Particularly in the light of submissions made to us we acknowledge, however, that it is difficult to draft a satisfactory provision for a bill and this may have been one of the factors which influenced the Scottish Law Reform Commission of 1957 to recommend against any legislation.

25. In the outcome we have drafted clause 10 of the annexed bill to make it clear that the term "representative of the insurer" does not include employees or agents of the insurer who have had nothing to do with the negotiation of the policy in question, i.e. it would be quite unfair for an insurer to be put at risk if one of its employees, perhaps in another part of the country, has some relevant knowledge but is unaware of the negotiation of the policy.

26. A number of parties who forwarded submissions took exception to the inclusion of brokers, house agents, accountants, car dealers, solicitors and such like who commonly assist with the completion of proposals. On balance, however, the Committee considers it preferable for such persons (if they are paid commission) to be treated as the agents of insurers, with it being the insurers' responsibility to ensure that commissions are only paid to representatives whom they are prepared to trust. For the same reason the Committee considers a provision similar to Section 126 of the Commonwealth Life Insurance Act 1945/74 to be too limited in scope.

27. We recognise that there are special considerations relating to professional insurance brokers who are instructed by the insured. Insurers, too, rely on their skill. The question is, who as between insured and insurer should take the risk of default or lack of skill

on the part of the broker. There are arguments each way. In the end we have been deterred from excluding brokers for the definition of "representative of the insurer" by the difficulty of arriving at a definition of a broker that does not leave such a large loophole in the proposed reform.

Non-causative exemptions

28. It is common for insurance policies in defining the circumstances in which the right to indemnity arises to provide (often but not always in an exception clause) certain circumstances which make the cover inapplicable and to define such circumstances in terms that are other than causative. Such phrases as "Whilst the driver is intoxicated", "Whilst the vehicle is being driven in an unsafe condition", "Whilst the insured is engaged in the sports of mountaineering, skiing, gliding or flying a single-engined aeroplane", are examples of the sorts of provision we have in mind. A somewhat uncommon provision of this class was the one referred to in Richards v. Port of Manchester Insurance Co. Ltd. and Brain (1934) 50 Ll. L.R. 88, 132 which excluded from the protection of a policy drivers of a hire car who were "Jews, Air Force officers, actors, actresses, commission agents, undergraduates or foreigners".

29. It is quite clear from the cases (two recent New Zealand examples are Parsons v. Farmers Mutual Insurance Association (1972) N.Z.L.R. 966 and State Insurance v. Harray (1973) 1 N.Z.L.R. 276) that the word "whilst" used in such a context has a temporal and not a causative meaning. The effect of such provisions is that if, for example, a vehicle the driver of which is intoxicated or which is (perhaps unbeknown to the driver) in an unsafe condition, is struck from behind while waiting at traffic lights the insurer who has insured that vehicle may escape liability even though the intoxication or the unsafe condition did not contribute to the loss in any

way. This seems to us wrong. Insurers are of course entitled to define the risks in respect of which they will indemnify by excluding circumstances that increase the risk. It is understandable that they should seek to define exclusions in temporal rather than causative terms for it is easier to prove (for example) that a vehicle was in an unsafe condition at the relevant time than that the unsafe condition caused the accident. But it is unreasonable for insurers to avoid liability on the grounds that the risk is increased where the loss results from some cause other than the circumstances relied on as increasing the risk. The Committee notes that the proposals for reform in this connection were accepted by some insurers who made submissions but rejected by others.

30. It may be that in the long term the only answer to this problem is either for the Courts to be given a general power to strike out provisions in a contract of insurance that are unjust or inequitable, or alternatively the provision by law of standard forms of contract to cover the more common classes of insurance coupled with a prohibition of provisions less favourable to the insured. To say more at this stage would be to anticipate the conclusions of our future report or reports on the question of insurance law. In the meantime the draft bill contains a provision (clause 11) designed to tackle the problem of non-causative exemptions. In considering the provisions of the draft it is important to note that the onus is cast on the insured to establish the absence of causation.

Application of the Act

31. The draft bill provides that the Act should apply only to new contracts of insurance or existing contracts as and when they are renewed. An exception is, however, made in the case of life policies, since otherwise the Act would not for many years come fully into force in relation to these policies.

32. Recommendation:

For the foregoing reasons we respectfully recommend the enactment of legislation in terms of the draft Bill annexed hereto.

For the Committee

Chairman

MEMBERS

Mr. C.I. Patterson (Chairman)

Mr. B.J. Cameron
Professor B. Coote
Mr. D.F. Dugdale
Professor E.P. Ellinger
Mr. J.R. Fox
Mr. J.S. Henry
Mr. W. Iles
Mr. J.H. Wallace

Mr. A.E. Wright (Secretary)

DRAFT BILL REFERRED TO

IN THE REPORT

A bill to effect certain reforms in the law governing contracts of insurance

1. Short Title - This Act may be cited as the Insurance Law Reform Act 1975.

2. Interpretation - In this Act, unless the context otherwise requires, -

"Company" has the meaning ascribed to that term by section 41 of the Life Insurance Act 1908:

"Continuous disability insurance contract" means a contract of insurance (which is by its terms to be of more than one year's duration and is incorporated in a policy) whereby any person is to be entitled to a benefit in the event of the occurrence, within the duration of the contract, of death by accident or by some other cause specified in the contract, or of injury or disability caused by accident or sickness:

"Life policy" means a policy insuring payment of money on death (not being death by accident or specified sickness only) or on the happening of any contingency dependent on the termination or continuance of human life (either with or without provision for a benefit under a continuous disability insurance contract); and includes an instrument evidencing a contract which is subject to the payment of premiums for a term dependent on the termination or continuance of human life and an instrument securing the grant of an annuity dependent upon human life.

3. Act to bind the Crown - This Act shall bind the Crown.

4. Mis-statements in contracts of life insurance - A life policy shall not be avoided by reason only of any statement (other than a statement as to the age of the life insured) made in any proposal or other document on the faith of which the policy was issued, reinstated, or renewed by the company unless the statement -

(a) Was substantially incorrect; and

(b) Was material; and

(c) Was made either -

(i) Fraudulently; or

(ii) Within the period of 3 years immediately preceding the date on which the policy is sought to be avoided or the date of the death of the life insured, whichever is the earlier.

(Cf. Life Insurance Act 1945-1965, ss. 4(1), 84 (Commonwealth of Australia))

5. Mis-statements in other contracts of insurance -

(1) No contract of insurance shall be avoided by reason only of any statement made in any proposal or other document on the faith of which such contract was entered into, reinstated, or renewed by the insurer unless such statement -

(a) Was substantially incorrect; and

(b) Was material.

(2) Nothing in this section shall -

(a) Apply in respect of any contract of insurance embodied in a life policy; or

(b) Limit the provisions of sections 4 and 7 of this Act.

6. Incorrectness and materiality defined -

(1) For the purposes of sections 4 and 5 of this Act, a statement is substantially incorrect only if the difference between what is stated and what is actually correct, would have been considered material by a prudent insurer.

(2) For the purposes of sections 4 and 5 of this Act, a statement is material only if that statement would have influenced the judgment of a prudent insurer in fixing the premium or in determining whether he would have taken the risk upon substantially the same terms.

(Cf. 1908, No. 112, s. 20(2), (4))

7. Mis-statement of age -

(1) A life policy is not avoided by reason only of a mis-statement of the age of the life insured.

(2) Where the true age as shown by the proofs is greater than that on which the policy was based, the company may vary the sum insured by, and the bonuses (if any) allotted to, the policy so that, as varied, they bear the same proportion to the sum insured by, and the bonuses (if any) allotted to, the policy before variation as the amount of the premiums that have become payable under the policy as issued bears to the amount of the premiums that would have become payable if the policy had been based on the true age.

(3) Where the true age as shown by the proofs is less than that on which the policy was based, the company shall either -

(a) Vary the sum insured by, and the bonuses (if any) allotted to, the policy so that, as varied, they bear the same proportion to the sum insured by, and the bonuses (if any) allotted to, the policy before variation as the amount of the premiums that have become payable under the policy as issued bears to the amount of the premiums that would have become payable if the policy had been based on the true age; or

(b) Reduce, as from the date of issue of the policy, the premium payable to the amount that would have been payable if the policy had been based on the true age and repay to the policy owner the amount of overpayments of premium less any amount that has been paid as the cash value of bonuses in excess of the cash value that would have been paid if the policy had been based on the true age.

