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C E N T R E D E D R O I T D E S O B L I G A T I O N S

Observations on the Draft Czech law on Insurance Contract

Note n° 3

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OBSERVATIONS

ON THE DRAFT CZECH LAW ON INSURANCE CONTRACT

Note n° 3

Introduction

Our preceding Notes n° 1 (August 1, 1994) and 2 (December 9, 1994) commented on the first version of a draft law "On Insurance Policy", that was also orally discussed during meetings held in Prague on September 12-14, 1994.

A new draft has been prepared, now more adequately entitled "Law on Insurance Contract". We have already given some oral comments on the whole of Chapter I (Art. 1-21), and on the beginning of Chapter 2 (Art. 1-7) during meetings held in Prague on March 13-15, 1995.

The following observations summarize those comments already submitted, taking into consideration the answers that were given, and proceed to analyze the following provisions of Chapter 2 of the draft.

A general comment is that many provisions are extremely long and would gain by being subdivided. It was said in Prague that it would be the case.

Chapter One

Fundamental Provisions

1. Insurance contract and purpose of insurance

- We have difficulty to understand the initial formula, according to which the insurance contract *"gives insurance its form"*, even after

the explanations that were given in Prague. Perhaps the formula is clearer in the original Czech version.

- In the following definition the formula *"... a settlement the extent of which has been agreed upon ..."* is satisfactory for personal insurance, but not for property and liability, where the extent of the settlement depends in principle on the amount of the actual loss, not on a previous agreement. We were told the provision meant to refer to the scope of the coverage (the risks insured), which is effectively the object of an agreement; in that case the formula should not refer to the extent of the *"settlement"*; perhaps it is again a problem of translation.

- The following paragraph ("A special decree ..."), we were told, refers to compulsory insurance (workmen's compensation, motor TPL), where temporarily, for historical reasons, insurance will still not be regulated by contract. It was repeated that it would be advisable, in the future, to submit compulsory insurance to a contractual regime as well as voluntary insurance.

- The *"insurance event"* is described as a *"fortuitous circumstance"*. Actually it is not always the case; in liability insurance, for instance, it is the essence of the insured event not to be fortuitous. *"Uncertain"* would be a more adequate term. It was explained that *"fortuitous'* should be kept because the word has been traditionally used, but the necessary explanations will be given.

- a) and e) Another discussion took place about the conflict between the necessity to have rules giving the desired safety about the moment a contract is concluded (hence the requirements of a written form or of payment of the first premium) and the need to permit the immediate purchase of insurance coverage (by phone, E-mail, etc...) in certain circumstances. It was said that the proposed rules in the draft did not deviate from the principles stated in the Civil code §§ 40-4 and 409. Perhaps the draft could also permit general conditions to provide special rules for such cases. More thought will be given to the problems involved. A suggestion was to allow the oral conclusion of an insurance contract in case of emergency, subject to a written confirmation in a very short time. There is already the possibility of preliminary coverage organized in Art. 10, and discussed below, but it also requires the written form.

- b) Add the duration of the contract ?

- c) Material control of general conditions is probably a good thing at the present stage of the Czech insurance market. The rule according to which deviations from the approved conditions would be only allowed to the benefit of the insured should also be stated about the law itself. We were told it would be the case in a provision still to be drafted.

- d) The rule is only adequate for situations where the insurance *"proposal"* amounts to an *"offer"*, which is not always the case. Very often, for instance, a proposal form filled by the future policyholder still does not mention the amount of the premium. A real offer can then only come at the next step, when the insurer submits the policy for signature by the other party. The rule should distinguish according to whether the *"proposal"* already contains all the necessary elements of the contract, or not.

2. Types and branches of insurance

- More logically, liability insurance [(ac) and (bc)] should come directly after property insurance [(aa) and (ba)].

- The formula ending (ab) (*"... or linked with other insured event"*) is not very clear. Medical expenses insurance was mentioned, but it rather belongs to property insurance (actually to a special variety of it) (see below, Part Two, Section Four, Art. 2). We suggest to characterize personal insurance by referring to risks linked to the duration of human life or the physical integrity of the insured. .

3. Insurable risk

This provision still has to be drafted. A discussion took place, concerning the respective notions of risk and interest. We consider *"risk"* as the uncertain event against which insurance is taken (fire, theft, liability, death, etc...), while the requirement of an *"insurable interest"* means that insurance can only be validly taken against losses that would affect the insured (I can insure *my* house, but not the Prague Town-hall). An *"insurable risk"* is a risk that threatens an insurable interest (fire in connection to my house).

A definition was proposed by Mrs. Skopova : the *"insurance risk"* would be *"the probability that an event will occur which will cause a loss or a need of certain financial resources"*. We feel this definition has much merit. We would replace *"probability"* by *"possibility"*, as one cannot limit insurance to cases where the

occurrence of the insured event is *"probable"* (insurers would never survive !). - but of course there is always a certain degree of probability, which the insurer will appreciate in each case. Also, we think the definition of an *"insurable"* risk should mention that the loss or need for financial resources is suffered by the insured. A risk is not insurable if its occurrence would harm a person who would not be insured.

4. Parties to insurance

a) It was said in Prague that the term *"parties"* is perhaps too narrow to extend to all persons deriving rights or duties from insurance. Technically, the *"parties"* to an insurance contract are the insurer, the policyholder, the insured and perhaps also the beneficiary (provided the very vague definition given in Art. 4 e is replaced by the other, and more accurate, definition given below by Art. 7), but not other people to whom the law gives some rights against the insurer or on the insurance indemnity, such as third party victims or creditors (it is clear, in that respect, that when the insurance contract, according to Art. 1 b, mentions the parties to the contract, it will not mention those categories of persons, whose identity is anyway unknown at the time of conclusion).

