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Unfair practices in the insurance market: Describing unfair clauses^{*}

Abstract

In a market economy, the protection of consumer rights is an extremely important issue. This also applies to the insurance market where these issues are generally understood as ones related to the conclusion and execution of insurance contracts.

The insured person is exposed to many dangers, being the weaker party in the insurance market, since insurance companies, as professionals, can easily impose convenient transaction terms.

The article aims to identify market practices including unfair terms imposed by insurance companies. It provides examples of such unfair terms and conditions in the form of so-called abusive clauses in insurance contracts and points to the consequences of their use.

Keywords: insurance market, unfair clauses

JEL Classification: G22, L51

1. Introduction

In a market economy, the protection of consumer rights is an extremely important issue. This also applies to the insurance market, understood as all the issues related to the conclusion and execution of insurance contracts.

^{*} The article is an updated version of the paper published in Polish in the *Annales. Ethics in Economic Life*, 14(2), 131–138.

In our opinion, every insured person is a consumer. The insured are exposed to many dangers, being the weaker party in the market, since insurance companies, as professionals, can easily impose convenient transaction terms. Therefore, the insured require adequate legal protection and education.

The aim of the article is to point to unfair market practices including so-called abusive clauses used by insurance companies. Examples of the use of abusive clauses are provided, and the consequences of their application are indicated. The article is written on the basis of a literature review.

2. The concept of abusive clauses—EU Directive 93/13/EEC

Until recently, the term “abusive clauses” was known only to legal experts. This concept is identified with the definition of prohibited contractual clauses, and the Civil Code refers to prohibited provisions (the so-called grey clauses).

In the insurance market, many contracts are concluded—regarding both life and non-life insurance. In many cases, insurance companies have ready-made contract templates. They are rarely subject to in-depth analysis or negotiation. Professional insurance companies take advantage of this fact, introducing into so-called standard contracts provisions convenient from the point of view of their own interests and disadvantageous to the insured. These provisions will be henceforth called abusive clauses.

An extensive analysis of the concept of *prohibited contractual provisions* is provided in the literature (Skory, 2005). The provisions used in the General Terms and Conditions (GTC) of life insurance contracts have recently been analysed (Office of Competition and Consumer Protection, 2010). In the discussion on the results of this analysis, the vagueness and ambiguity of their wording—or even how they mislead the consumer (the insured)—are indicated.

The practice of using abusive clauses is quite long, as evidenced by the Resolution of the Committee of Ministers of the Council of Europe of 1976, in which the work on a directive prohibiting the use of such provisions was initiated. The resolution indicated the need to protect the consumer (the insured person) from unfair provisions. Directive 93/13, adopted by the Council of the European Union on April 5, 1993, regarding unfair terms in consumer contracts, is also worth mentioning. The concept of abusiveness is based on formal and material premises that include (Czublun & Stykowski, 2007, pp. 36–37; Kowalewski, 2006, pp. 110–116; Rokita, 2007, p. 35):

- (1) a lack of individual negotiations between both parties to a contract,
- (2) a violation of the principle of good faith between both parties to a contract,
- (3) a gross disproportion of rights and obligations to the detriment of the consumer.

This directive obliges the Member States to build a system of verification of contract templates, including abusive clauses.

According to Directive 93/13/EEC, Article 3.1, a contractual term which has not been individually negotiated shall be considered unlawful if, contrary to the requirement of good faith, it causes a significant and unjustified disproportion of contractual rights and obligations to the detriment of the consumer. Article 3.2 stipulates that the contractual clause cannot be considered individually negotiated if it has been drafted in advance of the conclusion of the contract and the consumer has not been able to influence the substance of the term, particularly in the context of the pre-formulated standard contract.

In the case when a person running a business claims that the contractual clause has been individually negotiated, this person bears the entire burden of proof of this fact.