(Cf. Life Insurance Act 1945-1965, s.83 (Commonwealth of Australia))

8. Arbitration clauses not binding -

(1) Subject to subsection (2) of this section, a provision of a contract of insurance -

(a) Requiring differences or disputes arising out of or in relation to the contract to be referred to arbitration; or

(b) Providing that no action or suit shall be maintainable upon the contract or against the insurer in respect of any claim under or difference or dispute arising out of or in relation to the contract unless the issue, claim, difference, or dispute has first been referred to arbitration or an award in arbitration proceedings has been first obtained; or

(c) Providing that arbitration or an award in arbitration proceedings is a condition precedent to any right of action or suit upon or in relation to the contract; or

(d) Imposing by reference to arbitration or to an award in arbitration proceedings any limitation on the right of any person to bring or maintain an action or suit upon or in relation to the contract, -

shall not bind the insured.

(2) An agreement made by the parties to a contract of insurance after a difference or dispute has arisen out of or in relation to the contract to submit the difference or dispute to arbitration shall have effect as if subsection (1) of this section had not been enacted.

9. Time limits on claims under contracts of insurance - A provision of a contract of insurance prescribing any manner in which or any limit of time within which notice of any claim by the insured under such contract must be given or prescribing any limit of time within which any suit or action by the insured must be brought shall -

(a) If that contract of insurance is embodied in a life policy, not bind the insured; and

(b) In any other case, bind the insured only if in the opinion of the arbitrator or Court determining the claim the insurer has in the particular circumstances been so prejudiced by the failure of the insured to comply with such provision that it would be inequitable if such provision were not to bind the insured.

10. Salesmen etc. to be agents of insurer -

(1) A representative of the insurer shall for all purposes during the negotiation of a contract of insurance until the proposal of the insured is accepted by the insurer be deemed, as between the insured and the insurer, to be the agent of the insurer.

(2) An insurer shall be deemed to have notice of all matters material to a contract of insurance known to a representative of the insurer concerned in the negotiation of the contract before the proposal of the insured is accepted by the insurer.

(3) In this section the term "representative of the insurer" includes any servant of the insurer and any person entitled to receive from the insurer commission or other valuable consideration in consideration for such person's arranging, negotiating, soliciting, or procuring the contract of insurance between a person other than himself and such insurer.

11. Certain exclusions forbidden - Where -

(a) By the provisions of a contract of insurance the circumstances in which the insurer is bound to indemnify the insured against loss are so defined as to exclude or limit the liability of the insurer to indemnify the insured on the happening of certain events or on the existence of certain circumstances; and

(b) In the view of the Court or arbitrator determining the claim of the insured the liability of the insurer has been so defined because the happening of such events or the existence of such circumstances was in the view of the insurer likely to increase the risk of such loss occurring,

the insured shall not be disentitled to be indemnified by the insurer by reason only of such provisions of the contract of insurance if the insured proves on the balance of probability that the loss in respect of which the insured seeks to be indemnified was not caused or contributed to by the happening of such events or the existence of such circumstances.

12. Actions on or in relation to contracts of insurance to be tried before a Judge alone -

(1) Notwithstanding anything in section 2 or section 3 of the Judicature Amendment Act (No. 2) 1955, but subject to subsection (2) of this section, every action maintained upon any contract of insurance or against any insurer in respect of any claim under or difference or dispute arising out of or in relation to any contract of insurance shall, if tried in the Supreme

Court, be tried before a Judge without a jury.

(2) The service of a third-party notice making an insurer a party to an action shall not affect the manner in which the issues between the plaintiff and the defendant are to be tried but any insurer who is so made a party to an action may, if he agrees to be bound by the issues arising between the plaintiff and the defendant, require the issues arising between the insurer and the party who served the third-party notice to be determined by a Judge without a jury if the insurer, within the time limited for filing his statement of defence, files a notice to that effect in the Court and serves copies of it on the other parties to the action.

13. Application of Act -

(1) This Act shall apply in relation to life policies whether issued, reinstated, or renewed before or after the commencement of this Act:

Provided that nothing in this subsection shall affect -

(a) The rights of any claimant under a life policy if the event giving rise to the claim occurred before the commencement of this Act; or

(b) The rights of the parties under any judgment given in any Court before the commencement of this Act, or under any judgment given on any appeal from any such judgment, whether the appeal is commenced before or after the commencement of this Act; or

(c) The rights of the parties to any award made -

(i) Before the commencement of this Act following the reference of any matter to arbitration; or

(ii) After the commencement of this Act following the setting aside of an award made before the commencement of this Act; or

(d) In the case of an award to which paragraph (e) of this proviso applies, the rights of the parties to any proceedings by way of appeal against the making of any such award or for the setting aside of any such award.

(2) This Act shall apply in relation to contracts of insurance (other than life policies) entered into, reinstated or renewed on or after the commencement of this Act.

14. No contracting out - The provisions of this Act shall have effect notwithstanding any provision to the contrary in any agreement or in any contract of insurance (whether embodied in a policy or not).

15. Repeal - Section 23 of the Mutual Insurance Act 1955 is hereby amended by repealing subsection (3).

APPENDIX

List of those who made submissions upon the Committee's working paper.

Burnard, Bull & Co., Gisborne

Canterbury District Law Society

Consumers' Institute

Government Life Insurance Office

Hamilton District Law Society

Harley, Geoffrey J., Wellington

Insurance Council of New Zealand

Life Offices' Association of New Zealand

New Zealand Automobile Association Inc.

Non-Tariff Insurance Association of New Zealand

Otago District Law Society

State Insurance Office

Taranaki District Law Society

Wellington District Law Society

ASPECTS OF INSURANCE LAW (2)

A Report by the Contracts and Commercial Law Reform Committee

Presented to The Hon. The Minister of Justice on 19 May, 1983

ASPECTS OF INSURANCE LAW (2)

Contents

19 May, 1983

SECOND REPORT OF THE CONTRACTS AND COMMERCIAL LAW REFORM COMMITTEE ON ASPECTS OF INSURANCE LAW

To the Honourable the Minister of Justice.

1. Introduction

1.1 In the report of this Committee entitled Aspects of Insurance Law (the recommendations wherein were enacted as the Insurance Law Reform Act 1977) we referred to our intention to submit from time to time further reports on the topic of insurance law. This is the first of such further reports.

1.2 It was our view that before reaching any concluded opinion on the various matters referred to in this report we should as a first step consult with representatives of insurers and their customers. To this end we issued in October 1979 a discussion paper in which we referred to ten subjects on which it seemed to us that reform of the law should be considered. One hundred copies of this paper were distributed. Nine written comments were received. These came from:-

The Insurance Council of New Zealand
The Life Offices Association
The State Insurance Office
The New Zealand Law Society
Guardian Royal Exchange Assurance
Yorkshire General Life Insurance Co. Ltd.

Mr. J.H. Marshall of Auckland, Barrister and Solicitor

Mr. B.J. Paterson of Hamilton, Barrister and Solicitor

The Property Law and Equity Reform Committee

The submissions were carefully reasoned and constructive, and we express our thanks to the authors for the assistance they gave us.

1.3 The subjects raised in our discussion paper were:-

(1) Protection of Life Policies from creditors - which is considered in section 2 of this report.

(2) The Inalienable Life Annuities Act 1910 - which is considered in section 3 of this report.

(3) Insurable Interests in Life Policies - which is considered in section 4 of this report.

(4) Insuring Children's Lives - which is considered in section 5 of this report.

(5) Friendly Societies - limitations on the amounts payable on the death of children - which is considered in section 6 of this report.

(6) Payment of Interest on Life Policy benefits - which is considered in section 7 of this report.

(7) Particular Average - which is considered in section 8 of this report.

(8) Excusing non-compliance and (9) The Duty of Disclosure - were the subject of such strongly divided views that we have reserved them for further consideration. We refer to them in section 10 of this report.

(10) Insurance of buildings when land is sold - which is considered in section 9 of this report.

1.4 The submissions referred to other matters that were suggested for consideration, and we refer to those in section 11 of this report.

1.5 We recommend the enactment of legislation on subjects 1 to 7 and 10 in accordance with the draft Bill annexed.

2. Protection of Life Policies from Creditors

2.1 Sections 65 and 66 of the Life Insurance Act 1908 provide that "all policies that are dependent on accident, sickness, death or other contingencies of life" (with the exception of life policies maturing within 7 years, and certain paid up policies and policies where the premiums are payable by unequal instalments or at longer intervals than one year) do not pass to the official assignee on bankruptcy, are protected against execution creditors, do not pass under a general assignment of the policyholder's property, and on death are not available to pay creditors of legatees unless the will of the policyholder otherwise provides. The protection is limited in amount to $4,000 plus bonuses, or in the case of annuities to $208 a year.

2.2 The first statutory provision protecting life policies against creditors seems to have been a United Kingdom statute, the Married Women's Property Act 1870 s.10, which was replaced by the Married Women's Property Act 1882 s.11. The general scheme of those provisions is that a policy effected by a man or woman on his or her own life expressed to be for the benefit of his or her spouse and/or children creates a trust in favour of the objects named. In New Zealand section 48 of the Life Assurance Companies Act 1873 was to similar effect. (The equivalent section is today the Life Insurance Act 1908 s.75A.) The Life Assurance Policies Act 1884 provided an additional protection in sections 33 and 34, which are broadly to the same effect as sections 65 and 66 of the Life Insurance Act 1908. In particular it should be noted that the $4,000 or $208 per annum limit was first fixed by this statute.

