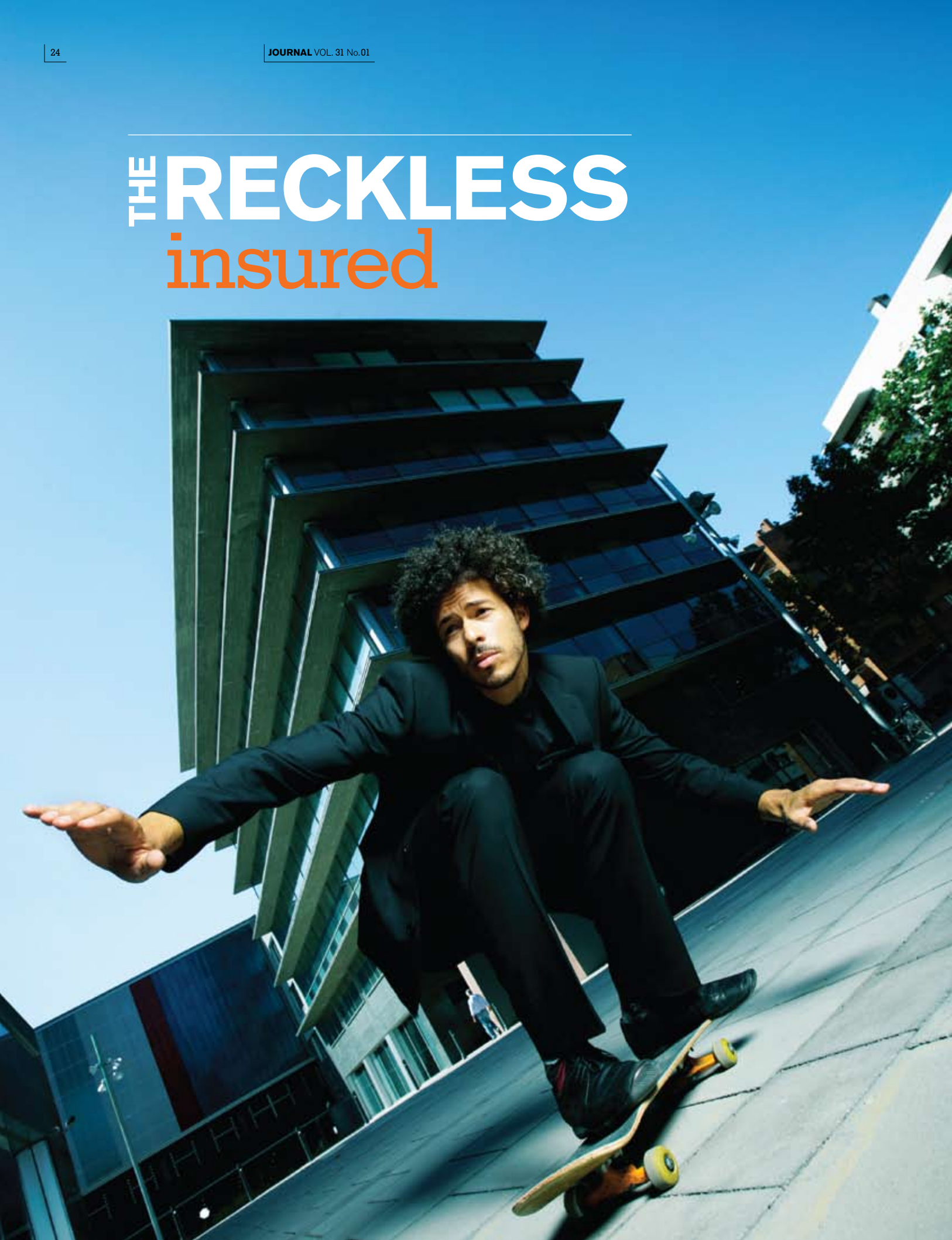

THE RECKLESS insured



FEATURE



This issue's comment from **Peter Hardham**, Panel Chair, Insurance Ombudsman Service.

comment

TO WHAT AN EXTENT IS AN INSURED LIABLE FOR MAJOR ERRORS OF JUDGMENT – OR MOMENTS OF SHEER INANITY? SHOULD THE INSURANCE INDUSTRY TAKE STEPS TO BE LESS RELIANT ON THE VAGARIES OF JUDICIAL INTERPRETATION OF THE TERM “REASONABLE CARE”?

