The legal control of risk management in the field of insurance

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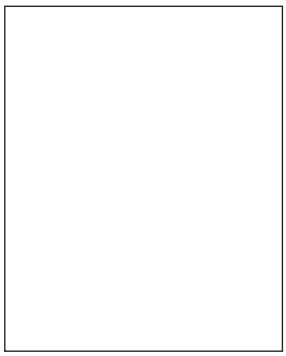

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A. Introduction

1. The main task of private insurance business is to manage risks. Rules applicable to this activity, insurance law, has the main function of controlling this management. They can be divided into three groups.

2. The first one consists of the supervisory law. This part of insurance law gives rules of the society´s control of insurance business. Many important and general principles of how insurance business must be driven can be derived from these rules. On the whole they give the frame of the room given the insurers in their activity.

3. The second group of insurance law is the *insurance contract law*. This part of the rules consists of those regulating the insurance contract, how it is concluded, which the obligations and rights of the parties and other circumstances are. Insurance contract law traditionally represents the heart of insurance law.

4. The third part of insurance law is composed of the rules concerning *intermediaries*. Here one finds rules about agents and brokers, concerning their liability and other legal issues.

5. From an international point of view it becomes evident, that the legal rules concerning risk management in insurance can be performed in many ways and that they may bring to the fore many problems for those managing risks. Some of the more fundamental problems will be discussed below.

B. Who controls the risk management?

6. The control of risk management in insurance business is outermost handled by the legislator. This means that the issue lies in the hand of the politicians. Courts complete the work of the legislator by giving answers where the legislator has been silent or where he has said something but in an unclear way. Also the legal literature has a role to play, since pronouncements of the doctrine might be guiding for the courts.

7. The intensity of the work by the legislator to a large extent depends on the field of insurance law (cf. 2-4 above) that is concerned. Nearly all countries have found that a rather detailed regulation is necessary as far as the supervisory insurance law is concerned. The interest of the legislator for insurance contract law, on the other hand, varies much between the countries. In England there is no general Act concerning this type of contract. Sweden represent the opposite model. A comparatively detailed regulation is given in the försäkringsavtalslag (Insurance Contract Act) from 1927 and in konsumentförsäkringslag (Consumer Insurance Act) from 1980. The international picture of the rules concerning intermediaries is also split between the countries. Many states, as for example Sweden, has a special legislation in this field but others, as Germany, might lack it completely. There seems to be no relationship between the legislators interest for insurance contract law and his interest for insurance intermediaries. A country which lacks an Act on insurance contract law might well have an Act on intermediaries. This is the case with England.

8. Sweden belongs to countries where the legislator in general has been very interested in matters of insurance. A problem is that all what is said by him is not said in the text of the Act itself. In stead it might be expressed in the *travaux préparatoires* of the Act. This creates great difficulties for the risk management, not at least with reference to foreign insurers who to be certain have to take part of the whole motives of the Act. And these are not insignificant. The printed motives of a proposed new Insurance Contract Act consists of more than thousands pages.

9. Insurance law issues only seldom go to court in Sweden. The explanation to this is not only the extensive and informing work of the legislator. It also depends on the existence of special boards, which are of great importance. These boards are voluntarily set up by the insurers. Most part of Swedish insurance law is developed by these boards. A problem is that different to what is the case with courts the principle of openess has no importance in the boards. Therefore the mass-media have no access to the activities of the boards. In a democracy this might be troublesome. For the risk manager considerable difficulties arise.

10. One thing is the basic and more long-term control of the acitivity of the insurance companies. Another is the immediate control. In most countries the legislator has created an order according to which the insurers are supervised by a special public authority.

In Sweden the authority given this task is called *Finansinspektionen* (the Finance Inspection Board). This public body does not only control insurance policies (to which belongs the size of the premium), but also the settlement of claims for damages. Where the insureds are consumers, there is a close collaboration between Finansinspektionen and the National Board for Consumer Policies.

The Finansinspektionen was founded on the 1st of July 1991 by a merger of two public authorities: Försäkringsinspektionen (the Insurance Inspection Board) and the Bankinspektionen (the Bank Inspection Board). The essential purpose of this fusion was was to be able to better control a market which was caracterized by a more and more close cooperation between insurers and banks. However, the appropriateness of the merger might be questioned. Without doubt there are risks that are unique for insurers respectively for banks. And from an organizational point of view a difference nevertheless has to be done between the two acitivies; at the Finansinspektionen the activity is clearly divided between a department for insurance, and two departments with reference to banks.

11. Some countries seem to have a rather easy system referring to the control of the insurers. Others, and to them Sweden belongs, works with a more complex system. This makes the work of risk management difficult. Simpleness is valuable.

C. The limits of freedom

12. Risk management certainly presupposes a certain freedom. Which legal freedom do the rules ought to give risk management in the insurance field? Which are the valutations behind the legal considerations here?

13. A must decisive position is taken by the supervisory insurance law (cf. 2 above). As far as rules once is given in this field by the legislator, there is not much room for liberty here. The rules are mandatory.

The same is, to a considerable extent the case with the law concerning the intermediaries (cf. 4 above).

The situation is quite another in the law of insurance contract (cf. 3 above). Here the rules given by the legislator may be only supplementary; in such a case, only if the insurer and the insurance taker have not decided what shall apply, the rules of the Act will apply. In the existing Swedish Act, Försäkringsavtalslagen (cf. 7 above), the rules only to a lesser extent are supplementary. Most rules are mandatory. In Konsumentförsäkringslag (cf. 7 above) all rules are. Also in the proposal for a new Insurance Contract Act (cf. 8 above) the rules in favour of consumers will be mandatory. Rules concerning insurance takers who are enterprises will however in general only be supplementary. In the references given for the legislation work it is said that this depends on a wish to ”deregulate”.