2.3 It is not proposed to trace the provisions corresponding to the New Zealand sections enacted by the various Australian States. The relevant provisions are now to be found in two Commonwealth Statutes, sections 92-94 of the Life Insurance Act 1954-1973 and section 116(2)(d) of the Bankruptcy Act 1924-1965. In neither of these provisions is there any limit on the amount of the protection, but the protection on bankruptcy applies only if the policy has been in existence for at least two years (or if a policy of pure endowment, 5 years) before the date of the bankruptcy.

2.4 The New Zealand provisions have been plagued by poor drafting. Section 65(1) refers to the bankruptcy etc. of

the "holder" of the policy. But if the policy is assigned by way of mortgage the holder is the assignee. The Life Insurance Amendment Act 1925 section 3 was enacted to remedy this position, but failed on a strict interpretation so to do, because while the amendment made it clear who was to be protected, the event giving rise to the protection (i.e. the bankruptcy etc. of the holder) remained unchanged. Finally, in the case of In re Ainge (deceased); Wheeler v. Bank of Australasia [1935] N.Z.L.R. 691, the Court of Appeal decided that it might properly strain the interpretation of the strict words of the statute to avoid rendering it inoperative and read the provision as if the reference were to the bankruptcy etc. not of the holder but of the life assured. (This history is narrated by Turner J. in Bissett v. Australia and New Zealand Bank [1961] N.Z.L.R. 687, 688 ff.)

2.5 The questions which in our discussion paper were identified as requiring decision were these :

(a) Should the protection conferred by the Life Insurance Act 1908 ss.65 and 66 remain?

(b) If the protection is to remain, should the limit be varied?

(c) If the protection is to remain, should the drafting be tidied up?

2.6 The arguments in favour of abolishing the protection seem to be these :

(a) The philosophy of the provision, namely to regard provision for dependants as more important than the rights of creditors antedates the existence of the cushion of the welfare state. In today's New Zealand, widows and orphans will not in any event be left to languish in destitution and a statutory protection of life policies is not needed to help avert this.

(b) The very fact that there has been no demand to lift monetary limits of protection first established nearly a century ago suggests that the protection is of little practical value.

(c) The amount of the monetary limits of the protection is so trifling that it is not in practice invoked by life insurers as a selling point, so that the protection can be abolished without any real interference in current patterns of trade in the life insurance industry.

(d) There is no particular logic in protecting life insurance over other types of investment; moreover it is arguable that in inflationary times some forms of life insurance may be inappropriate as investment vehicles.

(e) Any theoretical advantage in preserving his policy for a bankrupt policyholder is likely to be lost if as a result of his insolvency he is unable to service the policy and so has either to surrender the policy or have it forfeited.

2.7 The Life Offices Association of New Zealand Inc. advanced arguments in favour of retaining the protection. They adverted to the longstanding existence of the protection, the uniqueness of life insurance with its co-operative risk sharing and the need despite the existence of the welfare state to encourage self help. They also pointed out that a surrender value may in practice yield a relatively trifling sum for creditors and that a bankrupt having regard to his then age and state of health may find it difficult or excessively expensive to obtain new cover. Both the Life Offices Association and the Law Society (though in the latter case without any reasons being advanced) favoured an increase in the protection limits. It is notable that two life insurers (Guardian Royal Exchange Assurance and Yorkshire General Life Insurance) preferred to see the protection abolished.

2.8 This is a committee of lawyers, and we readily acknowledge that the issue of whether or not to preserve the protection is one of policy which lawyers are in no better position to determine than anyone else. No doubt it would be possible to tinker with the limits of protection, but we have come to the clear view and recommend for the reasons set out in paragraph 2.6 that the protection be abolished and that sections 65 and 66 of the Life Insurance Act 1908 and section 3 of the Life Insurance Amendment Act 1925 be repealed. Clause 4 of the draft bill proposes this.

3. The Inalienable Life Annuities Act 1910

In our working paper we recommended (for much the same reasons) consideration of the protection provisions of the Inalienable Life Annuities Act 1910. The Life Offices' Association point out that at present there is no market for annuities in New Zealand because both the capital and the income content of instalments are taxed in the hands of recipients as income. The Association and the Guardian Royal Exchange and the Yorkshire General Life supported the repeal of the statute in toto and we so recommend. Clause 5 of the draft Bill provides for this.

4. Insurable Interests in Life Policies

4.1 It is well established that one has an insurable interest in one's own life or that of one's spouse. In other cases, if the contract of insurance is not to be unenforceable as a mere wager, the Life Assurance Act 1774 (U.K.) (in force in New Zealand) requires the proponent to have a pecuniary interest in the life assured. The pecuniary interest must be one reasonably capable of valuation in money. Moreover, the amount of cover must relate to the actual loss the death causes the proponent.

4.2 A majority of this committee recommends that the requirement for an insurable interest to support a life policy should be repealed. The minority considers that it should be retained.

4.3 The majority relies on the following arguments:-

4.3.1 The requirement is avoided by insuring one's own life and assigning the policy (McFarlane v. Royal London Friendly Society (1886) 2 T.L.R. 755), but in that case it was observed that, if the policy was ab initio really and substantially intended for the benefit of another person only, the Act would apply. The majority consider that a requirement so doubtful should not be preserved in the law.

4.3.2 The requirement of a pecuniary interest is uncertain. Such an interest has been held to exist as between partners, in respect of a creditor insuring the life of his debtor, in respect of a surety insuring the life of the debtor, and in respect of an employer insuring the life of his employee. But it is doubtful whether such an interest exists as between the members of an incorporated company, or as between man and woman living together but unmarried - cases that both assume some importance in modern society. On this ground also, the majority consider that the requirement is too uncertain to be supported.

4.3.3 The requirement need not be insisted upon by the insurer, and may possibly be waived (Hadden v. Bryden (1899) 1 F (Ct. of Sess.) 710). Where the underwriters have received the premium, the objection that there was no insurable interest is

often "as nearly as possible a technical objection, and one which has no real merit, certainly not as between the insured and insurer" per Brett M.R. in Stock v. Inglis (1884) 12 Q.B.D. 564.

4.3.4 It is well-established that the enactment of the statute of 1774 was provoked by the current mania for wagering. The preamble to the statute recites that "it hath been found by experience, that the making of insurances on lives, or other events, wherein the assured shall have no interest, hath introduced a mischievous kind of gaming". It seems to the majority of us that this reason for the existence of the requirement has for all practical purposes ceased to exist and that the act of 1774 can be repealed insofar as it applies in New Zealand.

4.4 A minority of this Committee takes a different view. The existence of some form of insurable interest is, under our present law, a universal requirement for all contracts of insurance. That is necessarily so in the case of indemnity insurance, but it has been made so in all other cases; by statute in England and in this country, and as a matter of "public policy" in the United States. The minority does not accept that the only justification for the interest requirement in the case of non-indemnity policies is the control of gambling and wagering. In England, wagering contracts as such were not made void until 1845. But in

the hundred years before that, an insurable interest requirement was introduced by statute, first in the case of policies on ships and their cargoes (though significantly, not in respect of goods on land), and then in the case of policies on human lives. Of the Marine Insurance Act 1745 Arnould on Marine Insurance (15th ed, 1961), p.6 says, in terms which have obviously been carried forward from much earlier editions, "... it is plainly opposed to the true interests of a mercantile state to enable those who have no real stake in the safety of a maritime adventure to give themselves (by means of such a contract) a great interest in its loss or destruction". Not the least of the concerns of an 18th century "mercantile state" in a "maritime adventure" would have been for the safety of passengers (if any) and crew, not to mention "cargoes" of slaves.

The minority believes that behind the Life Assurance Act 1774 lies, at least in part, a similar concern for the safety of human lives. They note that this is also the view taken by R. Merkin, "Gambling by Insurance - A Study of the Life Assurance Act 1774" (1980) 9 Anglo-American Law Review 331. The objection expressed in the preamble to the Act is not to gambling as such but to a "mischievous kind of gambling". At that time, of course, the word "mischievous" had connotations much more serious than those now attaching to it. In MacGillivray & Parkington on Insurance Law (6th ed, 1975) it is stated (p.21 fn. 72) that judges have justified the rules on interest in life policies by the need to prevent the temptation for

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beneficiaries to do away with the life assured. But the authors comment:- "This is unconvincing. The criminal law and the rule 'ex turpi causa' should constitute a sufficient deterrent to calculating evil-doers...".