We were told *"parties"* in Art. 4 meant *"participants"*, a broader concept. We wonder about the utility of introducing such a concept, with the risk of creating confusion with the traditional concept of "parties", the more so as the following paragraphs b to e are only concerned with real *"parties"* (subject to reviewing the definition of *"beneficiary"* as was just said). Our suggestion would be to delete the last part of paragraph a (" ... *and any physical person ... from insurance*").

5. Intermediaries

- a) Is it necessary to state that the parties are entitled to act through intermediaries ? Is it not in principle always the case in contract law ?

- b) The rule may be adequate for insurance agents, but much less so for insurance brokers (who normally do not have a limited territory). We were told the present Art. 5 does not distinguish for the moment, that different rules for agents and brokers will be established at a later stage. We wonder if a complete set of rules, making the necessary distinctions, would not be worth introducing

from the start, in order to avoid the problems which a general regulation, necessarily inadequate, would create in the meantime.

- c) and d) It is not usual, in many Western countries, that intermediaries have a mandate to conclude insurance contracts. They bring the parties together, transmit proposals and other documents, etc..., but the insured and the future policyholder do not normally delegate the right to conclude.

Paragraph d), anyway, has to be conciliated with para c), as d) seems to imply that a special authorization is necessary to entitle the intermediary to conclude the contract. This last rule is more appropriate, but then we have strong reservations about the other part of d) according to which an authorization to conclude implies an authorization to modify or cancel the contract. This would give the intermediary a discretionary control over the contract the parties certainly do not wish to extend. A special authorization should be equally needed for modifications and cancellations (is it even necessary to state such an obvious rule ?).

- e) There may be a translation problem with the ending of that paragraph (*"they were aware ... of it through their own fault"* ???). It was said in Prague the meaning was that third parties had an obligation to verify the intermediary's authority.

- f) The language of the first sentence could apply to the situation when the intermediary acting on the policyholder's behalf does not reveal the falseness of some information to the insurer. Our comment was then that the remedy (the insurer would not be bound) was not harmonized with the rules given below in Art. 14, putting the policyholder in a worse position when the contract was concluded through an intermediary. We were answered Art. 5 f covered the opposite case when it was the policyholder who was deceived by the intermediary, in which case a different rule would be quite acceptable. It would then be necessary to make the text clearer, in order to be sure about the specific situation covered.

- The second sentence of paragraph f is a very different rule, that should be stated under a separate paragraph.

6. <u>The insurance policy</u>

- After some discussion we discovered that practices were different in the Czech Republic than in Western countries. The "policy" that the policyholder receives is not the full insurance contract, but only

a summary of it, signed only by the insurer, a document that will be required to be indemnified in case of loss. The insured does not receive a complete copy of the contract he has signed. The only copy that exists is kept by the insurer. We were told that was "simpler" and "safer".

We had the occasion to express rather strong reservations about this practice. Each party to a contract has the right to be treated on an equal footing. The policyholder, like any contractual party, should have an original copy of the full contractual documents, signed by the other party. This seems to be a basic requirement of consumer protection, and of contractual fairness in general.

Along that line, the insurance "policy" should be nothing else than the written evidence of the whole contract, including particular and general conditions, and later amendments if any.

- b) The practice of endorsable policies is useful in certain sectors, but it has to be conciliated with the requirement of an insurable interest in order to be covered. A solution could be to create a rebuttable presumption of interest for the person to whom the policy has been endorsed.

7. Insurance for the benefit of a third party

- The draft has the great merit to clearly distinguish between *"Insurance for the benefit of a third party"* (Art. 7) and *"Insurance of a third party's risk"* (Art. 8). The work *"risk"* , in those two provisions, should be understood in connection to what was said above concerning Art. 3, and the proposed definition of the *"insurable risk"* discussed then.

- a) should make it clearer that even though the beneficiary can still accept when exercising the rights derived from the insured event, he can also accept at any time before.

- b), c) and d) allow the policyholder to transfer or to pledge the rights deriving from the contract to another person, or to designate another beneficiary, even though a beneficiary has already accepted the benefit. The law can certainly contain such a rule. We were even told the second sentence of d) would be deleted, to give more liberty to the policyholder. In some other countries, however, it is no longer possible to affect the beneficiary's rights after he has accepted (except through the application of some rules of donation or family law).

It should be made clearer, in d), that the "insured" is here the person whose life is insured.

8. Insurance of a third party's risk

- a) Problems of translation cause difficulties of understanding (*"dispose"* ?). The meaning seems to be that the insured has all the rights but cannot in principle transfer them without the policyholder's consent.

- b) was also difficult to understand. It was explained the policyholder retained some rights, such as to "investigate" (?); the formula, however, is extremely broad, and could lead to serious conflicts between the policyholder and the insured. We were told the second sentence was meant to apply to situations such as that, frequent in fire insurance in the Czech Republic, where the insurance is concluded by the tenant on behalf of the owner, but the owner lets the indemnity to be paid to the tenant who will himself take care of the repairs.

- c) again called for explanations. We were told this applied for instance to the case where a tenant would also conclude an insurance contract on behalf of the owner, but to the benefit of the tenant's creditor. This could be a practical arrangement, if we understood well, in cases when the owner was objectively responsible of the damage (perhaps we misunderstood this, which is certainly not clear to us at the time we write the present commentaries).

