Complaints against insurers - do we need an Ombudsman?

Lunchtime address by Mr. Gordon Borrie
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1. I would like to begin by thanking you for asking me to speak at your meeting.

2. I have been asked to speak this afternoon on "Complaints against insurers do we need an ombudsman?" I should like to consider this question in two parts, first the complaints themselves, the main causes for complaints, and the statutory and voluntary measures which have been taken in recent years to improve the policyholder's position. I should then like to consider what remains to be done, and whether the creation of an ombudsman would be a useful and sensible solution to some or all of the remaining problems.

3. It is five years now since my predecessor, Sir John Methven, spoke at the opening lunch of your international colloquium in 1975 and mentioned a number of issues which seemed to him to require attention. It may be useful to remind you briefly of these issues because, although some progress has been made, the same issues are very much alive today.

4. The problems which Sir John identified were: the difficulties for consumers in understanding policy documents; lack of information about the surrender values of policies; doubts as to whether insurance brokers give independent advice; and consumers not knowing where to take their complaints.

5. But before I consider in detail the problems facing consumers, it might be helpful if I briefly describe the level and types of complaints that we receive.

6. My Office has, since its creation 6 years ago, collected statistics of consumer complaints about all kinds of goods and services that are made locally to consumer advisers. The number of complaints made to consumer advisers in local authorities and Citizens Advice Bureaux about insurance has been rising steadily over the past few years, and last year reached over 6,000. Complaints about insurance have also risen as a percentage of complaints about professional services, and they now account for slightly more than half the complaints about professional services.

7. A little while ago, we carried out a detailed study of 200 complaints about insurance (excluding life assurance) received by consumer advisers and this showed that the main complaints made by consumers were, in order of importance: claims being rejected, or disputed by the insurer; consumers being given wrong or misleading information; and delays in meeting claims or producing documents.

8. Some types of insurance give rise to a greater number of complaints than others; motor car insurance accounts for 50% of complaints, property and travel insurance 25% and 20% relate to life assurance. The job that my Office has of identifying and finding solutions to consumer problems is not, of course, simply one of counting consumer complaint figures. Indeed, it is very doubtful whether the complaints made to local Advice Centres, Trading Standards Offices and the insurance industry associations (together with those made to my Office direct) represent the whole story of the consumer's difficulties in the field of insurance. On the other hand, some complaints may not be justified or may arise because of factors outside the industry's control. Against the many millions of policies in existence, the level of complaints is small but for the individual concerned, the problem can, of course, be very serious indeed.

9. It is against that background that we have sought to take a closer look at the major underlying causes of these complaints, and we think there remain four problem areas.

10. The <u>first</u>, and in our opinion, the major cause of consumer problems remains the lack of adequate pre-purchase information. In our experience, consumers <u>assume</u> that they are fully covered; they remain unaware of how little they know about the cover of their policy until it is time to claim; and they then discover that the claim they wish to make may be ruled out because the cover is not as wide as they had thought. Consumers do not know the relevant questions to ask when taking out insurance and, in our view, they should be given much clearer guidance.

11. A good example of the way in which people so often misunderstand the position is shown by the use of standard terms such as "comprehensive". To the man in the street, this term probably means "all inclusive" and he will expect the "comprehensive" cover offered by different companies to be the same. He is therefore likely to choose the cheapest "comprehensive" policy he can find, and he will be unaware of the exclusions that may exist in such policies unless and until the time comes to make a claim. Let me state quite clearly that I am not trying to tell insurance companies what a particular policy should cover - that is a matter for them to determine - but I <u>am</u> saying that a potential insured should be told what he is buying, in particular any additions to or exclusions from the standard cover in the policies.

12. The low level of surrender values for life assurance policies in the early years is a further example where complaints arise because of inadequate pre-purchase information. While I of course accept that insurers must be free to determine surrender values according to sound underwriting practice, the potential insured should be made aware of his position when he takes out life assurance. It is not sufficient for him to be aware that there is no surrender value in the first year, and to know the final surrender value of the policy; he needs to be aware if he surrenders after, say, two years, that he may not be refunded the amount he has paid in. It would also be helpful if he could be advised about the amounts he can expect to receive if he surrenders his policy at any time in the middle years of the insured period. If consumers were provided with this kind of clear pre-purchase information, enabling them to make informed purchasing decisions, I think we might well see the level of complaints starting to fall. I certainly hope that insurers and brokers will regard the statutory "cooling-off" notice which was introduced in January of this year as the minimum requirement and that they will make an additional effort to explain orally as well as in writing to potential policyholders that life insurance really is a long term contract and must not be regarded as a device for making savings to be drawn on as the need arises.

