Insuring success - the overhaul of Switzerland's Insurance Contract Act

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With more money spent per head on insurance premiums in Switzerland than any other country, the first overhaul of Switzerland's Insurance Contract Act in 100 years is causing much discussion, say Christian Lang and Zsuzsanna Kunszt

Switzerland is not only known for its cheese, chocolate and (mistakenly) for the invention of the cuckoo clock, but also for its banks and insurance companies. The country is home to some of the world's largest insurance carriers (e.g. Zurich, Swiss Re, Swiss Life), and at $6,634 (£4,294) per person, more money was spent on insurance premiums in 2010 than in any other country. In the light of this long-lasting insurance tradition it might come as a surprise that the Swiss Federal Act on the Insurance Contract (Insurance Contract Act, ICA) is about to undergo its first total overhaul in more than 100 years. Although the bill was only sent to parliament in September 2011, it has already spurred a lively discussion in the market.

Although the revision of the ICA is predominantly a Swiss domestic issue, the impact of the revision may well reach far beyond Switzerland's borders. More than a third of the 151 insurance carriers currently licensed to conduct direct insurance business in Switzerland are branch offices of foreign insurers operating in or from Switzerland. The total premium income of all licensed direct insurers was CHF 53.7 billion in 2010 (£36.5bn). A substantial part of this business is in-bound and out-bound international business which often is governed by Swiss law.

After an Expert Commission installed by the Swiss federal government had submitted its draft for a new ICA in 2006, the government issued a preliminary draft for a new ICA in 2009. Based on comments received from interested parties (academics, the insurance industry, consumer organisations, etc) in a public consultation, the government issued its proposal to the parliament in September 2011. The enactment of the new law is not expected until 1 January 2014 at the earliest. The below comments are based on the government's proposal, which may undergo more or less substantial revisions in parliament's coming debate.

Industrial risks versus consumer risks

For the first time in the history of Swiss insurance law, the government's proposal draws a distinction between insurance for large industrial risks and other contracts. While some enumerated provisions of the law may generally not be amended to the disadvantage of the insured, this rule does not apply to large industrial risks. Therefore, in insurance contracts for large industrial risks, the parties are free to amend or delete any provision of the ICA and thus can – subject to public policy only – freely define the rules to govern their contractual relationship because they are considered to be negotiating at eye level. Additionally, there is unrestricted freedom of contract for credit risk insurance and surety bonds.

The definition of large industrial risks, however, is inconsistent in the new draft. Generally, the European concept of the definition of large risks is followed, ie certain types of risk or two of three thresholds for the policyholder (total assets of €6.2m (£5.1m), turnover of €12.8m (£10.6m), 250 full time employees) must be given to consider a risk a "large risk". Unfortunately, the new ICA provides for two different sets of thresholds, the European one

for international contracts and a separate, higher threshold for domestic contracts. This does unnecessarily complicate matters and there is hope that the parliament will sort out these differences.

Pre-contractual information and disclosure

While under the current ICA it is sufficient for the insurer to provide the insured with the general terms and conditions of the insurance policy, the new ICA provides that the insured needs to be given sufficient time to study and understand the terms of the policy before the insurance contract is concluded. The information needs to be given to the insured in writing and in an easy to understand manner. The law does not define what "sufficient" time or "easy to understand manner" shall mean. It remains to be seen whether the parliament will introduce more specific rules or leave it to the courts to develop a pertaining practice.

With regard to the disclosure duties of the insured vis-a-vis the insurer, the general rule of the current ICA that the prospective insured must disclose to the insurer all significant risk factors about which the insurer has asked in writing has been adopted in the new ICA. However, while under the current law the risk factors which the insurer addresses by written, precise and unambiguous questions are assumed to be significant, this assumption has been struck from the new law and it will be the insurer's onus of proof to demonstrate that a risk factor is significant.

Unless the parties have amended the respective provision in the new ICA, in connection with large industrial risks all information on material risk factors provided by the prospective insured is considered relevant, irrespective of whether or not the insurer has asked a pertaining question. However, the new law still allows the proposer to remain silent regarding a material risk factor as long as he is not asked about it by the insurer. Thus, there is still no duty of voluntary disclosure of material risk factors by the prospective insured, neither under the current nor under the proposed new ICA.

Admissibility of conditions precedent

Recent case law has confirmed that the current ICA generally allows for strict conditions precedent, ie conditions, the violation of which can lead to a loss of insurance benefits even in the absence of prejudice to insurers. Such strict provisions would no longer be admissible under the new ICA (again, except in connection with large industrial risks where full freedom of contract exists). Under the new ICA, the insurer can only deny coverage if a condition was intentionally breached by the insured and if such breach had an impact on the occurrence and/or the size of the loss. In cases of non-intentional breaches, the insurer may reduce insurance benefits according to the degree of fault attributable to the insured.

Right of direct action of the damaged party against the tortfeasor's insurance

A feature common to many continental European jurisdictions is about to be introduced into Swiss law with the new ICA: the right of the damaged party to bring direct claims against the tortfeasor's liability insurer (so-called 'action directe'). Although the majority of the liability claims to which the new law would apply are directly handled by the tortfeasor's liability insurer already today, some fear a dramatic re-interpretation of liability insurance if the tortfeasor is taken out of the picture and coverage issues were to be litigated with a claimant which is not a party to the insurance contract.

It is difficult to predict what the consequences of this new action will be. However, academics and practitioners seem to agree that the introduction of the action directe into Swiss substantial law could increase the risk for Swiss insurers to find themselves sued in a court abroad.

Disclosure of brokerage fees

In today's Swiss insurance market the broker is paid by the insurer. As the broker acts as the representative of the insured, this inevitably leads to conflicts of interest. Although the new draft ICA does not change this system per se, it introduces a broad information duty of the broker vis-a-vis the insured about all brokerage fees and other commissions. This is intended to ensure that the insured can assess the extent of the potential conflict of interest and take it into account when choosing a product. The Expert Commission's draft and the government's preliminary draft of 2009 contained a prohibition of any payments of brokerage commissions by insurers, which was vigorously fought by brokers and successfully pushed out of the government's proposal of September 2011.

Backwards insurance / statute of limitations

Finally, two smaller but nevertheless significant changes are worthwhile mentioning. First, the strict mandatory rule in the current ICA that the insurance contract is null and void if at the time of its conclusion the insured event had already occurred is abolished under the new draft ICA. Under the new law, the parties are free to conclude backwards insurance. Such a contract only is null and void in cases where the insured alone knew or should have known that the insured event already occurred.
Second, the current short two year limitation period for claims out of insurance contracts shall be extended to ten years, which is the limitation period applicable under general contract law. Claims for payment of premiums shall be time barred after five years.

Outlook

The government's draft for a new ICA takes into account the developments in the insurance industry, particularly in the field of consumer protection. Although not all provisions which have proven inadequate in a commercial setting have been eliminated, the new law at least allows for full freedom of contract in connection with large industrial risks, which is a very positive development. As in the current law, the new ICA will not apply to reinsurance contracts; they will continue to be governed by general contract law and the customs and trades of reinsurance business.

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