I have been contemplating to what an extent an insurance policy provides cover for acts of gross negligence, stupidity or recklessness of the insured. There are many circumstances where insurance policies clearly do not provide cover, such as when an insured intentionally damages property, or the insured expects the policy to provide cover for maintenance items e.g. gradual damage to a home caused by wear and tear, or if the insured acts unlawfully i.e. is involved in an accident after having robbed a bank, or while driving in a highly altered state of consciousness. However, I ask, to what extent is the insured forgiven for major errors of judgment or moments of sheer inanity?

I am sure the many hundreds of claims managers, assessors, underwriters and investigators who regularly read my articles all agree that an insurance policy will provide cover in the following circumstances:

- ❑ A young man is driving his new sports car along Beach Road in Melbourne when he spies a young lady suitably attired for the beach. In the course of admiring her uniform, he fails to observe a small car driven by a dear old lady on her way to church has come to a halt at the traffic lights, and his vehicle heavily collides with the rear of the vehicle, resulting in a crisis of faith for the driver and a look of contempt from the young lady.
- ❑ A harassed mother returns thankfully to the family home after collecting her three precious children from school in the new Beamer. After alighting from the vehicle, she carelessly fails to notice the smallest child has returned to the vehicle, and released the handbrake causing the newly polished car to finish up in the family swimming pool (remember the TV advertisements?).
- ❑ The new speedboat is not moored correctly and it drifts fatefully to sea and sinks or is lost.
- ❑ After participating in the office Christmas party, Gerald has consumed three light beers.

Unfortunately, he is late home for the family dinner and falls down the stairs thereby breaking his leg or alternatively, fails to observe a shredding machine does not have its guard in position and is left with 9.7 fingers.

The issue that needs to be addressed is to what extent is the insured reasonably responsible for the safety and welfare of the insured property, whether it is a motor vehicle, boat, motorcycle, luggage while travelling overseas – or for the safety and welfare of oneself in terms of personal safety.

In my opinion, the insurance industry and the law have provided different standards for insured persons for different forms of property. It would appear that in terms of a motor vehicle, acts of gross negligence, stupidity or even recklessness are covered, if not encouraged. However, if luggage is stolen while a policyholder is not in a position to observe it, most policies do not provide cover. In terms of marine/pleasurecraft, insurers have high expectations of policyholders in terms of maintenance and design of boats and yachts. However, in terms of personal safety, many policies effectively provide protection in many instances of gross carelessness e.g. leaving a guard off a machine.

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In an article published in this *Journal* in May 2001 (*Are Bad Drivers Covered?*) I discussed standards underwriters applied to drivers of motor vehicles in terms of what abhorrent behaviour was not covered. However, in this article, I want to more broadly explore the issue to a range of general insurance products in the light of recent case law and developments in judicial attitudes.



Commercial purpose and policyholder expectations

It is difficult for me to rationalise these anomalies apart from the fact that the commercial purpose of the policy must be considered as well as the reasonable expectations of policyholders. In my opinion, case law has clearly established that if a court (or the Panel) can be persuaded to take these matters into account, it may be the policy terms will be "read down" in order to give effect to these concepts. And of course, lurking behind every policy exclusion, (especially the ones that may produce an unfair or ultra-legalistic result) is the overriding duty to act at all times with utmost good faith towards policyholder, and the court (and the Panel) is given the power to refuse to allow an insurance company to rely upon a policy term if, to do so, would be contrary to the duty of utmost good faith. (See sections 13 and 14 of the Insurance Contracts Act and the very valuable discussion on this subject contained in the recently decided High Court case of *CGU v AMP* (2007 HCA36).

I would like to remind readers that this subject can impact on all of us in our everyday lives (for those who have them) particularly in the context of motor vehicle insurance. Most of the motor vehicle policies require the policyholder to take "reasonable precautions or care" for the safety and security of the vehicle

the conduct was reckless that is, did the insured party "court the danger" and then ignore the risk?

