The AFCA Approach to non-disclosure and misrepresentation

We have created a series of AFCA Approach documents, such as this one, to help consumers and financial firms better understand how we reach decisions about key issues.

These documents explain the way we approach some common issues and complaint types that we see at AFCA. However, it is important to understand that each complaint that comes to us is unique, so this information is a guide only. No determination (decision) can be seen as a precedent for future cases, and no AFCA Approach document can cover everything you might want to know about key issues.

1 At a glance

1.1 Scope

The purpose of this document is to explain AFCA's approach to complaints from consumers when an insurer denies a claim on the basis the complainant failed to disclose (non-disclosure), or misrepresented, a matter.

1.2 Who should read this document?

- Financial firms, consumers and consumer representatives who have a complaint at AFCA that includes non-disclosure or misrepresentation.
- Anyone who wants to understand how AFCA applies legal principles, industry codes and good industry practice when considering complaints where the issues of non-disclosure or misrepresentation are raised.

1.3 Summary

For innocent non-disclosure, AFCA will consider:

- Has the insurer clearly informed the complainant of their duty of disclosure?
- Has the complainant failed to comply with their duty of disclosure?
- Can the insurer show the extent of its prejudice?

For innocent misrepresentation, AFCA will consider:

- Has the complainant made a misrepresentation?
- Did the complainant, or a reasonable person in their circumstances, know their misrepresentation was relevant to the insurer's decision to accept the risk?
- Can the insurer show the extent of its prejudice?

A misrepresentation or non-disclosure will be considered fraudulent if the person did so knowingly, without belief in its truth, or recklessly. This will require clear and convincing evidence in support. If it is fraudulent, the insurer will generally be able to avoid the policy and deny a claim.

AFCA will also consider other relevant factors to ensure the decision is fair, including: if the complainant provided an obviously incomplete or irrelevant answer, if the complainant genuinely believed the answer provided was true, or if avoiding the policy is unfair.

2 In detail

2.1 Innocent non-disclosure

This applies to disputes where the insurer says the complainant failed to disclose a matter but does not allege this was done fraudulently.

For the sake of convenience, this approach presumes the complainant is the insured.

Sections 21, 21A, 21B, 22 and 28 of the *Insurance Contracts Act 1984* (Cth) (the Act) apply.

To refuse payment of a claim on this basis, the insurer must show:

- The complainant was clearly informed of the general nature and effect of their duty of disclosure before the relevant policy was issued – the relevant policy is the one that would respond to the claim.
- If the policy was an 'eligible contract of insurance'[1]:
  - The insurer asked the complainant a specific question (if the non-disclosure relates to when the policy was first issued); or
  - The insurer (if the non-disclosure relates to the policy being renewed) either:
    - asked the complainant a specific question; and/or
    - gave the complainant a copy of the matters previously disclosed and asked the complainant to inform it of any change
  - The complainant did not accurately respond to the question or update the information previously given
  - The complainant knew the correct answer and a reasonable person in their circumstances would have disclosed this information
- If the policy is not an 'eligible contract of insurance':
  - The complainant knew about the information
  - The complainant, or a reasonable person in their circumstances, knew this information was relevant to the insurer's decision to accept the risk
  - The complainant did not disclose this correct information

[1] These are policies for motor vehicle, home building, home contents, travel, consumer credit or personal accident and sickness.

- The extent of the insurer's prejudice by the complainant's failure to disclose this information.

  Normally, the insurer establishes prejudice if it can show it would not have not have issued a policy or would have issued the policy on different terms that would have resulted in a different outcome (e.g. an exclusion would have been imposed that would have applied to the claim)

Even if the insurer can establish all this, AFCA will consider any other aspect of the Act that may be relevant. For example, if the complainant provided an obviously incomplete or irrelevant answer (section 21(3)) or the insurer already knew about the matter (section 21(2)(b)).

Other considerations

AFCA may also consider other matters it believes are relevant. Such as, if the complainant was in a vulnerable situation (e.g. had minimal literacy skills, limited understanding of English) and the insurer was aware of this.