- d) seems to provide that in case the policyholder dies or disappears (legal entity), the insured takes over his contractual rights and obligations towards the insurer. We wondered why in cases the policyholder is a physical person and dies, the rights and obligations are not transferred to his heirs. It was answered it could take time to find out who the heirs are. On the other hand, we feel that the suggested rule could create difficulties as the insured may not have any contact with the policyholder and thus ignore his death (e.g. in transport insurance, where there the coverage can be transferred to several successive insured), and on the other hand the insurer may also have difficulty to identify the insured at the time the policyholder dies (also in similar situations such as transport insurance).

- A problem the proposed Art. 8 does not cover is that of the extent defenses the insurer may have against the policyholder can be opposed to the insured. For instance, can the insurer refuse to indemnify the insured because the policyholder failed to pay the premium ? This has been the subject of some debate in other countries, and there should be a legal solution. That solution may already be given by the general rules of civil law concerning contracts to the benefit of third parties. Otherwise it should be advisable to include a rule in Art. 8. During discussions held in Prague, it was agreed the better solution is that the insurer can oppose such exceptions to the insured.

9. Combined insurance

This provision has been replaced by the provision on co-insurance, analyzed later (Ch. 2, Part I, art. 7a).

10. Preliminary coverage

- This provision would gain by being located in connection to the provisions concerning conclusion of the contract in Art. 1.

- a) *"... before the contract has been concluded..."* could be replaced by *"... before the final contract has been concluded..."*, as preliminary coverage is itself granted on the basis of a preliminary contract.

- e) *"Inception"* should be clarified : entry into force ? We were told it referred to the date indicated on the cover note.

11. The premium

- The system in d), we were explained, is that the payment is effective when it is received, but then, the moment it is supposed to have taken place is that when the money was sent from a post office or deducted from a bank account.

The moment the insurer has "received" the payment should be made more precise : it is when the insurer's bank has received the transfer, or when the insurer's account has been credited ? The latter solution is more simple to verify, but it makes the policyholder bear the risk of the insurer's bank getting insolvent.

- e) The formula *"unless it is a non-capitalizing, lump-sum premium"* could not be explained. It will be verified.

- f) *"otherwise"* should be replaced by *"so"*. The rule, we were told, corresponds to a growing practice in the Czech Republic; it reflects humanitarian preoccupation. While this is of course very commendable, one should wonder about the compatibility of such a generosity with the commercial character of an insurance company, its obligations towards its shareholders, and mainly its obligations towards each of the insured to stay solvent.

- g) This rule will be discussed below, together with Art. 18 l.

- i) This provision is supposed to apply to risk modifications, also briefly alluded to in Art. 18 n. The problem receives the much more elaborate treatment it deserves in Chapter Two, Part One, Section One, art. 6 b-f. below. Art. 11 i should be deleted.

12. Rights and duties of the policyholder, the insured and the beneficiary.

- b) It was said that the words *"... unless a legal provision stipulates otherwise"* would be added.

- c) is a clear example of a provision that will have to be subdivided, and its contents arranged more logically. Very different obligations are put together in the same paragraph.

The first obligation of the policyholder is *"to answer truthfully and completely to all written inquiries from the insurer"*. This is a very important rule, as it seems to adopt the "questionnaire system" for risk description - a progressive solution. The sanction seems to be stated in Art. 14 a : see below. If this interpretation is right, it would be advisable to make the link between the obligation and its sanction more apparent.

Another obligation should be stated or recalled here, that of notifying risk increases : see above, our commentary of Art. 11 i; provisions on risk modifications to be reintroduced.

The second obligation provided by c) is to *"notify the insurer in writing and without unnecessary delay that an insured event has occurred, give a true explanation of the origin and extent of its consequences"*. The obligation expressed somewhat further in the provision, to *"present the required documents which the insurer*

may request"., should be more closely linked to the notification requirement. The sanction seems to be stated in Art. 14 b : see below.

A third duty is *"to meet the obligations which have been agreed upon in the insurance contract and the duties derived from legal provisions the aim of which is to prevent the consequences of an insured event from increasing"*. This is another basic obligation of the insured in case of a loss, which should be stated before those mentioned in the preceding paragraph, as it comes chronologically earlier. Here too, the sanction seems to be stated in Art. 14 b : see below.

Finally, c) obliges the policyholder to *"comply with any other duties stipulate in the insurance terms and conditions or agreed to in the insurance contract"*. The sanctions are also probably to be found in one of the provisions of Art. 14, depending on the circumstances.

13. Rights and duties of the insurer

- c) and d) It is quite commendable to provide for a quick settlement once the insurer has gathered all necessary elements, and to oblige the insurer to make an advance payment if the investigation requires more than one month, which will very often be the case, especially in liability insurance.

What a *"reasonable"* advance could however be the case of much argument between the parties. It is true it is difficult to find a more precise solution; it could be added that at least the undisputed part of the settlement, if any, must be paid.

On the other hand, we suggested that the law should allow the insurer not to pay any advances if there are serious reasons to suspect the loss was fraudulent.

14. Consequences of infringement of duties

- Even though we have suggested above to make links between the different obligations and their respective sanctions more apparent, the idea of regrouping all remedies in one provision is very attractive.

However there are apparent gaps. Failure to pay the premium is dealt with in Art. 18 1 (see below). Art. 14 does not deal with the

insurer's obligations. If this provision cannot deal with all possible infringements of duties, then its title should be amended, or some sort of reference should be made here to the other relevant provisions.