In order to constitute reckless behaviour of this type, it is necessary for an insurer to establish that the policyholder was aware of the danger and took no measures or no effective measures to avoid it, such as a driver continuing to drive at excessive speed despite the protestations and warnings from his passengers and then having an accident. This test was re-emphasised in another recent case of *Tilley v Lawless* [2007] VSC 103.

In this context, I mention that over the years, the Panel has had to deal with many disputes where vehicles have been stolen after the drivers have left the keys in the ignition, usually in a petrol station, when they have gone to pay for the petrol and purchase food in the petrol station store. In the great majority of cases, the Panel has determined the insurer is not liable for the claim because, to leave the keys of a motor vehicle in the ignition while the vehicle is unattended for a significant period, satisfies the definition of failure to take reasonable care for the vehicle in the context of reckless behaviour. However, every case is dependent on its own facts.

In Determination No. 26546, the applicant's vehicle was stolen while in the process of purchasing petrol at a service station. The relevant facts are that before he filled his vehicle with

less than 15 seconds. He admitted he was in error to the extent he suffered "a momentary lapse in judgment" and "I was returning to correct the lapse in judgment but was too late". He said if he had experienced a momentary lapse in judgment when driving the vehicle, he would have been covered under the policy.

The Panel accepted his submission and stated "a motor vehicle insurance policy is intended to cover the policyholder against lapses in judgment and, as the insurance company had produced no evidence he acted recklessly, it was obliged to meet the claim.

Another common factual scenario relevant to this issue is when vehicles break down and are left at the side of the roadway. The Panel has issued many determinations to the effect that if a loss occurred after a vehicle was left on the side of the road for a short period of time before it could be towed away or otherwise attended to, the driver has not behaved recklessly. However, if the vehicle has been left for a week or perhaps several days, e.g. while the policyholder went away on a holiday or given priority to social commitments, their conduct may be classed as reckless. The factors that are considered in these circumstances are the value of the vehicle, the remoteness or otherwise of the location, the availability of the means to remove the vehicle e.g. if a tow truck could have been called, and the difficulties associated in the process of removing the vehicle.

Travel insurance – taking reasonable care?

However, it appears to me that the degree of errant behaviour permitted with a motor vehicle policy is much greater than that permitted with other forms of insurance, particularly travel insurance. When I first commenced at IOS, most travel policies contained provisions requiring the policyholder to take reasonable care in the context of lost or stolen luggage. As a significant number of claims were being determined in favour of policyholders if they had been careless with their luggage but not reckless, the insurance industry introduced a much higher threshold before lost luggage claims were paid. Policy exclusions now began to appear in supporting denial of claims

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or may specifically exclude liability if the conduct giving rise to the claim is "reckless". As stated above, the courts have considered these terms in the light of the commercial purpose of the policy which is to provide protection against unforeseen damage including damage caused by driver error and negligence. The concept of reading down an exclusion clause was discussed in the case of *Fraser v Furman (Productions) Ltd* [1967] 1WLR 898 where the court held that a reasonable care provision policy had to be read down and considered in the context of whether

petrol, he had been listening to the radio. After filling the vehicle with petrol, he was intent on paying for the petrol and leaving, as the service station had become busy. He thus overlooked the fact that the keys were still in the ignition. He said he had taken approximately five paces towards the shop when he remembered the keys and turned back.

He then had his attention drawn to the fact that someone was stealing his vehicle and he attempted to chase the vehicle but to no avail. He said the whole incident took

for stolen luggage if the luggage had been "left unattended", a term which had been judicially defined to require the policyholder to place the luggage in a position where it could be seen, or was at least capable of being seen.

This meant that if luggage was left at a railway station or airport for a minute or so while the policyholder checked the next flight or the next train, the luggage was adjudged as having been stolen in circumstances where it was left unattended and the claim was not paid.

However, the industry was still not satisfied with the number of claims they were losing because the policyholder could establish the goods were not unattended, and special definitions of the term "unattended" were inserted into the policy so the words were artificially

54(5)(b) of the Insurance Contracts Act, which prevents an insurer from relying on a policy term with which it is impossible for the insured to comply. This occurred in a dispute when the insured, who was part of a tour, was directed by the tour operator to leave her luggage in the corridor outside her room and after doing so, discovered it was stolen shortly thereafter. The Panel considered the unattended luggage exclusion ought not to apply as it was impossible for the insured to comply with it in the circumstances.