AFCA considers this approach to be fair in all the circumstances because:

- it is mostly consistent with the Act, which was designed to ensure a fairer application compared to the previous common law
- it provides sufficient flexibility to take into account unusual circumstances that can arise in these matters

2.2 Innocent misrepresentation

This applies to disputes where the insurer says the complainant made a misrepresentation but does not allege this was done fraudulently.

Often this issue will arise alongside non-disclosure. This is because the same set of facts can give rise to both grounds.

Sections 23, 24, 26, 27 and 28 of the Act apply.

To decline a claim on this basis, the insurer must show:

- The complainant made a statement before the contract was entered into
- This statement was either a:
  - statement of fact that was untrue;
  - statement of opinion that was not the subject of an honestly held belief; or
  - statement of intent that never existed at the time provided.

- The complainant knew the statement was relevant to the insurer's decision to accept the risk, or a reasonable person in the circumstances could be expected to know the matter was so relevant

- The extent of the insurer's prejudice by the misrepresentation.

This part of the approach is the same as innocent non-disclosure. That is, the insurer would normally show it would have not have issued the policy if the misrepresentation had not occurred or would have issued the policy on different terms that would have resulted in a different outcome (e.g. an exclusion would have been imposed that would have applied to the claim).

Other considerations

Even if the insurer can establish all this, AFCA will consider any other provision of the Act that may be relevant. For example, if the complainant genuinely believed the answer to be true, and a reasonable person in their circumstances would have formed the same belief (section 26(1)), or the insurer's question was ambiguous (section 23).

AFCA may also consider other matters it believes are relevant. Such as, if the complainant was in a vulnerable situation (e.g. had minimal literacy skills, limited understanding of English) and the insurer was aware of this.

AFCA considers this approach to be fair in all the circumstances because:

- It is mostly consistent with the Act, which was designed to ensure a fairer application compared to the previous common law
- It provides sufficient flexibility to consider any unusual circumstances that may arise in these matters.

2.3 Fraudulent misrepresentation and fraudulent non-disclosure

There are times when an insurer says the misrepresentation or non-disclosure was fraudulent.

A misrepresentation or non-disclosure is fraudulent when the person did so knowingly, without belief in its truth or recklessly (not caring whether it is true or false). If it was made negligently or carelessly, this is not fraud.

Given the seriousness of the allegation, AFCA would expect the insurer to provide clear and convincing evidence to establish this.

If the misrepresentation or non-disclosure is fraudulent, then the insurer can generally void the policy if it can show that it would not have issued the same policy for the same premium if the correct information was disclosed.

In limited cases, voiding the policy may not be fair. This may be when the information not disclosed made little difference to the insurer's position. For example, it would

have simply charged a slightly higher premium or imposed a condition that made no difference to its liability.

In those cases, AFCA will consider whether it is fair in all the circumstances for the claim to be denied. This requires consideration of at least the following factors:

- The extent of prejudice the non-disclosure or misrepresentation had on the insurer's position
- The requirement to deter fraudulent conduct
- Whether the impact extends beyond the person who perpetuated the fraud (e.g. an innocent co-insured).

This is also consistent with section 31 of the Act. Whilst AFCA is not a court, it is required to do what is fair in all the circumstances. AFCA considers it is appropriate to have regard to this provision given it aligns closely to our purpose.

2.4 Important things to note

A person is only required to disclose what they know

That is, they need to disclose something that was subject to a true belief, held with sufficient assurance to justify the term 'known'. It means considerably more than suspects or strongly suspects.

Therefore, if a person disclosed something they believed was the truth (i.e. held with sufficient assurance to justify the term 'known'), then there is no non-disclosure even if that belief was wrong. However, if they have disclosed something they have not 'known' (i.e. they guessed or suspected the answer), then they have not complied with their duty of disclosure.

Most general insurance policies operate for one year and are renewable

Each renewal is a separate contract of insurance. Therefore, it is important to identify which period of insurance is relevant to the non-disclosure or misrepresentation. This includes ensuring the non-disclosure or misrepresentative is continuing, operative or applicable.

