

Fundamental Legal Concepts

for Life Actuaries
Workshop D03

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Topics to be covered

1. Essential Contract Law
2. UTCC, TCF and PRE
3. Basics of Company Law
4. Contracting Parties
5. Topical Issues
 - Distribution and Administration Agreements
 - Anti-age discrimination

1. Essential Contract Law

Contract formation

For a contract to be formed there must be:

- Offer
- Acceptance
- Consideration
- Intention to create legal relations

Electronic formation

- Signature free online contracts
 - Building satisfactory online process
 - Evidencing policyholder involvement/consent
 - Ongoing administration

- Third party involvement in applications
 - Origo declaration/confirmation schedule

Electronic formation

- Product-specific problems
 - Life assurance: non-disclosure
 - Investment bonds: risk of fraud

- Other issues
 - Life of Another – insurable interest
 - Trusts
 - ABI consulting on new policy for telephone/internet applications

What are the terms of the contract?

- Written terms
- Oral terms
- Express or implied?
- Non-contractual documentation?
- Incorporation

What do the terms mean?

- The terms should not be unfair and should clearly and unambiguously set out the rights and obligations of the parties.

Potential pitfalls

- Rules of contractual interpretation
- Impact of non-contractual communications
- Unfair contract terms, TCF, PRE

Rules of contractual interpretation

- "Four corners of the contract", implied terms, ambiguity
- Example:
 - Joint life second death policy literature states:
"No MVR shall be applicable on death".

Non-contractual documentation

- Key features document: "No MVR shall be applicable if benefits are taken at the normal retirement date".
- Terms and conditions: "No MVR shall be applicable if benefits are taken at the normal retirement age except in relation to:
 - any single premium applied within 5 years of normal retirement age; and
 - all regular premiums, if the policy commences within 5 years of normal retirement age."

Non-contractual documentation

- Steria v Hutchison [2005] EWHC 2993 (Ch)
- Conclusion
 - Contractual terms – *a question of proof*

2. UTCC, TCF and PRE

Unfair Terms in Consumer Contracts Regulations 1999 (“UTCC”)

- Originally effective from 1 July 1995 (under EU Directive):
Reg 5(1): “A contractual term which has not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties’ rights and obligations arising under the contract, to the detriment of the consumer.”
- UTCC states that an unfair term shall not be binding on the **consumer**.

Schedule 2 UTCC:

- Contains non-exhaustive list of unfair terms
- The FSA’s main concerns arising from Schedule 2 are:
 - Inequality of bargaining power
 - Open-ended discretions
 - Variation clauses
 - Penalties/conditions on withdrawal
 - Surrender charges
 - Reviewable premiums

Treating Customers Fairly (TCF)

- Principle 6 (PRIN 2.1.1) of FSA Handbook:
"A firm must pay due regard to the interests of its customers and treat them fairly."
- **Principle-based** regulation
- FSA will take into account UTCC in considering fairness under Principle 6.

TCF consumer outcomes

FSA report on Treating Customers Fairly (July 2006)

1. Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture
2. Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly
3. Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale

TCF consumer outcomes

4. Any advice to consumers is suitable and takes account of their circumstances
5. Consumers are provided with products that perform as firms have led them to expect, and the associated service is both of an acceptable standard and as they have been led to expect
6. Consumers do not face unreasonable post-sale barriers imposed by firms to change product, switch provider, submit a claim or make a complaint

Policyholders' reasonable expectations (PRE)

- Equitable Life – four factors shape PRE:
 - Terms of the contract
 - Statements made by insurer to policyholder
 - Past practice
 - Industry practice

Policyholders' reasonable expectations

- Manage expectations whilst enabling flexibility.
- Clear statements, transparency and disclosure.

- *TCF encompasses existing PRE wisdom.*

Role of Financial Ombudsman Service

- IFG Financial Services Limited v FOS (2005) QBD
HELD: "Ombudsman was free to make an award that differed from that which a court applying the law would make, provided he concluded that the award he wished to make was fair and reasonable in all circumstances of the case and provided he had taken into account the matters identified in Rule 3.8.1(2) of the Scheme"

Rule 3.8.1(2)

"In considering what is fair and reasonable in all the circumstances of the case the Ombudsman will take into account the relevant law, regulations, regulators' rules and guidance and standards, relevant codes of practice and, where appropriate, what he considers to have been good industry practice at the relevant time.