13. Similarly, consumers have little idea about the need for disclosure both when initially taking out insurance and on each renewal. The majority of consumers have not heard of the doctrine of "utmost good faith". It seems quite clear to me that a consumer who wishes to take out fire insurance and has at some time in the past been jailed for theft may consider that it would be irrelevant to disclose this, not fully appreciating that on the prudent insurer test all prison sentences must be disclosed, and a claim may be rejected in the absence of such disclosure. The Statement of Insurance Practice of 1977 requires that a statement should be prominently displayed on the proposal form informing the proposer of the nature of his duty of disclosure and of the consequences of his failure to comply with it. Renewal notices are required to warn the insured that the duty of disclosure arises afresh each year. These are excellent precepts though they will not apply in a situation where there is no proposal form as in building society block insurances exemplified by the 1978 case of Woolcott v Sun Alliance. Especially while the law on disclosure remains as it is - and I will refer to the Law Commission proposals shortly - there is a clear need for the attention of the potential insured to be particularly drawn to the duty of disclosure in whatever ways are most effective.

14. While I am referring to pre-purchase information I might perhaps make the point that more should be done to ensure that consumers receive value for money. For example, industrial branch assurance is still sold to very many people who may not be aware that they are often paying a higher premium than would be necessary if they had an ordinary branch policy, and paid their premiums though the banking or giro system. The labour intensive method of collecting industrial premiums means that the management expenses associated with industrial life policies are inevitably high. I am not sure that enough is being done by the insurance industry generally to explain the range and advantages of the different kinds of policies that are available.

15. The second major cause of consumer complaints concerns the difficulty of comprehending the documents presented to the consumer, especially the policy document itself.

16. The majority of people find legal documents very difficult to understand, and if a document is worded in an obscure way, will tend not to read it. I am well aware of the difficulties of putting into simple terms the meaning and effect of legal language. There is always the risk that simplification will distort rather than clarify. My Office has had the task of preparing information for the layman on the Consumer Credit Act 1974 and now we have the Estate Agents Act 1979. But simplification of contractual documents (like statutes) can be achieved: indeed it has been achieved. One of the major companies, General Accident, has brought out motoring and, more recently, household policies which are written in language suitable for one of the "better quality tabloid" papers. The policy is presented in the form of a booklet and contains clear explanations of difficult points: these explanations do not form part of the legal documents, but they are likely to be of immense value to the policyholder in understanding the policy. I have been looking to the other major companies to follow suit, and am glad to hear that two companies are following this initiative; but until this type of policy becomes commonplace, I am afraid there will continue to be justifiable complaints about rejected claims which have arisen simply because the insured failed to understand the policy document.

17. A third cause for complaint concerns delays by insurance companies in paying out claims. It is necessary, of course, for insurers to investigate claims carefully before payment is made, and I am aware of the many problems that can be involved. But I am not convinced that all companies make payments as quickly as they should. Where this kind of delay cannot be avoided in the case of life assurance, it is inequitable in my view if the insurer does not pay the dependents of the insured interest accruing between the date of the insured's death and the date of the payment of claim.

18. It may seem strange to refer to lack of publicity about complaints procedures as the fourth cause of complaint against insurers but in my experience lack of knowledge about where to take your complaints about any consumer goods or services is always potentially frustrating and is more noticeably a problem now in insurance than in many other fields.

19. The major insurance associations and Lloyd's are, of course, prepared to consider complaints made to them about handling by insurers of particular complaints. I understand that the associations are prepared to ask companies to review these cases at a quite senior level. But I do not think this potentially valuable service is adequately publicised. My Office and the Department of Trade have jointly circulated a note to consumer advisers, informing them of the bodies to which insurance complaints may be referred, but I am sure there is room for the industry itself to do more in the way of publicity in this area. The Code of Practice for the Motor Industry, for example, provides that if a dispute cannot be resolved between a dealer and a consumer, the dealer himself must make it clear to the consumer that he has a right to refer the complaint to the relevant trade association. I should like to see that practice adopted in the insurance industry. Why does not the insurer, as a matter of routine, when sending claims documentation to the insured, enclose a note to the effect that, if he is dissatisfied, he may wish to ask the relevant insurance association to look into his case?

20. I have mentioned the major causes of complaint against insurers, and perhaps I might now strike a more positive note and examine what has been, is being and may perhaps in the future be done to improve the position of the insured.

21. At the present time, there is not only a growing corpus of legislation, we also have a measure of self-regulation through the Statements of Practice agreed by the various insurance industry associations and Lloyd's. It is important to consider these and the question of what is the right balance between law and self-regulation before trying to answer the question of whether we need an ombudsman for insurance matters.