Art. 14 should also clarify to what extent the general remedies of contract law, as provided in the Civil code, are still applicable when this law organizes a specific remedy.

- Another merit of Art.14 is that it provides for reasonable and balanced remedies, thus preventing insurance contracts from stipulating disproportionate sanctions (e.g. loss of coverage for any slight delay in notifying the occurrence of the insured event). This is in line with the modern developments of consumer protection.

- a) seems to apply mainly to the obligation to describe the risk when concluding the contract (see above, Art. 12 c, beginning) and to the obligation to notify risk increases (see above, Art. 11 i, and below, Ch. Two, Part One, Sect. One, Art. 6 b-f).

- b) can apply to the obligations to attempt to minimize the consequences of the occurrence of the insured event, and to notify it rapidly, providing the insurer with all the necessary information (see above, other parts of Art. 12 c), but also to all behaviors of the insured, contrary to legal or contractual duties, that contributed to bring the insured event.

The settlement may be decreased *"in proportion to the part of the policyholder's or insured's fault"*. Another possible criterion, probably easier to manipulate, is to reduce the settlement up to the amount of the loss the infringement caused to the insurer.

- c) The possibility of a contrary agreement should be deleted. This provision legally determines the rights of the third party victim, and it should not be possible to modify them by private agreement between the insurer and the policyholder.

15. <u>The mortgage right</u>

- a) About the distinction between insurance contract and insurance policy, see above, concerning Art. 6.

We were explained in Prague that the criteria to decide when an insurance contract serves as a *"security"* will have to be determined, as special rules apply to *"securities"* in Czech law.

- b) and c) *"... and only if ..."* has to be replaced by *"provided"*.

- Art. 15 will have to be coordinated with Art. 8 b of Chapter 2, Part I, Section 1.

16. Periodization, period covered by the insurance assessment of time.

- c) This special time-limit for claims only concerns claims against the insurer for settlement of the loss. In other countries, there is a special time-limit for all sorts of claims deriving from an insurance contract. We were told this was intentional. Claims other than those for settlement of the loss are subject to the general limitation periods provided by the Civil code.

- The three years start running one year after the insured event, which is surprising. If the idea is to allow one extra year, why not make it four years, instead of three running after one ? We were told the purpose was to keep the three years' period, the usual duration in Czech law. Is it a sufficient reason to create such a strange system ?

- The limitation period starts running one year *"after the insured event"*. Any period of time can only be calculated if its departure point is very precise, and it is not always the case with the *"insured event"*. In liability insurance, more particularly, discussions are bound to take place to determine whether the insured event is the act that will cause the damage, or the occurrence of the damage, or the claim of the victim, or even the court decision establishing the insured's liability. This is a very delicate question, and distinctions can be made according to the type of claim concerned. Art. 26 of the Belgian Law of 1992 can give models of possible solutions.

- Art. 16 c) does not mention causes of interruption and suspension of the limitation period. Normal civil law causes probably apply, but some countries have special causes in the field of insurance (e.g. interruption through the mere notification of an insured event).

Art. 17. Arbitration proceedings

- We were told this provision will be reviewed after a new statute of arbitration in general has been enacted.

- a) It seems to be very restrictive to accept arbitration only about disputes concerning the amount of the settlement. It is usual, in many countries and in certain types of insurance, that all sorts or disputes are submitted to arbitration. On the other hand, there may be rules that restrict arbitration clauses in *"mass risks"*, as opposed to *"large risks"* concerning enterprises of a certain scale.

The expression *"... a panel of arbitrators selected by the parties ..."* should be made more precise. How many arbitrators ? Always an odd number ? How will it be ensured that no party is in a privileged position to select the arbitrators ? This should not be left to the arbitration agreement, as c) suggests. Probably the expected new law of arbitration in general will deal will such problems.

- e) Such a rule would greatly affect the utility of arbitration. If there is a valid arbitration clause, parties should not be allowed to apply to regular courts. Such courts can only be competent for claims of avoidance against an award that would have been given under irregular conditions or would be contrary to public law, as well as for the *exequatur* procedure in case an award is not voluntarily enforced.

- We have promised to send the special rules for arbitration in insurance applicable to ARIAS procedures (ARIAS has been established by AIDA). It will be done with the submission of this report.

18. Expiry of insurance

- This is an example of a very long provision which could be subdivided.

- Different words are used to characterize the various cases of termination of the contract : *expiration, ending, cancellation, rescission, lapsing*. It is difficult to judge about their respective appropriateness from an English translation, and without being familiar with the categories of Czech Civil law. Care must of course be taken to select the precise terms, and it could be advisable to classify causes of termination by categories.

- a) and c) organize a system which is not completely clear to us. It was said in Prague that *"period"* has two different meanings in those provisions : the total duration of the contract in a), and the time covered by a periodical premium in c); different words should then be used. If we understand right, it can be stipulated that a one-year contract will be tacitly renewed unless notice is sent to the contrary. Longer contracts can be canceled at the end of each "period" (second meaning), with prior notice. If that is so, the solution is in line with the consumer-oriented tendency to prevent long-term contracts with no way out; this approach is very favorable to competition.

- c) It was decided in Prague to delete the "exception" of accident insurance, since it does not belong to life insurance.