Thus we reach the sharp point of division amongst the members of this Committee. The majority consider that the requirement of an insurable interest does not deter malefactors who, in any event, are precluded by other rules from recovering judgment against an insurer in respect of their wrongdoing. (In the estate of Crippen [1911] P.108, Beresford v. Royal Insurance Co. [1938] A.C. 586.) The majority do not see any palpable risk that villains will insure the lives of strangers and kill them for the insurance proceeds. The minority, however, adhere to their view that adequate grounds do not exist for re-introducing this particular form of temptation to crime.

4.5 The majority view was supported by the Life Offices Association, the Guardian Royal Exchange and the Yorkshire General Life, but they suggested that there should be a requirement for the consent of the life assured if the insurance is being proposed by someone else. A majority of this Committee regards that suggestion as unnecessary - in practice, insurers will require statements of medical history and possibly medical examinations from persons whose lives are to be insured and so that it is unlikely to be possible in practice to insure a person's life without his consent. The majority consider that, in the interests

of simplicity, a consent from the insured should not be a statutory requirement. The minority point out that in the United States life policies are regarded as being "particularly against public policy" where the insured has no knowledge of the application for and the issuance of the policy (Appleman, Insurance Law and Practice (1966) Vol. 2, p.106). The point is, of course, that, to the extent that a life insurance policy is not one of indemnity, the requirement of an insurable interest may diminish but cannot remove entirely the temptation to crime. Consequently, in their view, consent of the life assured should be required in all cases.

4.6 Accordingly, the recommendation by a majority is that the requirement for an insurable interest in relation to life policies should be repealed, and that there should be no statutory requirement for consent of the life assured. Clause 6 of the draft bill proposes accordingly, and clause 7 preserves the present law in relation to other insurances.

5. Insuring Children's Lives

5.1 There are in this context two separate policy considerations that need to be kept distinct.

(a) There is the belief that the amount a parent who insures his child's life should be entitled to recover should be limited in case an evil parent does not scruple to cause the death of a child for the sake of

an insurance payment. The Life Insurance Act 1908 s.67 as modified by the Life Insurance Amendment Act 1921-22 section 3(1) - (3) lays down rules limiting recovery (apart from return of premiums with interest up to a maximum of 5% per annum) on death of a child under 5 to $12 from all insurers and between 5-10 years of age to $20. Obviously these figures are hopelessly out of date.

(b) In relation to the effecting by minors of insurances on their own lives, there is the general concern to protect them from oppression that the law expresses in the case of all types of contract entered into by minors. At present it is not certain whether a minor under 16 years of age can validly insure his own life. It is obviously desirable that any uncertainties and ambiguities should be removed from this area. In the case of minors 16 years and over, s.75 of the Life Insurance Act 1908 (as substituted by s.17 of the Minors Contracts Act 1969) gives a minor wide powers to effect, surrender and deal with a policy over his own life.

5.2 Our recommendation is that it be enacted:

(a) That a minor under 10 years of age has no power to insure his life;

(b) That the class of persons who may insure the life of a minor under 16 years of age, or collect on a policy on the life of such a minor, be limited by law;

(c) That in the event of the death of a minor under 10 years of age the maximum recoverable by any proponent from all insurers be limited to a return of premiums, interest thereon at the maximum rate fixed from time to time under the Judicature Act 1908 s.87 compounding annually, and $1,000 (representing a rough approximation of the cost today of a funeral). The amount recoverable under the policy taking into account this limitation should be set out in the proposal form and separately signed by the proponent.

5.3 Clause 8 of the draft bill proposes accordingly.

6. Friendly Societies

6.1 The Friendly Societies and Credit Unions Act 1982 contains, in s.46, limitations on the amounts payable on the death of children which should be varied in line with the recommendations in section 5 of this report. Clause 9 of the draft bill proposes this.

7. Interest on Life Policy Benefits

7.1 There is usually a lapse of time between the death of a life assured and payment to the person entitled to the moneys due. This time lag is not usually attributable to the insurers, many of whom pride themselves on the expedition with which they deal with claims. But the circumstances of the death may lead to delay in the issue of a death certificate. There may be problems that hold up

the grant of administration. There may be delays in obtaining release of the probate or letters of administration from the revenue authorities. Over this period of delay, which can often be lengthy, the insurer has the use of the policy proceeds. Should the insurer be required to pay interest on such moneys in respect of the period between the date of death and actual payment?

7.2 The Life Offices Association, while conceding that some offices pay interest in such circumstances, regard the matter as one for actuarial judgment and inappropriate for legislative direction. They point to the difficulties in fixing an appropriate interest rate, and suggest that many of the delays are caused by solicitors acting in the administration of estates. The Yorkshire General Life and Guardian Royal Exchange both regarded the matter as one to be determined by market forces. The New Zealand Law Society favoured a requirement that interest be paid from 30 days after date of death at the "at call" deposit rate of interest ruling from time to time.

7.3 From the date of death the insurer has the use of the moneys. We have no doubt that in practice all Life Offices have sufficiently sophisticated systems of cash utilisation to turn such moneys so held by them to profit. In these circumstances the logic in favour of allowing the persons entitled to the policy proceeds interest on such proceeds seems inescapable. The matter is not one in our view where it is really likely that competitive market forces will

lead all insurers to do voluntarily what it is now proposed that they should be required to do by statute. We do not think that there is any real logic in the 30 day postponement period suggested by the Law Society. We acknowledge the difficulty referred to in some submissions in defining an appropriate interest rate by statute. We acknowledge that the interest rate must reflect the fact that the moneys in question are effectively at call. The maximum rate of interest fixed from time to time under the Judicature Act 1908 s.87 has the advantage of being invariably modest in amount and of being certain. We recommend that insurers be required by statute to pay interest on the proceeds of life policies which become payable on the death of the life assured, such interest to be calculated from the date of death at the "prescribed rate" as that term is defined in the Judicature Act 1980 s.87(3). Clause 3 of the draft Bill proposes this.

8. Particular Average

8.1 Where a policy contains a pro rata average condition its effect is that where the value of an insured item lost or damaged exceeds the amount of the cover, the loss is borne by the insured and insurer in the same proportion as the amount of cover bears to the value. So that if a policy is for $700 on an item worth $1,000 and the damage is $500, the amount to be found by the insurer is only seven-tenths of $500, i.e. $350. The full sum insured is paid only in the event of a total loss of the subject insured. This

compares with an ordinary policy (not subject to average) underwhich an insurer must pay the full amount of any loss, up to the insured value, whether the loss is total or only partial.

8.2 In practice in New Zealand an average clause is not usually inserted in domestic policies. But this has not always been so, and there is no legal reason why an insurer should not insert an average condition in a householder's policy. Indeed it seems that in other parts of the world insurers have taken to introducing an average condition into domestic insurance as a means of countering the effect of under-insurance resulting from inflation (see Insurance Council Bulletin Issue 157). The first matter to be considered therefore is whether the legislature should forbid the insertion of an average clause in certain classes of policy.

8.3 The Insurance Council of New Zealand Inc. agreed that a condition as to average is rare or non-existent in domestic policies in New Zealand, and that "almost the same could be said of all other classes of non-marine assurance". But the Council expressed the view that "under-insurance is becoming a major social problem" (which leads us to think that there is a possibility that a condition as to average may become more common), and for this reason the Council opposed any restriction on the use of average conditions. The State Insurance Office opposed a statutory prohibition of conditions as to average essentially because a condition

as to average could not in practice be introduced without the State Insurance Office doing likewise and "the State Insurance Office in performance of its role as a regulator of insurance practice would never be a party to such a proposal". Mr. J.H. Marshall, a leading Auckland conveyancer, expressed the view that to meet the reasonable expectations of the general public average conditions should be prohibited in domestic insurance policies and that "serious regard also be had to abolishing average clauses in all policies of insurance over buildings and other structures".

8.4 We consider that average conditions should be prohibited in policies affecting dwelling houses and contents. As no New Zealand insurer at present inserts average conditions in such policies no existing practice will be interfered with. We agree with those (including the State Insurance Office) who are of the view that the practice of inserting such conditions in such policies should never be permitted to re-emerge. A statutory prohibition will put the matter beyond doubt.

8.5 The second question that arises in the context of average is this. The purpose of pro-rata average conditions is to prevent an insured obtaining an undue benefit from under-insurance (though it can be argued that no such undue benefit is obtained where the premium is calculated as an amount per dollar of cover which does not vary with the total amount of cover). As a matter of principle, there

can be no quarrel with the notion that an insured may elect to bear part of the risk himself, and it can fairly be said that the rules as to particular average do no more than reflect the degree of sophistication that has been attained by the insurance law of England and the nations that have inherited that law. The problem is that in practice there is all too often no genuine election by the insured. The small businessman tends to arrange his insurances unassisted by adequate professional advice. He does not read his policy and if he does, is unlikely to appreciate the implications of an average condition. He is usually completely unaware that such a provision lurks in the small print of his contract until it is too late. Its discovery comes as a nasty shock to him. It may be added that under-insurance is particularly common in periods of inflation. Loss of profits insurance is an example of an area where frequently in practice an average condition comes as a completely unexpected blow to a businessman who has suffered a fire or like misfortune. Accordingly, we propose that the law should endeavour to make certain that in non-marine insurance an average condition (as a precedent to its enforceability) will be brought specifically to the attention of the insured at the time the contract of insurance is entered into.