LEGISLATION

22. On the matter of legislation, the Department of Trade has primary responsibility for monitoring and supervising the solvency of insurance companies and those responsibilities go back quite a long way. Prudential considerations are vital and the failure of an insurer can, of course, represent financial disaster to the insured so that the role of the Department, who are themselves advised by the Government Actuary, is fundamental in protecting the consumer.

23. More recent legislation has strengthened the insured's position still further. The Policyholders Protection Act 1975 ensures that if, despite Department's supervision, an insurance company fails,private policyholders are protected from serious loss. The Insurance Companies Act 1974 also contains important safeguards and reflects an increasing awareness that today the purchaser of insurance expects not only that his investment will be safeguarded but that there will be rules protecting him when he buys insurance to ensure that he is treated in a fair and reasonable manner.

24. Then there is the Insurance Brokers Registration Act 1977 and its attendant rules. When the Act is fully in force, the title of "insurance broker" will be restricted to those brokers or broking firms which are registered or enrolled with the Insurance Brokers Registration Council. The Council must be satisfied that the broker has adequate experience or experience plus the possession of an approved qualification for the practice of the profession, and is of suitable character. Registered insurance brokers and enrolled bodies corporate must also comply with the rules laid down by the Council which set out sound professional practice and help safeguard the interests of clients. Except for Lloyds broking business, insurance brokers are required by the Act to take out professional indemnity against losses arising from claims in respect of any civil liability incurred by them or their employees in the course of their business. With the same exception, registered brokers must meet the Council's requirement as to working capital, assets and independence (brokers must prevent their business from becoming unduly dependent on any particular insurance company). There are rules concerning accounts and accounting records, of which perhaps the most noteworthy is the requirement that brokers keep, in a bank account separate from their own, all monies relating to insurance transactions. The Act also establishes a Grants Scheme under which the Council can make payments to relieve or mitigate losses suffered by clients on account of negligence, fraud or other dishonesty of a registered broker and can fund this scheme by a levy on all registered brokers.

25. From the point of view of my Office,a most important feature of the legislation, since it bears directly on standards of trading practice, is the statutory Code of Conduct which sets down three fundamental principles governing the professional conduct of insurance brokers and gives 19 examples of their application. The examples cover matters such as advertising, information to be given to clients and objectivity.

26. The Act might be called an example of statutory self-regulation. The Insurance Brokers Registration Council, composed largely of representatives of registered brokers, polices the Act. It can investigate complaints against registered brokers made by members of the public and has the power to erase from the register an individual insurance broker or broking firm in cases of crime or unprofessional conduct. As far as I can judge, this Act is already having a positive and useful impact in improving trading standards.

It stemmed from a White Paper of January, 1977 on Insurance Intermediaries and proposals put forward by insurance broking interests. There are, of course, intermediaries other than brokers. Sole agents of insurance companies must now disclose their relationship with the company when arranging insurance. The previous Government's White Paper went on to suggest that the right way to improve the standards of insurance agents generally is to make the companies employing them fully responsible for the agent's conduct in carrying out the terms of his agency with the company. I readily acknowledge that because of the broad spectrum of interests involved in selling insurance and the complexity of the law governing agency, this is not an easy area to tackle. Nevertheless, a good deal of insurance is sold by intermediaries other than brokers and it is entirely reasonable for consumers to expect to receive advice from properly trained and responsible agents. I very much hope that the companies themselves will be ready to respond with ideas as to the best way to promote higher standards. I have never thought it satisfactory, in law or in common sense, that the company's agent may somehow be transmuted into an agent for the intending insured while the agent is helping to fill out a proposal form; and I think it is time that the proposals of the Law Reform Committee in 1957 to change this, are implemented.

27. I am reminded of the story of the young man who wanted to take out life assurance and was faced with the questions in the proposal form: Are your parents alive? and If not, how did they die? His difficulty was that 20 years ago his father had been hanged. The agent said: "There is no problem - just put: 'No. My mother died of pneumonia. My father was taking part in an official function when the platform gave way'".

28. While insurance is regulated by many detailed and specific laws, insurance companies have been successful in preserving the principle of the utmost good faith and most notably gained exemption from the Unfair Contract Terms Act 1977.

29. As you know, exemption from that Act was won on the understanding that the insurance industry would exercise greater self-regulation by means of the industry Statements of Practice. These Statements of Practice were agreed between the industry and the Department of Trade and announced in 1977. We, in the Office of Fair Trading, tend to regard them as being closely akin to the self-regulatory Codes of Practice which we have promoted, now covering about 18 sectors of consumer goods and services, including motor vehicles, travel, footwear and funerals.

