**THE LAW REFORM COMMISSION**
**OF WESTERN AUSTRALIA**

Project No 10

# Motor Vehicle Insurance

**WORKING PAPER**

**MAY 1972**

## INTRODUCTION

The Law Reform Committee has been asked to examine the law and practice relating to motor vehicle insurance and to consider whether any alteration to the law is desirable.

The Committee having completed its first consideration of the matter now issues this working paper. The paper does not necessarily represent the final views of the committee.

Comments and criticisms are invited. The Committee requests that they be submitted by 7 September 1972.

Copies of the paper are being forwarded to -

The Chief Justice and Judges of the Supreme Court
The Judges of the District Court
The Law Society
The Law School
The Magistrates Institute
The Crown Law Department
The Solicitor General
The State Government Insurance Office
The R.A.C. Insurance Co. Pty. Ltd.
The Fire & Accident Underwriters Association
The Non-Tariff Association of Australia (W.A. Branch)
Other Law Reform Commissions and Committees with which this Committee is in correspondence.

The Committee may add to this list.

A notice has been placed in *The West Australian,* inviting anyone interested to obtain a copy of this paper.

The research material on which this paper is based is at the offices of the Committee and will be made available on request.

## TERMS OF REFERENCE AND COMMENTS THEREON

1. "To consider the law and practice relating to motor vehicle insurance and whether any alteration to the law is desirable".

2. In this State insurance against claims arising out of injury to or death of a third party is compulsory and must be effected with the Motor Vehicle Insurance Trust, pursuant to the *Motor Vehicle (Third Party Insurance) Act 1943-1971*. Although such insurance is motor vehicle insurance, the Committee has presumed that it is not intended that it should deal with insurance of this type.

3. Motor vehicle insurance policies with which the Committee is concerned are those which cover claims arising out of one or more of the following items -

(i) Loss of or damage to the insured vehicle;

(ii) Damage to or destruction of property belonging to a third party;

(iii) Personal injury caused to a third party outside the *Motor Vehicle (Third Party Insurance) Act*. This cover has been of restricted application since 1966, when an amendment to the Act removed all earlier money limits set to the liability of the Motor Vehicle Insurance Trust;

(iv) Personal injury to the insured.

Most policies cover items (i), (ii) and (iii) and are generally referred to as "comprehensive" policies. Item (iv) is optional, the additional cover being available on payment of a further premium. Policies covering only items (ii) and (iii) are also available. These are called "third party" policies.

4. Over the past few years complaints by insured motorists have been taken up by the press and sometimes by local government bodies. Such of these as have come to the notice of the Committee form the basis of the present study.

5. Allegations contained in the complaints can be classified generally as follows -

(i) The unfairness to the insured of arbitration as a compulsory means of settling differences. The complaints in this area fall into two categories:

(a) The insurer can, in the privacy of arbitration proceedings, advance technically valid but morally unjust defences.

(b) Some arbitration agreements provide for each party to bear his own costs, whether or not he is successful, and this inhibits some insured persons from pressing their claims.

(ii) The unfairness of certain conditions, exclusions and warranties forming part of most policies, and the alleged harshness of insurance companies in enforcing their strict legal rights.

(iii) The small size of the print in some policies.

6. The question of the financial stability of some insurance companies has also been raised. Legislative provisions aiming at ensuring that money is available to meet claims under insurance contracts are contained in the *Commonwealth Insurance Act 1932-1968*, which superseded the Western Australian *Insurance Companies Act 1918-1931*. The Commonwealth Act obliges insurers to deposit money or securities in stated amounts with the Federal Treasurer as security for the meeting of their liabilities to the policy holders. The Federal Treasurer, the Hon. B. M. Sneddon, Q.C., has outlined proposed Commonwealth legislation to tighten these financial requirements (Cth. *Parl. Deb.* 1971, H. of R., p.4455). The proposals have been worked out in close consultation with representatives of all States. This matter has not been considered in this paper.