8.6 The proposal set out in the previous sentence, which repeats an identical sentence in our discussion paper, was supported by both the Insurance Council and the State Insurance Office. In our view the only effective way of

bringing the condition to the attention of the insured is to require a conspicuous separately signed statement by the insured acknowledging that the cover is subject to average. While it may reasonably be anticipated that the expression "subject to average" will not by itself convey to the insured the precise subtleties of his contract, the requirement should be sufficient to put the insured on enquiry. The Insurance Council raised the questions of insurance arranged through a broker or other intermediary, and of insurance arranged informally without in the first instance the completion of a placing slip policy or covernote. It does not seem to us that these situations present any difficulty. The precise rule we propose is that an insurer shall not in relation to any insurance contract be entitled to enforce an average condition unless and until the insured has separately signed a conspicuous statement acknowledging that the cover is subject to average. It will be for the insurer to decide whether or not to enter into any particular insurance contract without obtaining such statement.

8.7 Clause 13 of the draft bill sets out the formal text we propose.

9. Insurance of buildings when land is sold

9.1 In our discussion paper we noted that this topic has been the subject of concern for a considerable time, and that there is general agreement the present legal rules are not

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satisfactory. The difficulties encountered are by no means confined to New Zealand, and ways of ameliorating the problems have been considered in several other common law jurisdictions.

9.2 The responses which we received to our discussion paper were in favour of reform, with one exception in the case of the Insurance Council of New Zealand Inc. Although conceding that the present legal rules are unsatisfactory, the Council suggested that the problems are virtually insoluble, and that any suggested alternative is equally likely to be the subject of dispute. While we acknowledge that there are difficulties, we do not consider that these are sufficient to cause the abandonment of reform in an area of the law which all concerned agree is open to serious criticism.

9.3 For convenience we again briefly summarise the existing rules, which were largely developed by the common law.

(a) In the absence of an express provision to the contrary, both equitable ownership and risk pass to the purchaser on the formation of a contract of sale, and the purchaser can thereafter be compelled to complete notwithstanding destruction of or damage to the buildings on the property prior to the date of settlement.

(b) From the time when the contract of sale is signed the vendor and purchaser both have an insurable interest.

(c) Unless the benefit under the vendor's insurance policy has been assigned to the purchaser with the consent of the insurer, the purchaser has no claim to the insurance moneys to which the vendor is entitled. The qualification concerning consent of the insurer is important. Although a vendor may covenant to hold an insurance policy on trust for the purchaser, if such agreement is made without the consent of the insurer then the vendor may find that, although he is obliged to hand the insurance money over to the purchaser, he will be liable when he later receives the full purchase price, on completion of the sale, to refund the amount of the insurance money to the insurer (see Williams on Vendor and Purchaser, paragraph 1157). Some of the cases in relation to the above rule are not entirely easy to reconcile, and it may be possible for the vendor to avoid the obligation to account to the insurer if the settlement is completed before a claim is made against the insurer or, alternatively, if the vendor covenants to confer the benefit of the policy. There is, however, some disagreement concerning these matters. Other problems may also arise when an insurer enforces its rights of subrogation: see Budhia v. Wellington City Corporation [1976] 1 N.Z.L.R. 766.

(d) A purchaser can require the vendor's insurer to lay out the policy moneys in rebuilding or reinstating the premises: section 83 of the Fires Prevention

(Metropolis) Act 1774 (U.K.). This Act applies in New Zealand, and it is probable that if a vendor is required, pursuant to his statutory obligation, to lay out the money in rebuilding, the vendor cannot then be called upon to refund the insurance money when he in due course receives the price of the property (see Williams at page 552).

9.4 The above rules frequently operate inequitably, as is shown by the relatively recent decisions in Budhia (ante) and Carly and Anor. v. Farrelly and Ors. [1975] 1 N.Z.L.R. 356. The difficulty, however, lies in devising a suitable alternative. This was attempted in the United Kingdom (and followed, for example, in Victoria) by section 47 of the Law of Property Act 1925 which provides:

> (1) Where after the date of any contract for sale or exchange of property money becomes payable under any policy of insurance maintained by the vendor in respect of any damage to or destruction of property included in the contract the money shall on completion of the contract be held or receivable by the vendor on behalf of the purchaser and be paid by the vendor to the purchaser on completion of the sale or exchange, or so soon thereafter as the same shall be received by the vendor.
>
> (2) This section has effect subject to:
>
> (a) any stipulation to the contrary contained in any contract;
>
> (b) any requisite consents of insurers;
>
> (c) the payment by the purchases of the proportionate part of the premium from the date of the contract.

We understand that, prior to the passing of the United Kingdom Act, it was usual to stipulate in contracts of sale

that, subject to the consent of the insurer, the purchaser would have the benefit of the vendor's insurance. While section 47 removes the need to make such a stipulation, it does not remove the need to obtain the insurer's consent: see Megarry and Wade, The Law of Real Property (4th Edition) page 577, where it is pointed out that, if the insurance is left in the vendor's name only, section 47 will not normally apply at all; for if the vendor can prove no personal loss, no insurance money will ever become payable under the policy.

A further problem in relation to the United Kingdom section 47 is that it does not adequately protect the purchaser. As is pointed out in Cheshire, Modern Law of Real Property (11th Edition) page 713, note 1:

> "If the house which is the subject of the sale is burnt down, the purchaser is nevertheless obliged to pay the purchase money, and if the insurance company refuses to give the requisite consent to the transfer of the insurance money, he will be unable to obtain payment of that money under this section. On the other hand, having regard to the nature of fire insurance it seems clear that a vendor is not entitled both to the insurance money and to the purchase money. A purchaser is well advised to insure the property himself immediately after the contract and not to rely on this section."

It seems therefore that the United Kingdom provision does not satisfactorily solve the difficulties.

9.5 In New Zealand there have been discussions between the New Zealand Law Society and certain insurers which have resulted in those insurers including special terms in their policies. An example is the following term which we

understand is included in policies issued by the State Insurance Office.

> "Notwithstanding the provisions of condition 4(d) of this policy, if at the time (during the Period of Insurance or during any further period in respect of which the General Manager shall have agreed to accept a premium) of destruction of or damage to the building or buildings hereby insured the Insured either as owner or mortgagee shall have contracted to sell his interest in such building or buildings or a part thereof and the purchase shall not have been but shall thereafter be completed within 3 calendar months of the making of such contract, the purchaser, on the completion of the purchase, shall be entitled to the benefit of this Policy so far as it relates to such destruction or damage (but excluding destruction of or damage to contents) but without prejudice to the rights and liabilities of the Insured either as owner or mortgagee or of the General Manager under this policy up to the Date of completion:
>
> Provided always that
>
> (a) the purchaser shall as though he were the Insured observe fulfil and be subject to the terms exclusions and conditions of the Policy;
>
> (b) if the purchaser is otherwise indemnified in respect of such destruction or damage then, notwithstanding the provisions of Condition 11 of this Policy, the benefit of this Policy shall not apply to the purchaser until the full amount of such other indemnity has been applied as far as it will go in satisfaction of such destruction or damage."

This and similar terms included in the policies of other insurers go a considerable distance towards ameliorating the difficulties inherent in the old rules, while also protecting the vendor and his mortgagees. As matters at present stand, however, there is no obligation upon insurers to continue including the term, and in any event the same or a similar term has not been adopted by all insurers. Moreover, the term is frequently only included

in policies relating to residential buildings, presumably on the ground that in farm sales the buildings usually form only a small part of the total price. In principle, however, we do not see any reason to distinguish between residential, commercial or farm buildings, and we note that this is the current policy of the State Insurance Office.

9.6 Many of the problems which arise when a building is wholly or partially destroyed between formation of the contract and settlement are evident from the foregoing discussion of the current rules. As is mentioned in the helpful article by Mr. Gordon Walker published in the Australian Business Law Review for June 1981, the problems can be eliminated if the parties plan the transaction properly: in particular by ensuring that the contract contains appropriate terms covering all the contingencies and by arranging adequate insurance cover. Although some of the forms of contract approved by District Law Societies endeavour to deal with the matter, adequate planning of the transaction by no means always takes place, with the result that a loss (or windfall) results to one of the parties in a capricious or unjust manner. It is also probable that difficulties arise more often in New Zealand than in some of the other common law jurisdictions, because in this country vendors and purchasers frequently sign a contract, binding upon them, without the benefit of prior legal advice. The opportunity to obtain proper advice concerning risk and insurance may therefore be delayed for some days, by which stage damage to or destruction of a building may have occurred. In any

event and for whatever reason, whether it be lack of competent advice or personal neglect, purchasers not infrequently fail to make proper arrangements.