30. I have a statutory duty under the Fair Trading Act 1973 to encourage trade associations to develop codes of practice and for many purposes they have advantages over legislation. Changing the law is slow, time-consuming and expensive. The Parliamentary time-table is crowded and the enforcement authorities have their work cut out to ensure that existing laws are kept. If a way can be found to achieve at least some of the objectives of consumer protection by means of self-regulation, the cost to society as a whole can be kept to a minimum.

31. Self-regulation has other advantages. Principles and practices agreed in this way are likely to be adhered to more enthusiastically than statutory controls. In particular, it is less likely that business will spend time, money and ingenuity in trying to get round the spirit or letter of an agreed code which business itself has helped to draw up. Another benefit is that it is possible to include in self-regulatory codes of practice, provisions which could not sensibly be included in legislation and to revise or expand them when necessary relatively quickly. Codes governing the conduct of particular industries contain provisions which are not appropriate to other industries and which could not be applied by law short of unduly elaborate and bureaucratic industry-by-industry regulation.

32. But although the provisions of codes of practice are tailored to the circumstances of individual trades, some provisions are common to all the codes we have endorsed. Such provisions include, for example, the supply of adequate pre-purchase information to the consumer. All codes provide for methods of conciliating in disputes which occur between a trader and his customer, and this usually takes the form of a four step procedure.

The consumer is encouraged to take his complaint in the first place to the supplier and, if he is not satisfied, he should seek the help of Consumer Advice Centres, Citizens' Advice Bureaux or local Trading Standards Officers. If this fails, the codes provide generally for the trade association promulgating the code to seek an agreed solution between the trader and the consumer. Experience shows that even quite complex disputes can be settled by conciliation operated by the trade association. If conciliation fails, most codes provide for a final stage of arbitration which is binding on both parties. The arrangements for the arbitration of disputes are explicitly without prejudice to the consumer's right to take a dispute to the Courts if he so prefers.

33. An essential strength of self-regulatory codes is that they are flexible and can be adapted to meet developing needs; in our experience it is essential to review the working of such codes as a specific exercise at intervals of, say, every 2 years. Such a review can determine whether the code's provisions are being complied with, whether the consumers are being adequately protected, and whether improvements are called for.

34. This may seem rather a long digression but I thought it important to explain that insurance is not excluded from the provisions of the Fair Trading Act and I can see no reason for the industry to seek to avoid the kind of trading standards that have been adopted, through the mechanism of codes of practice, by so many other sectors. Indeed, the industry's exemption from the Unfair Contract Terms Act suggests that a much more stringent regime, rather than a more relaxed regime, of self-regulation is required.

35. The Life and Non-Life Statements of Practice have been with us for well over 2 years, and I have been urging for some time now that they should be thoroughly reviewed. The review I want to see would have two aims. First, a check should be made to ensure that the existing statements are being complied with. It is vital to not only ensure that self-regulation is working but to show publicly that it is working. I know from a small survey conducted by the LOA in 1978 that a quarter of the offices replying to their questionnaire did not adhere to some of the provisions of the relevant statement. They did not, for example, insert a note in the proposal form or in a supporting document that a copy of the policy form or of the policy conditions were available on request. Second, the review should consider what improvements are required to make the statements effective in tackling the causes of consumer difficulties.

36. The kind of improvements that I have been suggesting are based on our experience with codes of practice now applicable in other industries. They include provisions in the Statements of Practice relating to the clarity of the information provided. There is need for a requirement that policies should include a clear and precise summary of the cover available and any exclusions which, because they are not common to all policies of the type concerned, may not be obvious to policyholders.

37. I think it is also desirable that the Statements of Practice require that where claims are accepted they will be paid promptly. Although the processing of some claims inevitably takes time, I think it is important that insurers should avoid unnecessary delays in their treatment of consumers once claims have been agreed. Our experience shows that where payments or transactions are unduly delayed, consumers tend to wait for very long periods indeed before going to the trouble of complaining to Government Departments or local advice centres. It may be that the complaint levels we receive in this respect may be only a limited indication of a much higher level of dissatisfaction.

38. Finally, I think the Statements of Practice should go some way toward the typical complaints procedure that we have in OFT-sponsored codes of practice by providing for conciliation by the industry associations. The insurance industry associations are relatively well equipped to undertake conciliation in difficult cases and I am hopeful that, if they accept this task and if the complaints and conciliation procedure is properly publicised, this will provide a useful service to consumers and assist in the speedy resolution of complaints.