7. This Committee has already issued a working paper dealing with the *Arbitration Act 1895* (working paper, Project No. 18, issued 29 October 1971). Among other matters, it suggested substantially limiting the circumstances under which a party could enforce an agreement to arbitrate. The Committee's preliminary views expressed in the working paper on Arbitration would, if adopted, overcome the causes for complaints under paragraph 5(i).

8. This paper is therefore confined to complaints aimed at matters referred to in paragraph 5(ii) and (iii) above.

9. In a letter to *The West Australian* of 20 January 1972, the Premier, the Hon. Mr J. T. Tonkin, stated that the Government had commissioned a study of the proposals of the British Columbia Royal Commission on Automobile Insurance. The Committee also has been informed that the Commonwealth Australian Transport Advisory Council is studying the possibility of uniform legislation making it compulsory to insure against third party property damage arising out of the use of a motor vehicle.

10. Legislation resulting from either of the studies mentioned in the previous paragraph could of course relate to parts of the areas covered in this paper.

## THE LAW IN WESTERN AUSTRALIA

11. Generally speaking in Western Australia the law relating to motor vehicle insurance contracts is part of the general law of contract. In addition, because of the special circumstances of the parties to such contracts, the common law has developed the complementary doctrine of *uberrima fides* ('utmost good faith'), which is summarised in Cheshire and Fifoot, *The Law of Contract* (2nd Aust. ed., p.368), as follows -

> "... every contract of insurance, irrespective of its subject-matter, involves *uberrima fides* and requires full disclosure of such material facts as are known to the assured... Insurance is a contract upon speculation where the special facts upon which the contingent chance is to be computed lie generally in the knowledge of the assured only, so that good faith requires that he should not keep back anything which might influence the insurer in deciding whether to accept or to reject the risk. The

requirement of *uberrima fides* is bilateral, although the case law emphasises mainly the obligation in this connection upon the part of the assured".

12. The only enactments bearing on conditions in motor vehicle insurance contracts are ss. 21 and 23 of the *Hire Purchase Act 1959*, which deal with the insurance of goods comprised in hire purchase agreements. Section 21 empowers the court to excuse a failure of the insured to observe a term of the insurance contract if it appears to the court that the insurer is not prejudiced by the failure. Section 23 restricts the application of s.21 to contracts of insurance in which at least part of the premium payable for cover has been included as part of the total amount payable for the goods bought.

13. The Committee knows of no statute relating to the minimum size of print in motor vehicle insurance policies.

## THE LAW AND PROPOSALS FOR REFORM IN OTHER PLACES VICTORIA

14. Section 25 of the Victorian *Instruments Act 1958* provides that no contract of insurance shall be avoided by reason of an incorrect statement on the faith of which that contract was entered into, unless that statement is either fraudulently untrue or material in relation to the risk of the insurer.

Section 27 of the Victorian Act enables an insured to maintain legal proceedings against the insurer notwithstanding the failure to give notice within the time required, provided that the insurer has not been unduly prejudiced.

(Section 28(2) (a) avoids clauses of the *Scott v. Avery* type by providing that arbitration shall not be a condition precedent to the institution of court proceedings and that neither party has the right to apply to the court for a stay of these proceedings).

### Ontario

15. Section 156 of the *Ontario Insurance Act* provides that the inaccuracy of any statement in an application for a policy cannot be pleaded to avoid that policy unless the statement is also material to the contract. (See R.S. Ont., 1914, c.183, considered in *Mutual Life Insurance Co. of New York v. Ontario Metal Products Co.* [1925] A.C. 344).

**Other jurisdictions**

16. In 1957, the English Law Reform Committee in its Fifth Report (*Conditions and Exceptions in Insurance Policies*) (Cmnd. 62, para. 14), made the following recommendations:

> " … We think that any or all of the following provisions could be introduced into the law and that no legal difficulties would arise in their application -
>
> (1) that for the purposes of any contract of insurance no fact should be deemed material unless it would have been considered material by a reasonable insured;
>
> (2) 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;
>
> (3) that any person who solicits or negotiates a contract of insurance should 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 should be deemed to be the knowledge of the insurers".
>
> No legislation has as yet resulted from these recommendations.