9.7 Broadly speaking, there are two possible solutions. The first is to alter the common law rules concerning the passing of risk. The second is to give to a purchaser the benefit of any insurance cover taken out by a vendor. As we pointed out in our discussion paper, both solutions have their own problems.

9.8 In relation to the rules concerning the passing of risk, it is clear that any changes require relatively far-reaching amendment to the law. Moreover, the existing rules as to passing of risk are well known, and have been developed through a long history of case law. Nevetheless, it is possible to draft legislation which covers many of the contingencies, as has happened in the U.S.A. where a number of States have adopted the Uniform Vendor and Purchaser Risk Act. That Act, as adopted in New York, includes the following provisions:-

> "1. Any contract hereafter made for the purchase and sale or exchange of realty shall be interpreted, unless the contract expressly provides otherwise, as including an agreement that the parties shall have the following rights and duties:
>
> (a) When neither the legal title nor the possession of the subject matter of the contract has been transferred to the purchaser:
>
> (1) If all or a material part thereof is destroyed without fault of the purchaser or is taken by eminent domain, the vendor cannot enforce the contract, and the purchaser is entitled to recover any portion

of the price that he has paid, but nothing herein contained shall be deemed to deprive the vendor of any right to recover damages against the purchaser prior to the destruction or taking.

(2) If an immaterial part thereof is destroyed without fault of the purchaser or is taken by eminent domain, neither the vendor nor the purchaser is thereby deprived of the right to enforce the contract, but there shall be, to the extent of the destruction or taking, an abatement of the purchase price.

(b) When either the legal title or the possession of the subject of the contract has been transferred to the purchaser, if all or any part thereof is destroyed without fault of the vendor or is taken by eminent domain, the purchaser is not thereby relieved from a duty to pay the price, nor is he thereby entitled to recover any portion thereof that he has paid; but nothing herein contained shall be deemed to deprive the purchaser of any right to recover damages against the vendor for any breach of contract by the vendor prior to the destruction or taking."

9.9 We consider that the above provision, with suitable amendments where the terminology is inappropriate for New Zealand, could be used as a basis for reform in this country. It has the very real advantage of simplicity, and also ensures that risk passes when most vendors and purchasers would expect it to do so, i.e. either when possession or legal title is given. Further, it has the advantage of consistency with the situation which generally pertains on the sale of a chattel. An amendment along the New York lines would, however, constitute a radical change in relation to passing of risk on sale of land and buildings. It could also introduce an element of uncertainty, which might arise in at least two ways:

(a) with regard to the meaning of "material"; it may be difficult to determine when destruction of a building or one of several buildings is material, e.g. a cowshed on a farm property; although this may be overcome by giving a purchaser the right to a reduction in price or rescission whenever any part of a building is damaged or destroyed, this in turn may lead to another form of uncertainty, i.e.

(b) with regard to the completion of the contract and the effect upon subsequent contracts which are dependent upon finalisation of the contract the subject matter of which has been destroyed or damaged; it is possible to envisage considerable delays while disputes as to materiality or price reduction are settled by way of court hearing or arbitration.

Despite the fact that damage to or destruction of buildings between the date of contract and settlement occurs only in a limited number of cases, the above difficulties are sufficient to make us reluctant to recommend the more radical if conceptually neater New York solution, provided another practical solution can be found.

9.10 In relation to the other option, i.e. statutory extension of a vendor's insurance cover to a purchaser, we have already pointed out in our discussion paper that it too has its problems. Thus to some extent it places insurers at greater risk. For example, a vendor sometimes vacates a property a considerable time before possession or

settlement, which is generally thought to increase the risk. Similarly, if a purchaser is automatically given the benefit of the vendor's policy (even if only for a limited period), the purchaser becomes insured without the insurer having the opportunity to consider whether the purchaser is an acceptable risk. There is also the difficulty that a purchaser may be left unprotected if a vendor has done or omitted to do something which enables the insurer legitimately to decline to indemnify. Further, it has been suggested to us that the three months time limit (and the period is shorter in some policies) has proved inconvenient, especially in cases of long term sale and purchase agreements.

Problems of that nature were stressed by the Insurance Council in its response to our discussion paper. The Council contended that it is an example of faulty reasoning to suggest that there should be a statutory restriction on the underwriting discretion of insurers to choose and measure risk simply to protect purchasers or their professional advisers from the consequences of carelessness and incompetence. The Council further suggested that parties to a contract for sale and purchase should be left to make their own contractual arangements to suit the circumstances, and that the risks should lie where they fall in terms of the contract, with the parties being left to make their own insurance arrangements accordingly.

9.11 While we acknowledge that there is force in the arguments advanced by the Insurance Council, we do not think that the

Council's contention that the status quo should remain is acceptable. It is too productive of injustice. Although the New York solution meets some of the criticisms raised by the Council, we have concluded that in New Zealand conditions the most practical solution is to opt for an extension of the vendor's cover to a purchaser. This view is supported by comments on our discussion paper received from such insurers as the State Insurance Office, which advised that the term included in some policies by New Zealand insurers has not in practice created problems.

9.12 The Chief Justice's Law Reform Committee in Victoria, Australia, reached a similar conclusion in its report issued in November 1979. The Victorian Committee proposed a draft section as follows:-

(1) During the period between the making of a contract for the sale of land and the purchaser taking possession of the land pursuant to the terms of the contract, any policy of insurance maintained by the vendor in respect of any damage to or destruction of any part of the land or fixture therein agreed to be sold pursuant to the contract of sale shall in respect of the said land or fixtures, to the extent that the purchaser is not entitled to be indemnified under any other policy of insurance, inure for the benefit of the purchaser as well as for the vendor and the purchaser shall be entitled to be indemnified by the insurer under any such insurance policy in the same manner and to the same extent as the vendor would have been if the land had not been sold.

(2) It shall not be a defence or answer to any claim by the purchaser against the insurer made under subsection (1) hereof that the vendor otherwise would not be entitled to be indemnified by the insurer because the vendor has suffered no loss or has suffered diminished loss by reason of the fact that the vendor is or was entitled to be paid the purchase price or the balance thereof by the purchaser.

(3) A policy of insurance shall not inure for the benefit of a purchaser under subsection (1) hereof if the

insurer establishes that a prudent insurer would not have insured the purchaser against the risk covered by the policy.

(4) (a) At any time prior to the happening of the risk insured against an insurer made liable to a purchaser under subsection (1) may terminate that liability by giving not less than 3 days' notice of such termination to the purchaser.

(b) Such notice shall be in writing and shall be served upon the purchaser personally or in the case of a company by leaving it at the company's registered office.

(c) Such termination shall not have effect until the expiration of the period specified in the notice.

(5) The service of a notice referred to in subsection (4) hereof shall not affect the liability of the insurer to the vendor under the policy of insurance.

(6) This section -

(a) shall apply only to a contract for the sale of land made after the commencement of this section; and

(b) shall have effect notwithstanding any stipulation or term to the contrary contained in the contract of sale or any policy of insurance as referred to in subsection (1) hereof.

(7) This section shall apply mutatis mutandis to a sale or exchange by order of a Court.

The Victorian Committee recorded that much consideration had been given to an attempt to draft a section which would specify the manner in which the proceeds of any policy of insurance would be dealt with in the event of the insured property being destroyed before settlement (as distinct from the purchaser's taking possession). The conclusion reached was that the possibilities were so numerous and so varied that it was preferable to leave the otherwise existing law to operate.

The Victorian Committee further recommended that there should be a requirement for notice to be given to the purchaser of the need for him to arrange his own insurance, the principal reason for this being that the proposed draft section, like the term inserted in policies by some New Zealand insurers, does not protect the purchaser if the vendor's policy happens to be inadequate as to amount or voidable for non-disclosure, misrepresentation, or any other reason.

9.13 It is interesting to note the strong similarities of the approach recommended by the Victorian Committee and the term included in some New Zealand policies mentioned in para. 9.5 above.

9.14 The Australian Law Reform Commission has also recommended legislation in accordance with the approach suggested by the Victorian committee, but the draft bill proposed by the Australian Commission is less detailed than the Victorian proposal. ("Insurance Contracts", Report No. 20, Canberra 1982, paras. 130-132 and clause 50 draft bill.) For New Zealand, we think the more detailed approach is appropriate, but we suggest some variations of the Victorian proposal.

Subsection (1)

(a) We agree it is desirable for the extended cover to continue only until the date of possession or earlier settlement. This will not expose insurers to the risk

of insuring a property when it is in the hands of a purchaser who is unknown to the insurer.