39. Now where should the line be drawn between legal regulation and self-regulation? Have we at present achieved a successful balance between the two? These are questions that have to be asked in many fields other than insurance and I earlier mentioned a number of the advantages of self-regulation. Many of the present provisions of the insurance Statements of Practice are simply not suitable for legal regulation and certainly the additional ones I have for some time now been suggesting are in that category. You could hardly legislate for the use in policy documents of plain language or define with the precision appropriate for a statute what is meant by the prompt payment of claims. But the Law Commission, in its Working Paper on Insurance Law published a year ago, saidthere are clearly limits to the protection that can be offered by self-regulatory statements or codes of practice. They pointed out that an insured would have no legal remedy if an insurer failed to act in accordance with the provisions of the Statements and, indeed, a liquidator of an insurance company would be bound to disregard the Statements. The Law Commission referred to the provision in the Statements that an insurer may not act "unreasonably" in repudiating liability or rejecting a claim and said it was not satisfactory for the insurer to be left as sole judge in any particular case.

40. The Law Commission will be publishing their final Report later this year and you had the benefit of hearing their chairman at one of your meetings last November. I think their Working Paper makes a strong case for law reform and raises serious doubts about whether the provisions as to disclosure and materiality in the Statements of Practice are a satisfactory substitute for legislation. The balance between legal regulation and self-regulation does not seem right at present because the present basic law about disclosure and warranties is unsatisfactory and only legislation can alter that. Insurers must be safeguarded against fraudulent and irresponsible claims but existing law allows too much discretion so that even honest and reasonable claimants can be disadvantaged.

41. I have been asked "Do we need an ombudsman?", presumably an insurance ombudsman. Frankly, my views on this will be influenced to a large extent on whether the law on disclosure and warranties is developed broadly on the lines the Law Commission has provisionally put forward in their Working Paper and whether the industry associations and their members are willing to monitor, review and develop self-regulation through the Statements of Practice. Clearly the development of adequate and well known complaints procedures are most important.

42. There is, of course, a clear precedent in the UK for more intensive supervision and control. The Industrial Life Commissioner plays a very effective role in protecting and helping consumers and where complaints are of a serious nature,he conducts informal hearings.

43. Presumably the question raised in the title of my address today is whether all insurance activities should be overseen by some new public authority.

44. I read an interesting article published two months ago in The Policyholder. Mr. Arthur Robertson said insurers adopted a "somewhat pained attitude" to the question of complaints from policyholders. He thought this may be doing the insurance industry a disservice. "Insurers tend to avoid getting too involved with complaints' systems believing they are unnecessary. But in doing this they are in danger of giving the impression of not caring.... At present, although several industries have open complaints' systems or user bodies, insurers prefer to keep this to themselves." That is very much in line with my own thoughts. Mr. Robertson said insurers could learn something from the complaints institutes that exist on the Continent - institutes run jointly by insurers and consumer representatives. Files are made available to them and insurers usually comply with the institute's recommendations.

45. The ombudsman idea developed in Scandinavia and spread into Holland and Switzerland is another alternative. In Sweden, the Consumer Ombudsman may require certain information to be given such as in relation to the scope and content of policy conditions. He and the insurance industry jointly produce informative material which is distributed by the insurance companies, they have jointly established a consumer advisory service and they have agreed procedures for the handling of claims. A separate authority is charged with ensuring that conditions of insurance are reasonable. There is also an independent Public Complaints Board which covers the whole field of consumer complaints, insurance companies have agreed to tell claimants in writing of the role of this Board and the Board's recommendations are normally followed by the companies in individual cases.

46. Clearly the Swedes have established and indeed are continuing to develop, a fairly elaborate system of advice and help for people buying insurance and people making claims on insurance policies. It is a system based on partnership between the insurance industry and various public authorities.

47. I doubt if we need a public official as an insurance ombudsman in this country. I do not think it necessary or desirable for there to be greater administrative control over the industry than is represented by the supervision and monitoring of solvency. The kind of administrative intervention in the market place that takes place in Sweden, including as it does a measure of control over contractual terms, would be an undue constraint on flexible, dynamic and competitive marketing. I hope that the final Report of the Law Commission will pave the way for a fairer and more certain legal framework for the basic rights and obligations of the parties to the insurance contract. I would like to see that new basic legal framework complemented by the insurance associations developing self-regulation from the modest beginnings of the 1977 Statements of Practice and being given by their members a bigger and better publicised role in handling complaints. If we advance on these lines we will be recognising and coping with the problems as other countries have done but finding our own solutions.