The conducted research on the use of abusive clauses in selected countries has led to the following conclusions (Skory, 2007):

- (1) specific legal solutions that comply with Directive 93/13 have been developed in Germany and France,
- (2) fairly direct translations of Directive 93/13 have been made in Hungary and the Czech Republic, while the content of this directive has been modified in Hungary and adapted to the legislation in this country.

In practice, the consumer has limited possibilities to pursue claims in another country in the face of the interpretive diversity of consumer protection provisions. It is worth mentioning the government institutions dealing with consumer protection:

- (1) Consumer Direct (UK),
- (2) Commission on Abusive Clauses (France),
- (3) European Consumer Centre (Germany, the Czech Republic, Slovakia),
- (4) European Consumer Centre of Hungary (Hungary).

3. Polish legal regulations

The first regulations in Poland concern the Act of March 2, 2000, on the protection of consumer rights and the liability for damage caused by a dangerous product. This Act replaced not very clear provisions in the area of combating prohibited provisions in contracts in force in previous years.

It was, however, the next amendment to the Civil Code of February 14, 2003, that introduced the definition of the consumer as well as the provision on prohibited clauses. The Civil Code stipulates that

the provision of the contract concluded with the consumer (the consumer contract) can be considered unlawful. The subject of the regulation is a known natural person who concludes a given contract for purposes not directly related to his or her business or professional activities.

In accordance with Article 76 of the Constitution of the Republic of Poland of April 2, 1997:

public authorities shall protect consumers, customers, hirers or lessees against such activities threatening their health, privacy and safety, as well as against dishonest market practices. The scope of such protection shall be specified by statute.

The above-presented provision of the Constitution forms the direct basis for consumer protection. In 2000, the Act on the protection of certain consumer rights and the liability for damage caused by a dangerous product was introduced (*Journal of Laws* 00.22.271). In 2007, the Act on combating unfair commercial practices was published (*Journal of Laws* No.17, item 1206). A commercial practice is understood as an act or omission on the part of an entrepreneur, the manner of proceeding, or a statement or commercial information, in particular, advertising and marketing, directly related to the promotion or purchase of a product by the consumer. The Act states (Article 4.1) that the practice used by an entrepreneur in relations with consumers shall be unfair whenever it is contrary to good customs and significantly distorts, or may distort, the economic behaviour of the average consumer prior to, during or after the conclusion of a product contract.

In accordance with Article 4.2, in particular, a commercial practice shall be regarded as unfair whenever it is misleading or aggressive and whenever a code of conduct is used that is contrary to law. Misleading may concern the concealment of information, the omission of material information, or the non-disclosure of commercial nature. Polish legislation in this regard can be seen as quite sufficient, due to the activities of the Office of Competition and Consumer Protection (UOKiK) as well as the Court of Competition and Consumer Protection.

It is also worth noting that abusive clauses concern more voluntary than compulsory insurance. The construction of compulsory insurance (e.g., automobile liability insurance, farmers' liability insurance, the liability insurance of various professional groups) is a creation of the legislator in which it is difficult to find abusive clauses.

The situation is completely different in the case of voluntary insurance. Each insurance company creates its own General Terms and Conditions of Insurance. Different departments of insurance companies are involved in the construction of insurance terms and conditions, including legal departments. These departments, due to their professional knowledge, should not allow general insurance conditions with abusive clauses to be constructed; meanwhile, the opposite is true. By means of abusive clauses, attempts are being made to blur the liability of insurance companies.

4. The register of clauses

In Poland, the Register of Prohibited Clauses is available.¹ The list of prohibited clauses is not a closed set. New items are systematically being added. The Register of Prohibited Clauses applies to various industries. Among the 1,760 (as of 20.12.2009) prohibited clauses, 54 concern insurance companies (Cerera, 2009).

¹ http://www.uokik.gov.pl/pl/ochrona_konsumentow/niedozwolone_klauzule/rejestr_klauzul_niedozwolonych/

On the list of insurance companies whose regulations have been disputed, Ergo Hestia and Warta (14 prohibited clauses each) appear most often. Most entries come from the years 2007–2008.