In terms of householder's insurance, many policies will also set out standards or conduct for the insured persons. In my experience, many policies will exclude cover if a home occupier has left the home without activating the alarm, where smoke alarms are not provided, or does

"The legislative monster in the form of section 54 may snatch defeat from the jaws of victory."

defined to mean that luggage was unattended if it was left "in the position where the insured was unable to prevent it from being stolen" which meant the luggage had to be virtually strapped to the policyholder's body, or the act of the luggage being stolen of itself satisfied the test.

In the light of those developments, claims were denied when the luggage was left outside a toilet cubicle, because it would not fit inside, goods were stolen from luggage because the insured fell asleep during an overnight train journey, or where the bags were removed from under the table at a restaurant when the policyholder was borrowing the salt shaker from the occupant of the next table.

The Panel found some of the policy exclusions were so draconian that it was impossible in some circumstances for the policyholder to comply with their obligations under the policy. In those circumstances the Panel invoked the provisions of section

not fit deadlocks to the door. There is usually a standard of reasonable care imposed in maintaining the safety of a property e.g. not lighting a fire in dangerous circumstances on a rural property or leaving goods unprotected e.g. failing to lock buildings where machinery is kept, and with respect to occupancy provisions.

Many motorcycle policies also require a high standard of care in comparison with motor vehicle policies, and require the motorcycle to be padlocked or chained to a fixed object when not in use. The Panel has also had to consider numerous claims where policyholders have had their claims denied when the motorcycle was stolen by a prospective purchaser who had provided bogus identity information or in some circumstances, had left goods for security of sufficient value to reassure the policyholder, but of insufficient value to deter the theft.

In the case where the policy terms simply provided a requirement to take reasonable care, the test of recklessness prevailed to protect the insured but in instances where the policies specifically excluded cover when the vehicle is stolen in the course of a test ride, the Panel



decided the specific policy provision overrode the reasonable care/reckless requirement in the same way as occurred in the case of the "unattended luggage" exclusion.

Of course, all these requirements are subject to the legal monster lurking in the depths, namely section 54 of the Act which provides that if the act giving rise to the claim occurred after the policy is entered into (which applies to all the above scenarios) the insurer cannot deny the claim unless it can show it has been prejudiced by non-compliance with the policy term (sub-section (1)), or the act giving rise to the claim was capable of causing or contributing to the loss, (sub-section (2)). In the majority of instances, it is self-evident that failing to take proper precautions to protect property is capable of causing or contributing to the loss or prejudicing the insurer, but in a variety of circumstances, this might be more difficult e.g. where the house was not fully secured but it was burgled by professional thieves equipped with jemmyes and who had robbed every other house in the street, or the motorcycle was stolen by specialist bike thieves equipped with bolt cutters or in the case of a motor vehicle not locked (or even if it were) was stolen by the use of a tow truck.

And in summary ...

The important points I wish to make are:

- ❑ There is a vast difference between the degree of carelessness, negligence or recklessness permitted in the

range of general insurance policies, and particularly in the context of motor vehicle insurance, acts of carelessness are not only tolerated by insurers, but in some instances, used as part of their marketing strategies to invite cover.

- ❑ The degree of delinquent behaviour permitted at law pursuant to the reasonable care test is much greater than when a specific requirement to do something is to be established e.g. the motorcycle test drive scenario, or unattended luggage. In my opinion, the insurance industry would be well advised to set out specific parameters in policy drafting so as to be less reliant on the vagaries of judicial interpretation of the term "reasonable care".
- ❑ Notwithstanding the specifics of the factual inquiry and the likelihood of a finding the policy term has been breached, the legislative monster in the form of section 54 may snatch defeat from the jaws of victory unless it can be established the breach of the policy term prejudiced the member, was capable of causing or contributing to the loss, or in the case of the luggage left in the corridor, whether or not it was impossible to perform the policy condition.

In the meantime, the reckless insured can live in hope. **II**