- d) This possibility of opting out of the contract in the first three months is also very progressive, but we expressed regret that the period could be shortened in the contract, thus allowing the insurer to reduce it to almost nothing, or to make the possibility unilateral to its lone advantage. It is theoretical to say the insured can always refuse such a clause. In adhesion contracts, a progressive rule that is not mandatory is not progressive any more.

Our suggestion would be to reduce the three months to a shorter period, like two weeks, but not to permit contractual deviations.

- e) is a well-balanced provision.

- h) This will have to be coordinated with the future provisions on credit insurance.

- i) The rule has already been stated in c) above.

- j) Why cannot a contract be rescinded once a settlement has been granted ? It there was an initial cause for nullity it should prevail, and a paid settlement can always be reimbursed if it was based on a void contract. This is especially important when the cause for avoidance is illegality. Supposing someone has insured certain quantities of drugs, pretending it was something else, and received a settlement after they were destroyed by fire, he should certainly not be allowed to keep the indemnity if the insurance contract is avoided when the true nature of the insured objects is discovered.

That was our reaction in Prague. We were then told that for such a case, Czech law does not provide for rescission of the contract, which is simply void by itself. The provision in j) would not then

apply. We suppose that it means the settlement would then have to be reimbursed in the preceding example.

- k) The second sentence is linked to Art. 8 d : see above.

- l) This important provision concerns the consequences of the policyholder's failure to pay the premium : *"If the premium has not been paid, in spite of the insurer's notification in writing, within three months of the date due, the insurance cover expires".*

The merit of this provision is that coverage will not be lost without a prior notification. Even though failure to pay the premium naturally has to be penalized, loss of coverage is the most radical remedy, and it should not take the policyholder by surprise; he should be reminded of his failure, given a last deadline to pay and warned of the consequences otherwise.

This provision, however, calls for a few observations.

First, the mechanism could be made clearer. If the insurer has to give notice within three months, when does termination occur ? At the end of those three months ? Then the insurer could validly give notice one day before the end of those three months, and deprive the policyholder of the protection this provision intends to give him. We suggest to provide that the notification must come within a certain time after the date due, and the termination will take place a certain time after the notification if the premium still is not paid.

However, if the notification has to take place within a certain time, what if the insurer does not send such a notification ? Are we right in assuming that in such a case the insurer could still sue for recovery of the unpaid premium, but could no more terminate the contract ?

More generally, one could imagine that insurers would in many cases prefer to keep the contract, hoping to be paid. Instead of providing for automatic termination if the premium is still unpaid after the insurer's notification, one could say that in such a case the insurer <u>may</u> terminate the contract.

- m) will be deleted : see art. 10 p. 29.

- n) should be deleted (it was deleted in the second version given to us); see above, concerning Art. 11 i, and below concerning Chapter Two, Part One, Section One, art. 6 b-f.

19. Joint ownership by a married couple

No special observations. Some clarification was given to us in Prague.

20. Interruption of insurance cover

- *"Suspension"* would probably be a better translation that *"interruption"*

21. Delivery

- This provision still has to be drafted, but we were told it will specify that a notice will be effective upon reception.

What if the policyholder does not claim a registered letter at the post-office ? The law could provide that a notification is validly made at the last address communicated to the other party, and that a registered letter sent to that address is considered as validly received if it has not been claimed after a certain number of days.

Chapter Two

Part One

Property and Liability Insurance

Section One
Fundamental Provisions

1. Purpose of insurance

- *"Purpose"* in the title will be replaced by a more adequate term. The same could be said about Art. 1 of the general provisions above.

- b) *"Material loss"* is too narrow, as the principle of indemnity does not prevent coverage of justified immaterial loss. An adequate term will be found in Czech to encompass both material and immaterial loss.

- c) *"... or if the law provides so"* will be added.

2. Insured event

- a) It should also be made clear that immaterial damage can be covered.

The second sentence expresses a general principle, which should be moved to the Fundamental provisions of Chapter One.

- b) This provision sets as a condition of liability insurance coverage that *"the insured is liable for* (the damage caused to a third party) *as a consequence of his conduct or relation while the insurance was effective"*.

Such language (at least in the English translation) may be ambiguous : must all conditions of liability (including the damage)

be satisfied *"while the insurance was effective"*, or is it only required that the insured's misconduct took place during that period ? (In other words, to which part of the preceding phrase does the expression *"while the insurance was effective"* apply ?). Also, are there no requirements as to the moment the victim's claim is introduced ? See all the recent developments about claims-made policies in various countries (e.g. France, Spain, Belgium).

In that respect, it was said in Prague that the wish was to allow for claims-made policies, except in compulsory professional liability insurance.

Another problem is that of "anteriority risks", i.e. damages occurred during the period of insurance, but due to prior causes. They are sometimes covered, under certain conditions, in some types of insurance (e.g. professional liability).

Our suggestion would be to give a narrow, but precise, definition of the risks covered in liability insurance, but allow for contractual deviations such as the extension to anteriority or posteriority risks, and provide for the desired exception of compulsory professional liability insurance.

Here is a tentative text along those lines :

"Unless the contract stipulates otherwise, liability coverage is granted only if the generating event, the damage and the victim's claim all occurred during the period of insurance.

However, in compulsory professional liability insurance, coverage is extended to all claims introduced after termination of the contract, provided the generating event and the damage occurred during the period of insurance".

The expression *"generating event"* is a literal translation from the French *"fait générateur"*. It is the event that caused the damage; very often it will be the insured's faulty behavior, but a broader expression was chosen to cover other causes of liability, such as strict liability or liability for other persons' acts.