Article 385 of the Civil Code contains a list of 23 prohibited contractual provisions (the so-called grey clauses). The Article states that “in case of doubt, unlawful contractual provisions are those which especially, etc.” As a consequence, it can be assumed that terms other than those specified in the Code may be considered prohibited provisions if they violate good customs or the interests of the weaker party, i.e., the consumer. It is worth noting that the prohibited provisions in the Civil Code are very general, ambiguous phrases.

5. Examples of abusive clauses used in non-life and life insurance

Referring to the prohibited clauses listed in the Civil Code, let us note, for example, the wording in Paragraph 18, which stipulates that “the contract concluded for a definite period of time shall be extended if the consumer for whom a disproportionately short time limit has been reserved fails to declare otherwise.” This clause may apply to insurance contracts where, due to inflation processes, it is necessary to index the sum insured (Malinowska, 2009). Imposing indexation is an unlawful practice of life insurance companies.

Similar wording is provided in Paragraph 21, in which the performance of obligations or liability is made conditional upon the insured fulfilling unnecessarily burdensome formalities. This problem concerns claims adjustment at successive stages of claims settlement, especially life and non-life insurance claims (cf., for instance, Jaraszek, 2007).

Some authors have noted that all abusive clauses can be divided into three groups (Ziemiak, 2008). The first group deals with the issue of premium refund. The following clause can be provided as an example: “In the event of termination of the contract, the premium for the unused period of insurance is refundable only if during the period of insurance there was no damage for which the insurer paid or is obliged to pay compensation” (the judgement of the Court of Competition and Consumer Protection of 25 June 2007 in the case XVII AmC 74/07).

The second group consists of provisions in the GTC of Insurance. For example: “The insurance contract may be terminated by either party by providing one month’s written notice in the event of payment of compensation or refusal to pay compensation” (the judgement of the Court of Competition and Consumer Protection of 11 October 2007 in the case XVII AmC 68/06). It is worth noting that these clauses are often coupled with other clauses of the GTC of Insurance stipulating in favour of the insurer the possibility of making various types of deductions from the premium amount refunded or completely excluding its refund.

The third group comprises provisions in the GTC regarding various types of deductions, handling fees, etc. As an example, the following provisions can be indicated: “Refunds for the unused period of insurance will be provided after

deducting handling costs in the amount of 20% of the refunded premium” (the judgement of the Court of Competition and Consumer Protection of 25 June 2007 in the case XVII AmC74/07) or “In the event of withdrawal from the contract or its termination, part of the premium will be refunded, deducting handling costs amounting to 10% of the refunded premium—no more than PLN 200” (the judgement of the Court of Competition and Consumer Protection of October 2007 in the case XVII AmC 68/06).

In 2010, the Office of Competition and Consumer Protection published several examples of disputed clauses concerning the premium refund (Table 1).

The summary presented in Table 1 shows that insurance companies are still using different types of wording to avoid refunding premiums.

It is also worth paying attention to the phenomenon of the emergence of many prohibited clauses appearing in all kinds of sales promotions (Bobowska, 2009). Most cases involve the manipulation of commodity prices in retail trade.