For example, a person may have failed to disclose a licence suspension they had in the past 5 years when the policy was first issued. However, if by the next renewal that suspension was more than 5 years old, it is no longer continuing, operative or applicable for that renewal.

An insurer is not legally required to clearly inform the complainant of their duty of disclosure at each renewal

This is because if the insurer has done so once, then effectively they have been deemed to do so at each subsequent renewal (section 11 of the Act).

Having said that, AFCA may consider it unfair if the information was provided a long time ago.

Prejudice

If the insurer shows that their prejudice is that no policy would have been issued, then the premium should be refunded from the point in time they would not have offered insurance. This is because the extent of their prejudice does not include the retention of the premium. The prejudice is limited to the claim itself.

'A reasonable person in the circumstances'

The phrase in the Act of 'a reasonable person in the circumstances' is generally an objective test although a degree of subjectivity must be applied. It is a matter of looking at a reasonable person in the same circumstances as the complainant.

2.5 What information does AFCA need?

From the insurer

AFCA may ask the insurer to provide:

- Clarification on what basis it is denying the claim
- How was the policy arranged?
- Was the duty of disclosure provided?
- What questions were asked of the complainant or its representative?
- How did the insurer record the response(s) provided by the complainant?
- A copy of the underwriting guidelines (at least of the relevant extracts) and a statutory declaration from the underwriter confirming how the insurer would have assessed the complainant's risk if accurate information was provided.
- Does any discretion apply to the insurer's underwriting decision?
- Proof of despatch of documents (if the complainant says they did not receive the insurer's correspondence, especially the renewal certificate).
- Product Disclosure Statement
- Certificate of insurance and/or Renewal certificate
- Has the insurer cancelled the policy?
- From when should the insurer refund the premium?

From the complainant

AFCA may ask the complainant to provide:

- A description of when the damage occurred
- An explanation of how the insurance policy was taken out:
  - Did the complainant do it themselves or through an agent or broker?
  - Was the policy purchased online, over the phone, at a branch?

- Did the complainant complete and/or sign a form? If so, have they got a copy of the form?
- Does the complainant recall being asked the specific question in dispute? If so, do they recall how they responded?
- Did the complainant receive the policy documents (Product Disclosure Statement and Certificate of insurance, renewal certificate)? If so:
  - Did they read the documents?
  - Did they notice any error? If yes, did they attempt to correct this with the insurer?

3 Context

3.1 Case studies

Case study 1 – A case of criminal acts (655054)

The complainant lodged a claim on 1 November 2016 for fire damage to his home.

The insurer denied the claim due to non-disclosure. The insurer said the complainant failed to disclose a criminal charge when altering the policy in late 2015. If the complainant had done so, the insurer would not have continued to cover the property.

When the policy was altered, the complainant was asked to verify the following information was still correct:

> You or anyone to be insured under this policy has NOT committed any criminal acts in relation to Fraud, Theft or Burglary, Drugs, Arson, Criminal, Malicious and/or Wilful damage

On 12 June 2015, the complainant was charged with criminal offences, including the cultivation of a prohibited substance. Later, he pleaded guilty to this offence. This plea was made some time after the alteration.

The insurer said that he should have disclosed his criminal charge in response to the above statement. The panel disagreed.

The panel considered a reasonable person may interpret this phrase as referring to criminal convictions, as the complainant did. The question that the insurer asks the complainant to respond to is, at the least, ambiguous as to whether it refers to a charge rather than a conviction.

This view is consistent with the presumption of innocence in criminal law. It is also unreasonable to expect a person to admit to an insurer a matter which could prejudice their legal defence in criminal proceedings.

Therefore, the panel was not satisfied the complainant was required to disclose his criminal charge in response to the above.