(b) In our opinion the proviso that the purchaser is only entitled to be indemnified "in the same manner and to the same extent as the vendor" is essential. Otherwise insurers could have quite unforeseen liabilities placed upon them. The proviso also serves to protect the interests (if any) of the vendor's mortgagees or lessees.

Subsection (2)

In view of the common law rules to which we have earlier referred, we consider that this subsection is desirable, but it needs to be amplified.

Subsection (3)

We are concerned that this subsection introduces an unnecessary element of uncertainty. In our opinion the insurer is reasonably protected by the provision that the policy inures for the purchaser's benefit only until possession is given. We do not recommend the introduction of this subsection.

Subsections (4) and (5)

For the same reasons as apply to subsection (3) we do not consider that these subsections are necessary. We also think that subsection (4) would probably be of little practical use to an insurer who would not know of the

contract for sale unless there was a term in the policy requiring the insured to notify the insurer when a contract was made (which in itself we would consider undesirable since it could lead to the insurance cover being lost for failure to notify).

Subsections (6) and (7)
We agree that these subsections are appropriate.

9.15 An enactment to the foregoing effect (and a term in the contract of sale and purchase purporting to entitle the purchaser to the benefit of the vendor's policy) can create a problem of double insurance where the purchaser takes out his own insurance. The purchaser's policy may include a term avoiding the cover if the purchaser is otherwise entitled to indemnity. In such cases, the enactment of clause 11 or the term of the contract could have the paradoxical effect of vitiating the insurance specifically arranged by the purchaser. It is therefore necessary to include in the legislation a rule to settle that matter. Our recommendation is contained in clause 12 of the draft Bill. It is intended to secure that the purchaser will be covered by any policy arranged by him notwithstanding that the policy includes a term purporting to avoid it for other insurance.

It is desirable that we should mention that we think there are grounds for undertaking a reform of the law relating to other insurance, especially relating to the insured's

rights against the insurers respectively, order of indemnities, and indemnity and contribution amongst insurers. The subject is complex, and at this stage we propose legislation only to settle questions of other insurance that otherwise would arise out of clause 11 or the terms of the contract of sale.

9.16 We have considered whether the provisions of section 83 of the Fire Prevention (Metropolis) Act 1774 (U.K.) should be abolished. This section has, however, wider implications and for the time being we do not recommend any change in that regard.

9.17 Our proposals are set out in statutory form in clauses 11 and 12 of the draft bill annexed.

9.18 We cannot leave this difficult subject without a word of warning. Purchasers should arrange their own insurance. Standard form contracts of sale and purchase should include a warning to the purchaser that he should arrange appropriate insurance without delay. No statutory provision can solve all the problems. We have already mentioned some of the possibilities concerning the right of an insurer to avoid a policy. A policy may also be quite inadequate because of inflation and rising replacement costs. Again a policy may expire between the date of settlement and the date of possession or become void because, for example, the vendor vacated without giving the insurer notice of unoccupancy as required by the policy.

However, a provision along the lines which we suggest will serve to lessen the very real hardship which may result at the present time when a building is destroyed between the date of contract and the date of possession.

9.19 We are grateful to Miss Judith Potter and Mr. J.H. Marshall of Auckland, barristers and solicitors, for the information they supplied regarding the development of standard form contracts for the Law Societies.

10. Excusing Non-compliance, and the Duty of Disclosure

10.1 In our discussion paper we referred to section 18 of the Insurance Act 1902 (N.S.W.) (as amended by section 6 of the Commercial Transactions (Miscellaneous Provisions) Act 1974 (N.S.W.)) which provides as follows:

> "18.(1) In any proceedings taken in a court in respect of a difference or dispute arising out of a contract of insurance, if it appears to the court that a failure by the insured to observe or perform a term or condition of the contract of insurance may reasonably be excused on the ground that the insurer was not prejudiced by the failure, the court may order that the failure be excused.
>
> (2) Where an order of the nature referred to in subsection (1) has been made, the rights and liabilities of all persons in respect of the contract of insurance concerned shall be determined as if the failure the subject of the order had not occurred."

The New South Wales section has a wider field of operation than section 11 of the New Zealand Insurance Law Reform Act 1977 (which deals with non-causative exemptions or exclusions) because the New South Wales section gives the

court power to excuse the breach of any term of the contract of insurance on the ground that the insurer has not been prejudiced.

10.2 The responses of some insurers took exception to the introduction of a provision similar to the New South Wales section, but in our view none of the objections raised any matter of real substance. As we previously indicated, we consider that reputable insurers have nothing to fear from the introduction of a provision similar to the New South Wales section, and it was interesting to us to learn that the State Insurance Office had no objection to the proposal, it having already established a similar policy.

10.3 Having, however, given the matter further consideration, we have decided to defer this point, partly because there is little evidence that the wider powers given by the New South Wales section are required in New Zealand, and partly because the introduction of a similar provision would probably best be considered in relation to any changes concerning the duty of disclosure.

10.4 The comments made in our discussion paper concerning the duty of disclosure were limited to one aspect of the duty raised by the decision in Gulf Charters & Brokers Ltd. v. Guardian Royal Exchange Assurance of N.Z. Ltd. (Unreported High Court Auckland 7.2.79 Perry J.). The question which we raised for consideration was whether any modification of the duty to disclose material circumstances is required

where the proposal asks a series of specific questions and does not contain some warning statement or question drawing the general duty of disclosure clearly to the proponent's attention.

10.5 Even such a modest suggestion of amendment to the duty of disclosure produced conflicting responses from insurers. Although the suggestion was acceptable to some insurers, it was strongly opposed by others. This led us to consider some of the other aspects of disclosure in insurance contracts, a topic to which we had in any event intended to turn in due course. Our present view is that there are number of aspects of the existing rules concerning disclosure which require serious study and possible amendment. In other jurisdictions, suggestions have been made that the duty of disclosure requires very great modification (even an abandonment of the concept of utmost good faith), or that the proper test of disclosure should be materiality to a prudent insured (instead of prudent insurer), or that there should be some general power given to the courts to exercise a discretion where the existing rules result in injustice. These considerations have led us to the conclusion that it would not be wise to deal in isolation with only one aspect of the law concerning disclosure. We have therefore decided to defer making any recommendation on the one question raised in our discussion paper, but we propose to undertake a full consideration of the rules relating to disclosure, in respect of which we

will seek advice and comment from all interested parties in response to a discussion paper we have in preparation.

11. Other matters

11.1 It may be that in some future report on insurance law we will think it appropriate to recommend some provision regarding standard forms of insurance contract. If we were to do so, our approach would not be identical with that of s.57 of the Finance Act 1933 (No. 2), which provides that every policy of fire insurance of a class or classes defined by Order-in-Council "shall contain only such provisions as may be approved by the Governor-General in Council". So far as we are aware the section has never been used and we believe that it should be repealed. Clause 10 of the draft bill proposes accordingly.

11.2 The submissions received in response to our discussion paper raised a number of other suggestions for reform. In addition, the Australian Law Reform Commission has published a major report on proposals for the reform of insurance law in Australia. There is certainly enough to warrant a third round of consultations. Accordingly, we are preparing a third discussion paper which we will publish in due course.

12. Recommendation for Legislation

We recommend that legislation be enacted in accordance with the draft bill annexed. The recommendation is unanimous in respect of all provisions except clause 6, which is recommended by a majority.

For the Committee

C I Patterson

Chairman

Wellington

19 May, 1983

DRAFT INSURANCE LAW REFORM BILL

An Act to effect certain reforms in the law governing contracts of insurance

1. Short Title and commencement - (1) This Act may be cited as the Insurance Law Reform Act 1983.

(2) This Act shall come into force on the day of 1984.

2. Act to bind the Crown - This Act shall bind the Crown.

3. Interest payable from date of death - The Life Insurance Act 1908 is hereby amended by inserting, after section 41, the following section:

"41A.(1) Where any money becomes payable by a company under a policy as a result of the death of the person on whose life the policy was effected, the company shall, in addition to that money and at the same time as that money is paid, pay to the person entitled to the money interest thereon from the date of death to the date the money is paid to that person.

"(2) The interest payable pursuant to subsection (1) of this section shall be paid at the rate specified in the policy or at the rate for the time being prescribed for the purposes of section 87 of the Judicature Act 1908, whichever is the greater.

"(3) The provisions of this section shall have effect notwithstanding any provision to the contrary in any agreement or in any contract of insurance".

4. Abolition of protection of life policies from creditors - (1) The following enactments are hereby repealed:

(a) Sections 65 and 66 of the Life Insurance Act 1908:

(b) Sections 3 and 4 of the Life Insurance Amendment Act 1925.

(2) The enactments repealed by subsection (1) of this section shall continue to apply, as if they had not been repealed, in respect of policies held by a person who died or was adjudged bankrupt before the date of commencement of this section.