Impact

- UTCC, TCF and PRE are inextricably linked
- The FSA is a qualifying body under UTCC
- FSA "pre-emptive strikes" - undertakings
- TCF agenda widens scope of UTCC and PRE

Conclusion

- *New terms must be **drafted** appropriately*
 - Clear, concise and fair.
- *Existing terms must be **operated** appropriately*
 - Terms and conditions should be reviewed to pre-empt FSA review, avoid undertakings and ensure powers, rights and discretions are fairly applied.
- ***Inter-connectedness** - TCF should be factored into all aspects of a firm's business*

3. Basics of Company Law

The Company

- A separate legal entity
- Limited liability i.e. if a company is put into liquidation, the people who own the company will only be required to pay what they have already paid or agreed to pay towards settling its debts.
- Memorandum of Association - lays down the objects and powers of a registered company.
- Articles of Association - contain the internal regulations covering procedure, shares, meetings, directors and other administrative issues

The Directors

- Officers of the Company – day-to-day running
- Directors' resolutions – board minutes or written resolutions
- Must manage the company's affairs in accordance with its Memorandum/Articles and the law.
- Directors' duties:
 - Act in good faith and in the company's best interests
 - Minimum standard – act with reasonable care and attention
 - Supplemented if additional skills - must perform duties to the standards which could reasonably be expected of someone with your knowledge and experience

The Shareholders

- Owners of the Company
- Rights depends on nature/proportion of shareholding
- Ordinary resolutions – passed by simple majority e.g. to authorise allotment of shares
- Special resolutions – passed by three quarters in value of shares e.g. to alter Articles, change objects
- Minority shareholders – certain rights

Potential Conflicts

- Shareholder who is also a director has “two hats”
- Directors’ duty to act in the best interests of the “company” – unclear what constitutes the company but probably includes shareholders
- Must also take into account duties to policyholders. Should reach a fair balance between interests of policyholders and shareholders
- No requirement to override shareholder interests

4. Contracting Parties

Are the right parties bound by the contract?

- Paying out on investment contracts
 - Partnerships and companies
- General commercial agreements
 - Subsidiaries/guarantors

“We, ABC Subsidiary Ltd, will indemnify you in respect of any loss suffered as a result of our negligence.”

Confidentiality Agreements

“All of Company 2’s information received by us from Company 2 and marked “Confidential” shall be subject to the terms of this agreement.”

Distribution Agreements

“X Bank plc shall distribute Company 2’s products”.

Authority to contract

- Actual authority
- Ostensible authority

Intra-group contracts

- Actuarial involvement – ensure it is clear **who** you are acting for.
- SUP 4.5.3:
“An actuary appointed under this chapter must take reasonable steps to satisfy himself that he is free from bias, or from any conflict of interest from which bias may reasonably be inferred. He must take appropriate action where this is not the case.”

5. Topical Issues

Distribution agreements

- Impact of TCF: consider customer interests
- Know the distributor’s client base
- No need to “police” the distributor’s compliance BUT obligation to provide information
- One of 10 issues reviewed in ARROW visits.

Administration agreements

- VAT exemptions
 - “Back-office” services - Accenture case
 - OEICs and AUTs – Abbey case
 - Retain certain services intra-group?
 - Specify liability for VAT?

Anti-age discrimination

- Employment Equality (Age) Regulations 2006
 - Employers cannot require retirement at 65
 - Prevents direct/indirect age discrimination
 - "Objective justification" for providing different benefits

- Discrimination remedy – "level up" or "level down" benefits?
- Alter scheme rules?
- Remains uncertain

- **Cadman v HSE [2004] EWCA (Civ) 1317**
 - Lessons from a sex discrimination case

Financial Ombudsman annual review

- Closed funds – conflict of interest between policyholders
 - Role of FSA: general overview of funds
 - Role of FOS: consider individual cases
- Reviewable whole of life policies

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