Further, even if it could be said the complainant should have disclosed his criminal charge, the panel was not persuaded the insurer would have refused to cover the property based on the following:

- On 9 November 2016 the complainant disclosed his criminal charges (yet to be convicted) to the insurer's investigator
- Eight days later the insurer renewed the complainant's home and contents policy for another property
- On 20 April 2017 the insurer issued an amended certificate of insurance after the complainant altered the home building policy for the destroyed insured property
- On or around 25 October 2017 the insurer issued a policy renewal for the destroyed property.

Further:

- The insurer's underwriting guidelines refer to a person's criminal history, not charges
- The insurer's underwriter was unclear as to whether they referred to charges or convictions when saying the insurer would not have offered any policy
- The insurer did not provide any examples that they refused to provide cover by reference to a charge rather than a conviction.

Given this, the panel was not satisfied the insurer showed any prejudice by the complainant's failure to disclose the charge and therefore, the insurer was liable to accept the claim.

Case study 2 – A case of context and risk (634952)

The complainant held a contents policy with the insurer. He lodged a claim for storm damage to contents at his place of residence.

The insurer denied the claim on the basis the complainant failed to disclose his claims history. The complainant's claims history showed he had lodged five claims in the past five years.

The insurer says if he had disclosed this history, it would not have renewed the policy. This is because the underwriting guidelines say they will not issue a policy to a person who has lodged more than three claims in the last five years.

The relevant question asked by the insurer in the renewal was:

> In the last 5 years has the insured or any household member had any thefts, burglaries or made any insurance claims for home and/or contents?

There is no dispute the complainant did not disclose any claim in response to this.

The complainant had numerous investment properties. At least two of these claims involved his investment properties. The issue was whether he had to disclose his claims for the investment properties when asked about 'any insurance claims for *home* and/or contents?'.

The ombudsman concluded he did not need to for the following reasons.

The policy defined 'home' as the complainant's current place of residence. This did not assist the insurer because none of the claims involved this property.

Both Macquarie and Oxford dictionaries refer to 'home' as a person's place of residence.

Given this, the ombudsman concluded that a reasonable person in the complainant's circumstances would have only disclosed their claims history about their place of residence (or their contents). This is consistent with:

- the ordinary and natural meaning of the word 'home'; and
- the risk being insured – that is, the complainant's contents at his home

Therefore, the complainant did not need to disclose claims for his investment properties.

This meant the insurer could not show it was prejudiced to the full extent of the claim. This is because the insurer's underwriting guidelines do not exclude people with only three claims.

Therefore, the insurer had to accept the claim subject to any additional premium that may have been charged if the claims history involving the complainant's home had been disclosed.

Case study 3 – A case of underwriting (647598)

The complainant lodged a claim for hail damage to his commercial property with his insurer.

The insurer denied the claim on the basis the complainant failed to disclose the correct age and condition of the property. The insurer says that if the complainant had done so, it would not have issued the policy.

The available information showed that the complainant had purchased the policy through a broker. The broker had disclosed that the property was built in 1970 however, there was no dispute the property was built around 1925.

Therefore, the complainant had failed to comply with his duty of disclosure. There was no dispute this was innocent. The issue became whether the insurer could show its prejudice.

In support of its position, the insurer provided a statutory declaration from the national underwriting manager. This underwriter said a policy would not have been issued if it was disclosed:

- The property was constructed between 1898-1900; and/or
- The condition of the property was as outlined in two reports provided by two experts (IB and CD).

The panel reviewed the underwriting guidelines and noted:

- They related to a home building – this was a commercial property
- They did not refer to the age of the property
- They only required the property to be actively cared for, water tight, well-maintained, structurally sound and secure, and likely to withstand natural peril.

Various reports were provided about the property. In analysing these reports, the panel noted:

- The insurer's loss adjuster (C) said the property appeared to be well-maintained
- Another expert (CD) said the building has been maintained in a satisfactory condition given the age and method of construction
- Another expert (IB) said the roof was in average to good condition and the maintenance related issues repaired.

These reports also noted the previous maintenance work and that the roof was structurally sound and water-tight. There was no information implying that the roof could not withstand natural peril. There was also no suggestion the complainant had actual knowledge of any issues with the roof.

