FRAUD From Back Forwards
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1 In the public, as well as the legal arena, there is one area of insurance in which there appears to be some consensus. The insurance industry generally, often for good reason, gets itself into all sorts of bother with the courts, other tribunals, the public, and in particular the media in its attitude to the technicalities and niceties of insurance law. One area in particular is the issue of non-disclosure and mis-statement on inception. The Law Commissions proposed changes to this duty in the latest insurance law reform legislation will, to some extent, level the playing field.

2 But why is it that the area of fraud remains relatively intact? In two of TOWER's recent forays into the media spotlight, it was interesting to note the public perception. The first was the famous case of Detective Garner who deliberately destroyed his house in an attempt to defraud TOWER. The second and most recent case was one that appeared on *"Fair Go"* in which a Northland family deliberately inflated their contents claim in an otherwise legitimate fire. In that case TOWER declined both the house and the contents claim, relying on the well-established principle in NZI v Gibbs. In both cases, the anecdotal public response to TOWER was overwhelmingly against paying these fraudsters. For some reason, the public have no tolerance to fraud and reject any attempts to use what they see as "their funds" to compensate fraudsters.

3 As an insurer, fraud is one area in which we see no room for negotiation. And by fraud I mean both deliberately false or inflated claims and false statements in support of claims. In the area of fraud, insurers tend to have a harder attitude with little or no room for negotiation or compromise. If the extremely high standard of proof is met, the insurer will defend fraud cases, often to the bitter end. I know of many cases, both when I was in private practice and currently in which insurers have spent significantly more than the amount of a claim in defending fraud.

4 But why is this so? The old-fashioned and technical answer would turn on complex and somewhat archaic concepts such as the duty of good faith, and I still see cases in which people resort to the use of Latin when considering such issues. But from my perception as an insurance lawyer, it is a bit more simple. If the consequence of fraud was any less than total failure of the claim, there would be no downside to insureds "tweaking" the truth or bolstering their claims. It would be open slather and people could lie or exaggerate as much as they wanted with no civil downside if they got caught. This is certainly the approach that was taken by the Australian Law Commission when considering the issues that eventually became part of the Insurance Contracts Act 1984.

5 In this context it is important to distinguish between two general areas of fraud. This is because I believe that the insurance industry needs to be careful of recent attempts to develop some form of "first and second degree fraud":

- <u>The first category is false claims</u> – By this I mean claims that in themselves are false, such as arson or a staged burglary or car theft. As yet, there are no suggestions even in the most extreme cases

that insurers should have to meet these claims. Back was one of these cases and the fact that Mrs Back deliberately torched their house became pretty obvious. One of the main difficulties that insurers face in catching such criminals is that they often have to do so with one hand tied behind their backs. One of the more "interesting" aspects of the Back case was Mrs Back's attempts to interfere with the photo albums to make them look like they had been in the fire when in fact they had been carefully stored in a friends house before lighting this fire. When we "found" the albums, we thoroughly photographed them, and then asked Mrs Back to produce them for forensic inspection to see if they'd been in the fire. Surprisingly, when she dropped them off they were covered in soot! Her learned QC had the audacity to accuse TOWER's investigator of entrapment! But the investigator explained that he was actually giving her the chance to tell the truth!! The point? I've found that sometimes it's necessary to think outside the square when dealing with the criminal mind, and within reason, I believe the Courts accept this.

- The second category is genuine claims that are otherwise tainted in some way by fraud – It is in this area in which there is a school of thought suggesting that false statements in otherwise genuine claims should not taint the entire claim. This appears to have started with the Orakpo decision in the UK, and the Ormsby decision. Some commentators have developed the concept of "bolstering fraud". Somehow this is treated as less serious than the first category of fraud, so that when the insured is caught out, his or her claim is not compromised.

6 As an insurer, I find this idea abhorrent. For one, if the insured has been caught out lying in one area of the claim, who knows where else there is dishonesty or fraud? The person, like Mr Orakpo, who is prepared to panel-beat the facts to make his or her claim look better (whatever his or her motive) cannot be trusted in any other respect.

7 In the good old days, the courts took a much stronger line on issues such as this. Probably my favourite case is an old American case from the 1890s, Dolloff v Phoenix Insurance Co, in the Supreme Judicial Court of Maine. The insured had been caught making false statements and the Judge made the following statement:

> *"The Court will not undertake for* [the insured] *the offensive task of separating his true from his false assertions. Fraud in any part of his formal statement of loss taints the whole. Thus corrupted it should be wholly rejected and the suitor left to repent that he destroyed his actual claim by the poison of his false claim"*.

8 Strong words for sure, but I do not believe that anything has changed.

9 After a brief foray into the realms of political correctness, it is refreshing to see that the Courts may be heading back in the right direction. The decision in Ormsby has now been rejected at a number of levels. In particular:

- In Vermeulen v SIMU, Justice Hardie-Boyes said that he had *"considerable difficulty with the decision"*;

- In NZI v Forbes the court found that the decision was limited to its facts.

10 Then in the Back decision, Justice Hammond found that it is fraudulent to persist in a claim that is seemingly honestly made after deliberately damaging property in order to deceive the insurers.

11 In Kelly and Ball – *Principals of Insurance Law*, the authors expressed the opinion that Ormsby should be regarded as a case decided on its own facts and of no precedent value.

12 Then finally, the Supreme Court of Victoria in Tiep Thi To v Australian Associated Motor Insurers had the courage to reject the decision once and for all. The judge in that case said:

> *"I regret to say that I find I cannot agree with the conclusion in Ormsby. I consider that the existence of an underlying valid claim does not render fraud irrelevant; the dishonest intention required for fraud is at least one to induce false belief in the insurer for the purpose of obtaining payment or some other benefit under the policy, with or without belief or knowledge of a lack of entitlement; and fraud which relates to the claim with the requisite intent will disentitle the claimant, even if made subsequent to the first presentation of the claim".*

13 My simple perception or interpretation of this summary is that it is a somewhat more sophisticated statement of that made in the very early American case I have referred to, and in particular that the Court recognised the "downside" argument I have put forward.

14 I think the days of referring to concepts such as "utmost good faith" as somehow elevating insurance policies to a special level may be drawing to a close, but I would take a more commonsense approach. My perception is that the extremely high standard of proof required for an allegation of fraud is sufficient protection for insureds. In Back, Justice Hammond used the phrase, *"clear and convincing"*. I believe that once an insurance company has proven fraud of any type to this level, the entire claim should fail. And by fraud I mean both deliberate exaggeration and false statements. It does not matter that the insured lied about something collateral to the claim. If the courts and other bodies do not take a not negotiable position on fraud, then it will become open season and there will be no downside to dishonesty of the type we are aware of.

Note: The above represents the personal opinion of the author and not that of TOWER or the ISO.

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