- c) *"Fortuitous"* : see above, Art. 1 of Chapter One.

The rule expressed in the second sentence is repeated below, under Art. 8 1. This repetition should be eliminated.

On the substance, it is an important (and we think arguable) choice not to give the victim a direct action against the insurer, except when there is a special legal provision (we believe it should at least be the case in all compulsory types of liability insurance).

Under the proposed rule, it should be clarified that the policyholder may sue the insurer to oblige the latter to pay to the victim, since the victim itself has no right to claim the indemnity it is entitled to.

- d) should be harmonized with Art. 13 c and d of Chapter One, above.

It was said that Art. 13 d would not apply (i.e. no advance payment would be made) if the principle of the liability was controversial, not only the amount of the damage (though literally that provision contains no such restriction).

This should be reconsidered in favor of certainly innocent victims, who should be able to get advance payments without waiting for the determination of the respective liabilities of those who caused the event. We were told this did not take long in the Czech Republic in the case of traffic accidents, because of strict liability, but the problem can still arise with other types of liability, such as medical liability (is the surgeon or the anesthetist liable?).

3. Sum insured

No observation.

4. Insurable value

- a) *"Material"* will be expressed in Czech in a way that will also cover *"immaterial"* damage.

We were told the *"general price"* is defined by regulation.

- b) *"... provided the purpose of insurance is held up"* will explicitly refer to Art. 1 of this section.

5. Over-insurance

- b) We feel this provision creates the risk that a policyholder would take advantage of an over-insurance situation to find an

opportunity to cancel the contract, by asking for an excessive reduction that the insurer will certainly refuse. Perhaps it could be said that this applies only if a *"reasonable reduction"* is refused, or if the insurer insists an *"unreasonably insufficient"* reduction.

6. Underinsurance [Also Risk increase]

- While we have no observations about a), which adequately deals with underinsurance, paragraphs b) to f) do not belong under the same heading. They deal with risk increase and should constitute a separate provision (underinsurance concerns the insufficiency of the insured sum, risk increase concerns the aggravation of probability of occurrence of the insured event).

Two short provisions of Chapter One (Art. 11 i and 18 n) which already dealt with risk increase, but much less adequately, should be deleted. It has already been said above.

- b) It should be added (perhaps in Art. 13 c of Chapter One) that the policyholder has the duty to notify risk increases to the insurer as soon as he is informed of them.

- c), d) and e) It was decided in Prague that rescission would be replaced by non-retroactive cancellation.

7. Multiple insurance

- The idea of regrouping co-insurance (7a), parallel insurance (7b) and double insurance (7c) is attractive. The situations are different, but sometimes confused. It makes it clearer to deal with them in consecutive provisions.

Perhaps *"double insurance"* itself could more adequately be called *"multiple insurance"*, as it may involve more than two insurers. In that case another collective expression should be found for Art. 7.

- The policyholder's obligation to notify the existence of other insurance contracts and insurers is not fit in the case of coinsurance. It should be dropped in Art. 7 and introduced in Art. 7 b and 7 c.

7a. Co-insurance

- f) It should be left open to stipulate otherwise. There are forms of coinsurance where coinsurers are jointly and severally liable.

7b. Parallel insurance

- *"... will not exceed the sum insured"* should be replaced by *"... will not exceed the insurable value"*.

7c. Double insurance

- A definition should be added; it could be inspired by that of "parallel insurance " in Art. 7b, except that the sum of the shares of the individual insurers would this time exceed the insurable value.

- We have a preference for Version II, which is more favorable to the insured. However, the obligation of each insurer should be limited to the amount of its coverage (see art. 45 § 1 of the Belgian law of June 25, 1992, which we were told inspired this Version II).

- b) After our Prague discussion, it was decided that this provision would be rephrased as follows : *"If an insured event occurred neither the policyholder nor any of the insurers may change or rescind any of these insurances to the disadvantage of other insurers"*. We were explained this was meant to prevent some problems that have occurred in the past.

THIS WAS THE POINT REACHED DURING OUR DISCUSSIONS IN PRAGUE.

THE FOLLOWING OBSERVATIONS ARE ALL NEW.

8. Rights and duties

This is again a very long provision, which we feel should be subdivided. It would be advisable to regroup rules concerning both property and liability insurance, and rules specific to each type.

- a) This rule provides for compensation of expenses incurred by the insured to prevent the insured event when constituting an immediate threat, and to reduce the consequences of such an event. In the first instance, compensation is rightly limited to expenses *"purposefully"* incurred, and it should also be the case in the second instance.

This provision is linked with Art. 12 c of Chapter One, where the obligation to take measures to prevent the consequences of the event from increasing is stated.

- b) Mortgage rights have already been covered, more extensively, in Art. 15 c and e of Chapter One. This should be coordinated.

"... and only if..." should read : *"... provided ..."*.

- c) Subrogation of the insurer is a basic rule of property insurance, but it should not be stated three times : also see n) of the same Art. 8, and further below, Art. 9. Also see e) below.

- d) This provision is unclear to us. Under what circumstances does it apply ? When the lost or stolen insured object is found again after settlement ?

- e) seems to apply to subrogation, and it should be put together with Art. 8 c) or n), or Art. 9, whichever will be kept as the basic provision on subrogation.

"He" probably means the insured ?

- f) Why should the obligation stated in this provision be limited to the case when the damage is higher than *"what had been contemplated in the insurance contract"* ?