17. Although England and New Zealand have enactments relating to insurance, these are aimed at ensuring the financial stability of insurance companies. Queensland established the office of Insurance Commissioner by the *Insurance Act* of 1960. The Commissioner's powers, however, are confined to financial matters.

## DISCUSSION OF THE COMPLAINTS

### Terms and conditions: sum insured and market value

18. Motor vehicle insurance policies can be either "comprehensive" or "third party" (see paragraph 3 above).

Paragraphs 19 to 26 below do not apply to "third party" policies. The remainder of the paragraphs, however, would.

19. There appear to be three types of comprehensive policies in use in Western Australia:

(a) the "indemnity" policy;

(b) the "safety record plan" policy; and

(c) the "valued" policy.

20. In the "indemnity" type policy, the insured is asked to state the sum for which he wishes to insure his vehicle, and the premium is calculated on that sum. The insurer undertakes to indemnify the insured against loss or damage to the vehicle; but, by agreement, the sum payable is not to exceed the market value of the car at the time of loss, or the sum insured for, whichever is the lesser amount. Thus in the case of total loss, it is possible that the insured would be paid less than the sum for which he insured the vehicle.

21. The "safety record plan" policy applies only to private vehicles. The premium is calculated in accordance with a formula which takes into account the insured's driving record, the price of the vehicle when new, how prone the model is to accidents, and how expensive it is to repair. The insured is indemnified up to the market value of his car at the time of loss. Policies of this type are offered by members of the Fire and Accident Underwriters' Association of Western Australia.

22. The "valued" policy is a policy under which an average of the depreciating value of the vehicle over the year insured for is agreed upon annually by the parties prior to the contract and this becomes the "sum insured". The premium payable is calculated on that basis. Damage or loss is paid up to the "sum insured". The policy expressly declares that the market value of the vehicle shall not be deemed to be less than the "sum insured".

23. Some dissatisfaction has arisen concerning payments for total loss. As far as the Committee is aware complaints in this regard have been only in connection with "indemnity" policies (see paragraph 20 above).

24. The complainants in these cases appear to have misunderstood the nature of the obligation undertaken by the insurer.

25. If the insured knew that under an "indemnity" policy he would not be paid more than actual market value at time of loss, doubtless he would ascertain the real value of his vehicle and quote a realistic figure as "sum insured". Alternatively, he could if he so wished take his business to an insurer who offered a "safety record plan" policy or a "valued" policy (see paragraphs 21 and 22 above).

26. It has been suggested that motor vehicle insurance policies should be restricted to the "valued" policy type. The Committee thinks this would not be justified. Some insurers in their proposal forms emphasise that the sum quoted by the proposer as the "sum insured" will not necessarily be the value that will be placed on the vehicle at the time of loss. Such a practice appears to have much to commend it and in the case of "indemnity" policies could perhaps be made a statutory requirement. To be of use the statement would need to be conspicuous and, indeed, it would need to be brought expressly to the insured's attention.

**Terms and conditions: the "basis of the contract" clause**

27. The duty of disclosure imposed by law under the doctrine of *uberrima fides* is confined to facts actually known to the insured (Fletcher-Moulton L.J. in *Joel v. Law Union and Crown Insurance Co.* [1908] 2 K.B. 863, at p.884). This duty may be enlarged by the contracting parties themselves. Cheshire and Fifoot, *The Law of Contract* (2nd Aust. ed., p.370) comments -

> "... insurers have taken extensive, perhaps indeed unfair, advantage of this contractual freedom. In practice they almost invariably require the assured to agree that the **accuracy** of the information provided by him shall be a condition of the validity of the policy. To this end it is common to insert a term in the proposal form providing that the declarations of the assured shall form the basis of the contract. The legal effect of this term is that if his answer to a direct question is inaccurate, or if he fails to disclose some material fact long forgotten or even some fact that was never within his knowledge, the contract may be avoided despite his integrity and honesty of purpose. Nay more, his incorrect statement about a matter that is nothing more than a matter of opinion is sufficient to avoid the policy".