14. Deregulation is an international phenomenon. It is perhaps most apparent in the field of supervisory law. How can one explain its existence in this part of the law?

It is not excluded that deregulation has to do with the philosopy behind insuance law; the content of the rules depends on the values of the society. From an international point of view there seems to be two ways of looking upon insurance business. According to one of them insurance business is considered as a pure question of market economy; all is considered to be a question of money coming and going. The other way of looking on insurance matters is to treat the activity as a question of solidarity.

The former one (in the following called the market economical approach) seems to be the existing one in England and entails that insurance business has a tendency to meet with bank activity. The other one (in the following called the solidarity approach), existing in Germany and France, gives the insurance business a more special image; it does not lack moral undertones.

The approach chosen can influence the performance of the rules. In a world where the market economical approach dominates most possible freedom in insurance business seems to be an essential catchword. Certainly, the advocate of the solidarity approach cannot be said to be an opponent of freedom. But it cannot be denied that he strives more in favour of a strong intervention by the society referring to insurance business.

In Sweden the solidarity approach has been prevailing since long. The development, however, goes today towards a more market economical approach. The same seems to be the case in many other countries, not at least the European ones.

D. Insurance contract law

15. Insurance contract law offers a great many problems, which must be considered in the work of risk management. Some of them are the following.

a. Interpretation of contract

16. Even if the parties of the insurance contract are free to decide what they want, the law is not always out of the picture. There might be difficulties to understand afterwards what the parties have meant. The contract must be interpreted. Finally this is done by the lawyers.

The rule most commonly applied in Scandinavian insurance law, when it comes to interpretation of an insurance contract, is ”the unclear rule”. This rule means that if the insurance contract is unclear this will be to the disadvantage to the the party who wrote the policy, here the insurer.

b. Insurable interest

17. In all countries there seem to be a requirement of insurable interest for an insurance undertaking to be valuable. From an international point of view a distinction has to be made between life and indemnity insurance in this respect. Swedish life insurance law does not require that the person on whose life insurance is taken belongs to a certain category. English insurance law, however, in principle only accepts life insurance taken on those who are closest to the insurer; husbands and wives are considered to be such persons but not children.

Insurance law relating to property insurance also requires an economic interest of the insured. So, for example, the sentimental value of old letters are not insurable.

In some countries, as in England, a ”legal and equitable relation” to the subect-matter insured is also required. What does this mean?

Without doubt, the owner has such an interest in his property. Sellers of goods are in English law supposed to have an insurable interest in goods until their rights and duties relating to the goods have come to an end. Buyer of goods, who does hot have the goods in his possession or at his risk, or who has not made any advance in respect of the purchase, have no insurable interst in the goods. Lessor and lessee have an insurable interest in the property subject of the lease. The mortgagor of goods has an insurable interest in the goods.

These are some examples. But on the whole the law is rather unclear on the topic of insurable interest. This must be troublesome for the risk manager.

c. The time of payment

18. The most important obligation of the insurer is in Scandinavian and German law considered to be the duty to pay premium. This is said to be the insureds ”main” duty. Many legal questions arise in this respect, as for example the issue of the amount of premium, the place of payment, the mode of payment and who is authorised to receive the premium. The most burning issue for the insured however is the time of payment.

The general law of contract does not require a prompt payment unless the contract clearly indicates otherwise. All over the world, however, insurance law is much more exacting as far as the time of the payment of the premium is concerned. Most policies prescribe that the duty of the insurer shall be void in the event of default in the payment of any instalment. Hosever, in international case law it has been said that ”such a condition is wholly unnecessary, the punctual payment of every part of the premium being a condition precedent to the liability of the company.”[1] What is the reason for such a strict way of regarding delayed payment? The answer probably comes close to what was expressed by an American court, which said that ”promptness of payment is essential in the business of life insurance. All the calculations of the insurance company are based on hypothesis of prompt payments. They not only calculate on the receipt of the premiums when due, but on compounding interest upon them”.[2]

19. There are exceptions to this rule (”days of grace”). But these are very restricted. On the whole the main position is very firm. And this not only concerns life insurance. It is also valid for indemnity insurance.

20. In Scancinavian insurance law special rules concerning the time of payment of the premium have been set up in indemnity insurance in favour of consumers. But the main rule is stil rigid as far as enterprises have paid their premiums too late. The enormous difference between the general contract law and the insurance contract law in this respect could be called in question.

d. Non-disclosure

21. The insurance taker is obliged to disclose to the insurer all material facts; a fact must be distiunguished from opinion. The evident purpose of this rule it to enable the insurer to decide whether to make the contract and, if he does so, on what terms.

22. The rules concerning non-disclosure seem to be almost the same all over the world. According to them the onus of proving that there has been non-disclosure of a material fact is upon the insurer. There are many excuses which are accepted for having not disclosed to the insurer. One is that the information was not disclosed because it was a matter which the insurer could be presumed to know already. Another one is that the information was disclosed because the insurer made an error of judgement; he was not, as it is said in English insurance law, a prudent insurer.

Also these rules can be said to be vague in many regards. A lawyer can say much but not all. This creates a fundamental problem for the risk manager. What is he supposed to know about the legal rules? On what authority must he rely? To what extent must he devote himself to educated guesses when managing the risks?

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[1] *Frank* v *Sun Life Assurance Co* (1893) 20 OAR 564, 567 *per* Burton JA.

[2] *New York Life Insurance Co* v *Statham*, 93 US 24; L Ed. 789, 791 *per* Bradley J.