- j) starts by repeating what has already been expressed in Art. 12 c of Chapter One (regrettably omitting the requirement that the notification be in writing). Again, it would be preferable to avoid such repetitions. If there is a special provision for property or liability insurance, it should restrict itself to the specific rules of such types of insurance.

In liability insurance, the views the insured is asked to express should not be limited to the compensation claimed but also cover his opinion about the extent of his liability.

The ending of j) concerns another important aspect of liability insurance, conduct of the claim by the insurer. It deserves a separate provision, and such conduct should be allowed by the law, not be dependent on an authorization given by the insured in each single case.

- k) should be linked to the problem discussed in the preceding paragraph.

- l) is a repetition of Art. 2 c of this section. See above.

- m) entitles the insurer to receive a *"reasonable"* compensation for the settlement paid to a third party in case the damage was caused by the fact that the insured had ingested alcohol or other similar substances. Which criteria will determine what is a*"reasonable"* compensation under such circumstances, and who will decide ? If such behavior of the insured should deprive him of part of the coverage, why not also in property insurance ? Compare below about Art. 3 ac of Part Two, Section Three.

- n) See above, c).

- o) should be regrouped with j).

9. Transfer of rights to the insurer.

This is the most complete provision on subrogation. Also see Art. 8 c and n, and the comments made above.

- c) We do not understand this provision. In liability insurance, subrogation is usually out of place, since the liable person is the insured himself. However, a liability insurer can be subrogated if he has indemnified the whole damage caused by several liable persons (including the insured), and claims their shares from the co-authors.

10. Change of ownership

This provision is more explicit that Art. 18 m of Chapter One, that will be deleted. See above. On the other hand it only concerns real estate; what about moveables ?

- d) is a dangerous rule : it could encourage an insurer always to cancel the contract in such a case, an easy way to cash premiums

without running any risk. We feel the premium should be refunded for the period following cancellation.

- e) is more understandable, as the cancellation is imposed upon the insurer.

- f) However, we think that if the insurer can keep the premium in that latter case, it should be borne by the seller, not by the buyer. Suppose the buyer canceled the contract because he has concluded a contract with another insurer - a perfectly legitimate initiative. According to f) he should bear the payment of both premiums ! It is after all the seller who created the problem by selling the insured property, and he could have made continuation of the insurance contract a condition of the sale.

11-23. Specific types of insurance

These provisions are not drafted yet. However we have the following observations.

- The list is sometimes puzzling. It contains several relatively minor types of insurance (12, 13, ...), while important branches such as fire insurance, or personal liability insurance are not mentioned.

- Insurance of natural hazards (11) can of course be covered by some provisions, but one would expect that a law on the insurance contract would in the first place express the traditional (but not mandatory) exclusion of losses caused by natural hazards - as well as by war and similar events, and perhaps also by nuclear energy. This is certainly a gap in the current draft.

- What is 15. meant to cover ? Vandalism ? Acts of violence ? It would then be connected with what was just said about 11.

Part Two

Personal Lines Insurance

Section One
General Provisions

1. Content of insurance

- a) This definition of personal lines insurance calls for a few observations.

First we do not understand what is meant by *"pure endowment"*; is it meant to cover forms of life insurance where the capital is paid if the insured is still alive at a certain age ? Art. 1 of Section Two below seems to indicate it is so.

"Any other insured event" is definitely too vague. Literally it could also apply to all sorts of property and liability insurance, which cannot be, since we are defining the scope of provisions where the principle of indemnity will not apply. For this reason, it is absolutely necessary to define personal insurance in a very precise and limited way. The basic criterion seems to be events that affect the life or physical integrity of a person; it could be extended to some events that affect the insured's family situation if one wants to open the door for types of personal insurance like nuptiality or natality coverage.

We also feel that *"Unless it has been stipulated otherwise"* should not be said about a provision that defines the scope of application of certain rules; the formula is also dangerous, since it seems to leave the exclusion of the principle of indemnity within the domain of freedom of contract.

2. Parties to the insurance in personal lines

- a) Same remark as above about *"other insured event"*.

- b) *"Social status"* (also in a) is again defined in a dangerously vague way. It should not be forgotten that we are defining the scope of exceptions to the principle of indemnity. What is meant by

"a juridically significant fact linked with a change in his personal situation" ? This could apply to getting married ("against" which insurance can be taken, in nuptiality insurance), but also to getting divorced, changing nationality, becoming a tradesman (*Kaufmann, commerçant*), getting bankrupt and many other situations which certainly cannot be covered by a personal line insurance.

3. Incorrect information on age

No observation.

4. Insurer's rights in connection with the ascertainment and checking of state of health.

No observation on this important provision, which will probably provoke some reactions from the medical profession. We approve this rule, based on the conception that the medical secrecy is there for the benefit of the patient, and does not "belong" to the doctor.

5. Insurance of infants

Also a very good rule.

6. Inviolability of the right to compensation of damage

Idem. This is an important consequence of the non indemnitary character of personal insurance.

7. Transfer of rights and duties in personal line insurance

Nothing is said about the case when a beneficiary has been designated. In some other countries, the beneficiary must agree to the transfer, which will deprive him of his rights. However, the Czech draft freely permits change of beneficiaries (above, Chapter One, Art. 7 d; see above); under such a system it is coherent to permit the transfer without the beneficiary's consent.

8. Reduction

In some countries, the technicalities of reduction (as well as of surrender) are not provided in the law on insurance contracts, but in the supervision regulations. The law on contracts only deals with problems such as who is entitled to ask for reduction or surrender, or whether such operations are possible without the beneficiary's consent.