28. We have been informed that policies in common use in Western Australia oblige the insured to warrant the truth of the statements made in the proposal and to agree that they shall be the "basis of the contract" between insurer and insured.

29. One question usually asked by insurance companies is -
"Have you or any person who to your knowledge will drive the motor vehicle any physical defect, infirmity, impairment or affection of the eyesight or hearing, or suffered from a fit of any kind?" Such a question refers to a matter which, even for a doctor, may be a subject of speculation or opinion.

30. Complaints have been made that some insurance companies have relied on unintentional omissions relating to unimportant or long forgotten accidents or traffic convictions to avoid the contract.

31. The Committee believes that the practice of drafting insurance contracts so that the insured warrants the truth of every statement made is one that could result in injustice.

32. The Committee is provisionally of the view that, in the absence of a fraudulent intention, an incorrect statement or an omission in the applicant's answers should avoid a contract of insurance only if the statement or omission is material. Thus the Committee feels that legislation along the lines of s.25 of the *Victorian Instruments Act* (see paragraph 14 above) is desirable. The Committee also believes that the practice of enlarging the duty of

disclosure (see paragraph 27 above), so as to make it apply to facts that the insured did not know or could not have known, could cause injustice and that there is something to be said for implementing the proposals of the English Law Reform Committee (see paragraph 16 above), that a contract of insurance cannot be avoided where the insured can prove that the statement was true to the best of his knowledge and belief.

33. The Committee is also of opinion that there is value in the suggestion by R. A. Hasson in *The Modern Law Review* (1971 Vol. 34, p.29, at p.40), that an insurer should be required by statute to attach to the policy, when it is delivered, a copy of the completed proposal form. The insured would then possess the complete contract (see paragraph 28 above). Hasson, in the same article, supports the substance of the Victorian legislation and the English Law Reform Committee's report.

**Terms and conditions: warranties and exclusions**

34. Motor vehicle insurance contracts invariably contain warranty or exclusion clauses which limit the liability of the insurer. Such a clause, for example, is the common exclusion clause relating to unsafe condition: the insurer shall not be liable for any accident, injury, loss, damage or liability caused, sustained or incurred whilst the motor vehicle is being used in an unsafe condition.

35. In some respects this clause has been interpreted by the courts in favour of the insured. In *Bashtannyk v. New India Assurance Co. Ltd.* [1968] V.R. 573, the Court held that the words "being used whilst in an unsafe condition" were not concerned with the condition of the car unrelated to its user at the time of the accident. Even though the vehicle had worn tyres which in other circumstances could have made the vehicle unsafe to use, the exclusion clause may not apply if the accident happened whilst the vehicle was being driven on a dry road at a moderate speed. In *New Zealand Insurance Co. Ltd. v. Pihema* [1967] N.Z.L.R. 285 the court held that, although the presence of three passengers by the side of the driver had impaired the driver's ability to control the car, this had not affected the steering mechanism itself and it could not be said that the car had been in an unsafe condition.

36. In other respects the courts have interpreted the clause strictly against the insured. Under it an insurer can deny liability whether or not the loss or damage was due to the unsafe

condition. In *Bashtannyk's* case (paragraph 35 above), counsel for the insured put forward the argument that an exclusion clause of the type set out in paragraph 34 above applied only where the damage and the unsafe condition were causally linked. Winneke, C.J., dismissed the submission with these words: "It is sufficient for me to say that in my opinion such a construction is precluded by the plain grammatical meaning of the words used in the clause" (at p.575). In *Trickett v. Queensland Insurance Co. Ltd.* [1936] A.C. 159, the Privy Council held that the driving of a car by the insured in a damaged or unsafe condition within the meaning of an exception clause relieved the insurer of liability irrespective of whether the insured was aware at the time of the accident of the damaged or unsafe condition of the car.