5. Repeal of Inalienable Life Annuities Act 1910 - The Inalienable Life Annuities Act 1910 is hereby repealed.

6. Need for insurable interest in life policy abolished - Notwithstanding any other enactment or rule of law, a person may enter into a contract of assurance on the life of another person, whether or not he has an interest in the life of that other person.

7. Insurable interest required for other contracts of insurance - (1) Subject to section 6 of this Act and notwithstanding anything in Part IX of the Gaming and Lotteries Act 1977, no insurance shall be made by any person -

(a) On any event whatsoever wherein the person for whose use or benefit or on whose account the policy is made has no interest; or

(b) By way of gaming or wagering.

(2) Every insurance made contrary to subsection (1) of this section shall be void.

(3) Nothing in this section applies to contracts of marine insurance within the meaning of section 3 of the Marine Insurance Act 1908.

(4) As from the commencement of this section, the Life Assurance Act 1774 (14 Geo.3, c.48) shall cease to have effect as part of the law of New Zealand.

8. Insurances on children's lives - (1) The Life Insurance Act 1908 is hereby amended by repealing section 67, and substituting the following section:

"67.(1) Except as provided in subsection (2) of this section, no person may effect a policy on the life of a minor who is under the age of 16 years.

"(2) Subject to subsections (3) to (5) of this section, any of the following persons may effect a policy on the life of a minor who is under the age of 16 years:

(a) The parents or guardians of the minor, or one of them:

(b) A parent or guardian of the minor and the spouse of that parent or guardian, jointly:

(c) The minor, if he has attained the age of 10 years:

(d) Any person who has obtained the consent of a District Court to do so.

"(3) No company shall pay any sum on the death of a minor under the age of 16 years, except to a person specified in subsection (2) of this section, or an executor or administrator of such a person, or any person to whom payment may be made under section 65(2) of the Administration Act 1969.

"(4) No company shall pay on the death of a minor under the age of 10 years any sum that is more than the total of the following amounts:

"(a) The total amount of premiums paid under the policy issued by the company on the life of the minor, together with interest thereon (compounded annually) at the rate for the time being prescribed for the purposes of section 87 of the Judicature Act 1908; and

"(b) The amount that, when added to any other sum payable by any other company pursuant to this paragraph (or by any friendly society pursuant to section 46 of the Friendly Societies and Credit Unions Act 1982), equals $1,000.

"(5) No company shall issue a policy on the life of a minor under the age of 16 years unless a statement explaining the effect of subsections (3) and (4) of this section is set out in the proposal for the

policy, and the person effecting the policy has signed a separate acknowledgment that he is aware of the limitations imposed by those subsections:

Provided that the issue of a policy in contravention of this subsection shall not make the policy illegal, unenforceable, or of no effect.

"(6) Any company that contravenes this section commits an offence and is liable on summary conviction to a fine not exceeding $1,000.

"(7) If any person claiming money on the death of a minor under the age of 16 years produces to the company from which the money is claimed a false certificate of death, or one fraudulently obtained, or in any way attempts to defeat the provisions of this Act with respect to payments upon the death of minors, the person so offending commits an offence and is liable on summary conviction to a fine not exceeding $1000."

9. Amendments and savings consequential upon section 8 - (1) The Friendly Societies and Credit Unions Act 1982 is hereby amended by repealing section 46, and substituting the following section:

"46. Subsections (3), (4), (6), and (7) of section 67 of the Life Insurance Act 1908 shall, with all necessary modifications, apply in respect of a registered society or branch as if -

"(a) Every reference therein (except subsection (4)(b)) to a company were a reference to a registered society or branch; and

"(b) The reference in subsection (4)(a) to premiums paid under the policy issued by the company on the life of the minor were a reference to any money paid to the registered society or branch in order to obtain the benefit payable on the death of the minor".

(2) Section 4 (5) of the Administration Amendment Act 1964 is hereby repealed.

10. Repeal of power to regulate provisions of fire insurance policies - Section 57 of the Finance Act 1933 (No. 2) is hereby repealed.

11. Purchaser of land entitled to benefits of insurance between dates of sale and possession - (1) During the period between -

(a) The making of a contract for the sale of land and all or any fixtures thereon; and

(b) The purchaser taking possession of the land and fixtures pursuant to the contract, or final settlement, whichever is the sooner -

any policy of insurance maintained by the vendor in respect of any damage to or destruction of any part of the land or fixtures shall, in respect of the land and fixtures agreed to be sold and to the extent that the purchaser is not entitled to be indemnified under any other policy of insurance, enure for the benefit of the purchaser as well as for the vendor, and the purchaser shall be entitled to be indemnified by the insurer under the policy in the same manner and to the same extent as the

vendor would have been if there had been no contract of sale:

Provided that nothing in this subsection shall oblige an insurer to pay more in total under a policy of insurance than it would have had to pay if there had been no contract of sale.

(2) It shall not be a defence or answer to -

(a) Any claim by a purchaser against an insurer under this section, that the vendor otherwise would not be entitled to be indemnified by the insurer because the vendor has suffered no loss or has suffered diminished loss by reason of the fact that the vendor is or was entitled to be paid the purchase price, or the balance thereof, by the purchaser; or

(b) Any claim under this section by a purchaser against the vendor's insurer in relation to the land or fixtures sold, that the purchaser's entitlement under the policy to which the claim relates is affected or defeated by the existence or terms of another policy; or

(c) Any claim by a purchaser against an insurer (other than the vendor's insurer) that the purchaser's entitlement under the policy to which the claim relates is affected or defeated by a claim under this section.

(3) In this section the word "vendor" includes a mortgagee of the vendor and any person claiming through the vendor.

(4) Where, in respect of a contract for the sale of land and all or any fixtures thereon, -

(a) There is damage to or destruction of any part of the land or fixtures during the period specified in subsection (1) of this section; and

(b) The whole or part of the amount payable in respect of the damage or destruction under the policy of insurance maintained by the vendor is payable to a mortgagee of, or any person claiming through, the vendor -

the purchase price payable under the contract of sale shall be reduced by the amount so payable to the mortgagee or person claiming through the vendor.

(5) This section shall not apply to the extent that the purchaser and vendor under a contract of sale expressly agree at any time.

(6) This section -

(a) Shall apply only in respect of contracts of sale made after the commencement of this Act; and

(b) Subject to subsection (5) of this section, shall have effect notwithstanding any provision to the contrary in any enactment, rule of law, policy of insurance, deed, or contract; and

(c) Shall apply, with all necessary modifications, in respect of a sale or exchange of land and

fixtures by order of a Court as if the order were a contract of sale.

12. Double insurance relating to contracts for sale of land -

Where there is a contract for the sale of land and all or any fixtures thereon, it shall not be a defence or answer to any claim by the purchaser against an insurer (other than the vendor's insurer) that the purchaser's entitlement under the policy to which the claim relates is affected or defeated by the existence or terms of any policy held by or on behalf of the vendor.

13. Conditions as to average -

(1) No contract of insurance relating to a dwellinghouse or any of the contents thereof, or both, shall contain a condition as to average; and any provision of a contract of insurance that contravenes this subsection shall be of no effect.

(2) Where a contact of insurance (not being a contract to which subsection (1) of this section applies or a contract of marine insurance within the meaning of section 3 of the Marine Insurance Act 1908) contains a condition as to average, the condition shall be of no effect unless a document relating to the contract contains -

(a) A conspicuous statement that the contract is subject to a condition as to average; and

(b) A conspicuous explanation of the condition in terms substantially the same as the following statement:

"The Meaning of Subject to Average

"(1) If your insurance policy is "subject to average" you will be entitled to recover the full amount of your loss only if your property is insured for its full value at the time of loss.

"(2) If your property is insured for less than its full value at the time of loss, the following rules apply:

"(a) If you suffer a total loss, you will recover the full amount for which your property is insured:

"(b) If you suffer a partial loss you will be entitled to recover only a proportion of your loss. What you recover will bear the same proportion to your actual loss as the amount for which your property is insured bears to the full value of your property:

"(c) Whatever your loss, in no case will you be entitled to recover more than the amount for which your property is insured.

"Example: Your property is worth $20,000. You insure it for $10,000. You suffer a loss of $5,000. If your policy is "subject to average" you will be entitled to recover only $2,500."

(c) An acknowledgement, separately signed by the person insured, that the contract is subject to a condition as to average.

(3) Subsection (2) of this section does not apply in respect of a contract of insurance entered into before the commencement of this section.

Appendix B

Members of the Contracts and Commercial Law Reform Committee as at the date of this Report

Mr C.I. Patterson (Chairman)

Professor J.F. Burrows

Mr B.J. Cameron

Mr R.S. Clarke

Professor B. Coote

Mr D.F. Dugdale

Mr J.R. Fox

Mr J.S. Henry, Q.C.

Hon Mr Justice Wallace

Mr P.J. Carroll (Secretary)

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