- a) The language of the provision seems to indicate that reduction takes place when the second periodical premium is not paid. This is probably not what is meant as reduction can also take place at later moments of the initial duration of the contract.

- c) Why is there no reduction in that case ? Perhaps we do not completely understand what is precisely meant by *"an insurance with death benefits which ... was to be paid over a given number of years"*.

9. Surrender

See the observation introducing our comments on Art. 8 above.

10. Reinstatement of insurance after reduction

One could also provide the reinstatement of the contract after surrender, provided the surrender value is reimbursed and premiums are paid again.

11. Policyholder's creditors' claim

The consequences of this solution are difficult to grasp, since we do not know the Czech organization of bankruptcy and *"receivership"*. Does it mean the designation of a beneficiary can be revoked by creditors ? By the officer in charge of the procedure ?

Section Two
Life Insurance

1. Content of insurance

"Pure endowment" : see above, about Art. 1 of Section One.

2. The insured's consent

More generally, life insurance, like any insurance, is valid only if there is insurable interest, which means in this case that the subscriber has an interest in the insured person's survival. Since this may sometimes be difficult to establish, some countries have replaced the requirement of an interest on the insured's life by the requirement that the insured person gives his written consent. This provision adopts that solution.

Is this not a rule to be applied to all types of personal insurance, and not exclusively to life insurance ? See Art. 2 of Section Three, below.

3. The beneficiary

This is an important application of the general provision of Art. 7 of Chapter One, concerning insurance for the benefit of a third party.

Are these not also rules to be applied to all types of personal insurance, and not exclusively to life insurance ? Beneficiaries can also be designated in accident insurance, in case of death.

4. The insurance policy as security

We do not understand this provision very well. It probably has to be connected with Art. 6 b of Chapter One.

5. Exclusions from insurance

- a) Why would the suicide of the policyholder have any effect ? Only the death of the insured can provoke the settlement.

- c) In this case it should be made clear that the beneficiary will never receive the settlement (instead of providing that the insurer *"may"* refuse the settlement), but the surrender value should be attributed to the heirs.

Section Three
Accident Insurance

1. Content of insurance

- b) In this definition of *"accident"*, is it necessary to enter into details such as the*"unexpected and uninterrupted effect of high or low temperatures, gases, vapors, radiation, electronic current and poisons (excepting microbial and immunotoxic substances)"*, since they are already covered by the preceding reference to the *"unexpected and sudden effect of external forces"* ?

- c) also enters into some very specific details (see cc). Is it necessary ? Cannot it be left to insurance terms and conditions ? In any case, this provision should allow for contractual deviations.

- d), on the contrary, may be too broad. What is probably meant is that accident insurance contracts may exclude certain circumstances when defining the insured events. But the language of Art. 1 d could for instance also be interpreted as allowing such contracts to exclude settlement in cases where Art. 14 of Chapter One provides for less drastic sanctions. We suggest to add *"Subject to the mandatory provisions of this Law ..."*

2. Insurance contract

- a) We do not understand this provision. How can an unknown person be insured ? Or does it simply mean the name must not be written in the policy ? For what purpose ? Or does it concern collective accident insurance, where the insured are a group of people who do not have to be individually identified ?

- b) The reference to the insured's written consent proves that Art. 2 of Section Two is a general rule for personal insurance, and should not be limited to life insurance.

3. Settlement limitations

- a) Reduce to what extent, according to which criteria ? This should not be left to the discretion of the insurer.

- ab) What is meant by a conduct *"which grossly violated an important social interest"* ?

- ac) This applies to accident insurance the same philosophy as the rule expressed in Art. 8 of Part One, above.

b) confirms the impression given by the initial paragraph of a) that the insurer is rather free to decide by how much it will reduce the settlement. We learn here, *a contrario* , that it should not be by more than half if the act was not intentional. We also learn that the insurer can decide than the act was *"particularly socially dangerous"* to deny all settlement. This is disturbing. We feel the extent of a party's obligations should never be left to the appreciation of that party. The law should provide criteria, and make them as precise as possible.

Section Four
Other Types of Insurance

1. Content of Insurance

It is suggested to say : *"Those types of personal insurance which cannot, etc..."*.

2. Insurance of medical expenses

Though this is a usual accessory of certain types of personal insurance, we believe this type of insurance belongs to property insurance (see above, Chapter One, Art. 2). It is subject to the principle of indemnity .

3. Indemnification

- a) We do not understand this provision.

- b) The location of this rule implies that it only concerns *"other types of insurance"*, and for instance not accident insurance. Such a rule would be unusual for personal insurance in general; since the insurer's settlement consists in a sum, not an indemnity, the victim can cumulate his personal insurance settlement and any compensation he may get from other sources (see Art. 6 of Section One, above).

Still, the rule we are discussing should not apply to types of personal insurance that are neither life nor accident insurance, since they are still personal types of insurance. Is it meant to apply to medical expenses insurance ? This would confirm what has just been said, that such insurance does not belong to personal insurance.

There should also be a coordination with the rules governing health insurance, since it is not unusual that the insured will first apply to the health insurance institution, which is apt to grant a quicker settlement. On the other hand, it is a policy decision to determine who, the social security institution or the private insurer, will have to bear the costs in the last instance. In Western countries, it is generally attempted to impose it on the private insurer. The rule in Art. 3 b gives the opposite solution.

Chapter Three

Transitional and Final Provisions

This Chapter is not drafted yet in the document available to us.

Prof. Marcel FONTAINE
May 21, 1995