37. In commenting on this area of insurance practice, the English Law Reform Committee (Cmnd. 62, paragraph 11) said:

> "It appeared to us that such a state of the law [concerning compulsory arbitration clauses], combined with the prevalence of such terms and conditions in insurance policies as we have described in the preceding paragraphs, is capable of leading to abuse, in the sense that a variety of circumstances may entitle insurers, after a loss has occurred, to repudiate liability as against an honest and at least reasonably careful insured. Material was available to us, in the form both of reported cases and of instances within the experience of those who supplied us with information, which showed that such abuses had in fact sometimes occurred. It was forcefully represented to us by those representatives of insurance interests who submitted memoranda or gave oral evidence that no reputable insurer would rely on a purely technical defence to defeat an honest claim. This may well be true, and we think that in general it is true, but it does not alter the fact that 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".

38. In spite of having reached this conclusion, the English Committee felt that it was not within its competence to suggest alterations of the law that would alleviate such situations in the interest of the insured. We, however, suggest that where the unsafe condition was not and could not reasonably have been detected by the insured, or where the accident was not caused by the unsafe condition, the insurer should not be able to escape liability.

**Terms and conditions: loss of no-claim bonus**

39. Complaints under this head fall into two categories -

(i) those where the complainants take the view that if they were not at fault in an accident they should not lose their no-claim bonus, in spite of their having claimed on their insurer; and

(ii) those where the complainants hold that there is injustice when a no-claim bonus, lost for a claim made, is not reinstated where all payments made by the insurer under the claim are subsequently recovered from a third party.

40. A no-claim bonus is, as its name suggests, a discount on premiums, allowable to an insurer who has not claimed. By the terms of most motor vehicle insurance contracts, a discount is allowed where the insured has no claim pending and has received no payment under a prior claim during preceding specified periods. Under most contracts a claim for a broken windscreen does not affect the no-claim bonus.

41. In at least one case an insurer's proposal form contains the additional concession that the no-claim bonus will be reinstated, notwithstanding the making of a claim, if payment made by the insurer under the claim is recovered from a third party. Where no such concession is included as a term of the contract and a claim is made, it would appear that the bonus is lost and the insured has no right to reinstatement even if the insurer recovers in full. The Committee, however, has been informed that many insurers do not insist on the strict application of the clause.

42. Where complaints are due to a misunderstanding of the legal effect of a no-claim bonus clause, they would disappear if applicants for a policy were given a clear explanation of the operation of the clause, emphasising the fact that it is a no-claim, and not a no-fault, bonus. The steps for achieving this could be prescribed by statute.

43. In so far as the complaints are not based on a misunderstanding, they appear to lack substance.

**Size of print**

44. Complaints have been made that motor insurance policies are printed in small type and that this makes it difficult for the insured to become aware of all the terms, conditions and exclusions these contain. Although there may not be any real objection to a statutory requirement as to the size of the typescript to be used, the Committee is not convinced that this of itself would be of any real advantage. The common practice is for the applicant for insurance cover to sign a proposal form which contains a statement whereby the applicant agrees to accept the insurer's policy, subject to the terms, exclusions and conditions prescribed by the insurer and contained in the policy. The policy itself is sent to the insured later, after the contract has been made.

45. It seems clear that the terms, exclusions and conditions of the policy are binding on the applicant whether or not he has read them. Although some insurers include in the proposal form a summary of what they consider to be the important terms, others do not. It could possibly be made a statutory requirement that the terms, exclusions and conditions of the policy be made available *in extenso* to the applicant before he signifies acceptance of them or, at least, that specified clauses be adequately summarised in the proposal form. A statutory requirement of the size of print would be most useful at this point. Possibly the majority would not read the material made available, but this does not seem to be a reason for denying to others full opportunity of doing so.