Table 1. Provisions that should not be included in insurance contracts

Provisions disputed by the Office of Competition and Consumer Protection (UOKiK)	What rights the client actually has
The refundable premium is determined proportionally to the unused period of insurance coverage and the unused sum insured.	The premium should be refunded taking into account only the insurance coverage period (the refundable amount should not be affected by any reported claims).
The insurance does not cover damage to a vehicle illegally introduced into the customs territory of the EU, i.e., when [...] incorrect data have been provided in the customs declaration or another document.	The insurance terms and conditions should specify what documents and data are referred to (though they may sanction, e.g., reducing the value of the car in the customs declaration).
If the “valuation” option has been adopted in the insurance contract, the compensation is determined on the basis of [...] valuation, excluding VAT.	Compensation should be estimated taking into account the applicable prices, i.e., including VAT.
In the case of withdrawal from the insurance contract or its termination by either party, the premium for the unused period of insurance coverage is refundable only if no compensation has been paid or if the company is not obliged to pay it.	The payment of compensation does not deprive the client of the right to the premium refund for the period between the withdrawal or termination of the contract and the date on which the contract would expire under normal conditions.
In the absence of an arbitration clause, disputes arising under the insurance contract shall be resolved by a common court which has jurisdiction over the insurer’s statutory seat.	The client has the right to have the case heard by the court with jurisdiction over the place of his or her residence.
The insurance premium is payable in advance for the entire insurance policy period and is not refundable.	The client has the right to the premium refund for each day of unused insurance coverage.

Note. Adapted from “Firmy ubezpieczeniowe stosują w umowach zapisy wcześniej zakazane przez urząd antymonopolowy,” by M. Jaworski, 2010, January 18, *Dziennik Gazeta Prawna*, 11(2642), p. C11.

6. Consequences of the occurrence of abusive clauses

The immediate consequences of the occurrence of prohibited insurance clauses involve the emergence of conflict situations between the insurance company and the insured. The most severe conflict situations are set to be investigated by the Insurance Ombudsman, among others. Complaints addressed to the Insurance Ombudsman derived from the “Interpretation of insurance regulations” group form the premise of abusive clauses.

In 2008, they constituted approx. 2.8% of all complaints addressed to the Insurance Ombudsman, which in comparison with 2007 is an increase of 0.3%. This is due to the difficulties encountered by the insured in understanding the issues related to non-life and life insurance and provisions in the General Terms and Conditions of Insurance. The insured see in the institution of the Insurance Ombudsman a professional and objective source of information and insurance education, serving to explain legal issues which raise doubts among consumers related to their application in practice (2009, p. 5). Many complaints were associated with the premium refund for the unused period of insurance coverage, e.g., due to the early loan repayment period.

The complainants pointed out that before signing the contract, they did not receive the GTC, only information that taking out an insurance policy is a prerequisite to receive the loan.

Another consequence of abusive clauses is the loss of the image of an insurance company. A cheated consumer causes the loss of many other clients for the insurance company. Apart from that, due to the existence of abusive clauses, insurance companies reduce their liabilities, decrease the value of compensations paid, and generate positive technical insurance results.

The literature does not provide data on the reduction in compensation paid as a result of the use of prohibited clauses. This issue requires separate research.

The use of abusive clauses in the General Terms and Conditions of Insurance violates the interests of the insured. For such practices, the President of the Office of Competition and Consumer Protection may impose financial penalties up to 10% of the income earned in the accounting year preceding the year of imposition or up to twice the average compensation in the event of failure to achieve revenues that year (Czublun & Stykowski, 2007, p. 37).

In conclusion, it is worth referring to the judgement of the Supreme Court of 13 July 2006 (III SZP 3/06), which states that once prohibited clauses are included in the register, they are prohibited from future use (Cerera, 2009). This means that the appropriate organisational units of insurance companies ought to keep track of the content of prohibited contractual provisions.

7. Conclusions

The presented considerations show that prohibited clauses, conventionally called abusive clauses, are being used in the insurance market. These are general provisions which include words that are not sufficiently defined, allowing for freedom of interpretation. Poland, like other countries, is obliged to apply EU Directive 93/13/EEC. The provisions in Polish legislation in the sphere of consumer/the insured protection comply with the requirements of EU law.

In spite of fairly stringent laws protecting the weaker party, i.e., the insured, abusive clauses are still being used, and not only in insurance practice. In the article, the problem of the use of prohibited clauses in the General Terms and Conditions of non-life and life insurance has been only signalled. Further research is needed in this area.

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