The panel also noted the insurer had previously insured the property (with a previous owner), with a build date disclosed as 1905.

The complainant had also submitted that:

- A new roof was fitted in the last 10-30 years
- All circuit boards had been updated in the past 3 years
- The previous owner had undertaken electrical rewiring; and
- Licenced tradespersons were employed to maintain the roof.

The insurer did not refute any of this.

When considering this evidence, the panel was not satisfied the insurer could show that it would not have insured the property. This meant the insurer could not establish the extent of its prejudice.

Therefore, the insurer was liable to accept the claim.

3.2 References

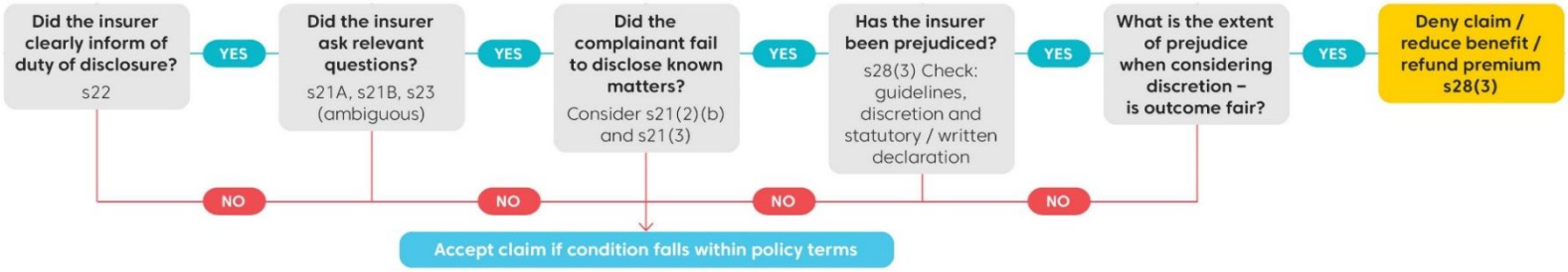
Term	Definition
Complainant	a person who has lodged a complaint with AFCA
Financial firm	a financial firm such as an insurer, who is a member of AFCA

Useful links

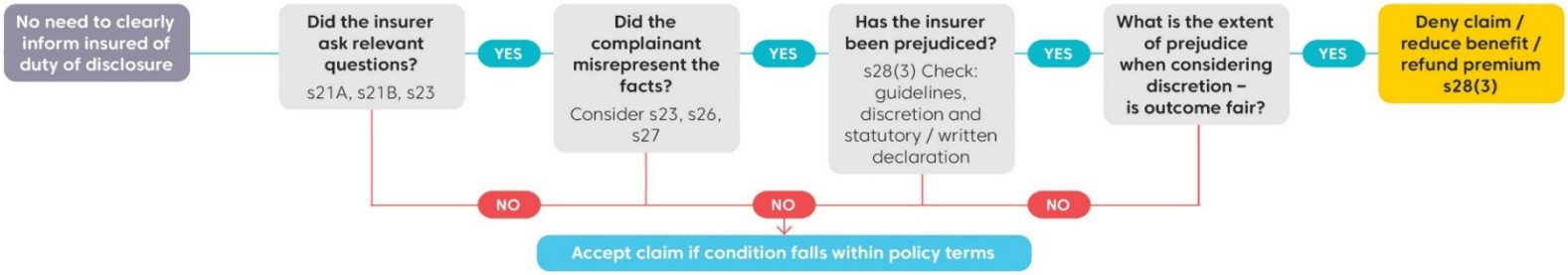
Document type	Title / Link
Insurance Contracts Act	This Commonwealth statute can be found here: legislation.gov.au/Details/C2019C00115
Austlii	Austlii is a free resource that contains a full extract of most of the judgments issued in Australia austlii.edu.au

Appendix A - Innocent / fraudulent non-disclosure and misrepresentation decision guide

Innocent non-disclosure



Innocent misrepresentation



Fraudulent non-disclosure / misrepresentation