Arson and the insured

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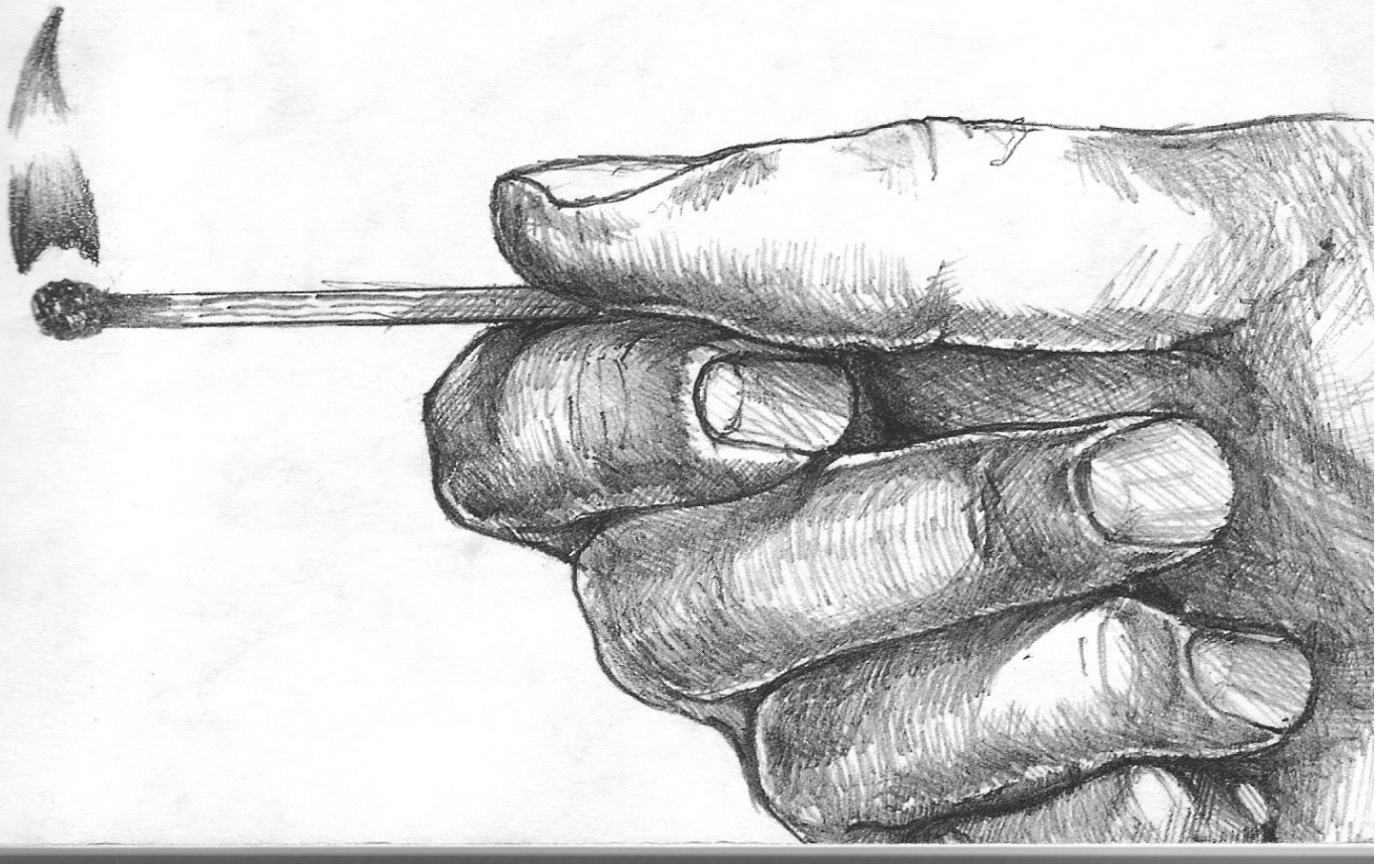

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ARSON AND THE INSURED

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CONTENTS

1. INTRODUCTION

The aim of this paper is to draw attention to the problems and difficulties that exist in

- identifying the precise cause of a fire
- assessing whether or not the insured was responsible for the fire
- quantifying the total cost to insurers and the economy of arson damage
- detecting fraud by the insured
- prosecuting fraudulent claimants
- overcoming handicaps to the resolution process brought about by deficiencies at the underwriting stage.

Recommendations and suggestions put forward in this paper are intended to provide a positive contribution to the detection and resolution of fraudulent arson insurance claims.

2. THE PROBLEMS

Harnessed and controlled, fire has been a major factor in the development of the human race. The negative value of fire as a force of destruction has no doubt been present since its discovery, and remains a formidable risk to life, property and the environment.

INSURERS

As the fire insurance industry began to develop, insurers tried to minimise the cost of fire damage by introducing means such as

- fire brigades
- building material testing and classification
- fire fighting equipment discounts
- the surveying of premises
- policy warranties.

Scientific research and developments have led to an ever increasing body of knowledge which enables the risks of fire to be assessed, the cause of a fire to be established and protective measures to be designed.

To a large extent rates were fixed when fire insurers operated a tariff. Insureds faced some difficulty in avoiding implementing improvements, paying a higher than normal premium, or indeed not being fully insured. Market forces and anti-cartel attitudes led to the recent decline of the tariff system, resulting in what seems to be continual downward pressure on premiums and a resistance to full underwriting procedures (proposal, surveys, supplementary questionnaires) as well as risk improvements.

FIRE BRIGADE

In the event of a fire the fire brigade is required to produce a report which should include the supposed cause. However, the fire brigade does not appear to have

- any training or interest in assessing the state of a business at the time of a fire
- any obligation to co-operate with insurers
- the resources to salvage property and preserve evidence.

The fire brigade's role is to protect life and property.
Occasions may therefore arise when the extent of fire damage increases because the fire brigade is concentrating on saving life or protecting adjacent high-value property. Evidence at the scene may be disturbed during damping down and post fire activities.

POLICE

If the fire brigade suspects arson the police will be involved. Arson is a criminal offence and the police are the only organisation empowered to investigate and prosecute. However, the police are not trained in fire science and need to rely on reports either from scenes of crime officers or forensic investigators.

There is no obligation to assist or co-operate with insurers and, in fact, the police have a deliberate and well-publicised policy of non-response to enquiries from insurers and loss adjusters.

CRIMINAL PROSECUTION

A criminal charge of arson will succeed only if it can be proved in court that the accused was responsible beyond reasonable doubt. Securing evidence to achieve such a high standard of proof requires investment in trained manpower and laboratory support.

Insurers are reluctant to provide the police with too much information in case this could prejudice a civil case. Recently several civil cases brought by an insured against an insurer have been successfully defended by the insurer on the grounds of arson/fraud even though criminal charges against the insured had failed at an early stage.

LOSS ADJUSTERS

The fire brigade and police authorities have roles and duties at the scene which do not properly support the needs of the insurer and the insured. The emergence of loss adjusters, as the professionals engaged by insurers, occurred as a natural development during the expansion of fire insurance over the last 300 years or so.

Loss adjusters' duties include:

- identifying the extent to which a claim is covered
- quantifying the amount that the policy should pay
- consideration of possible recovery action

The educational requirements to become a chartered loss adjuster are demanding, yet there are no formal subjects related to fraud investigation or fire cause assessment techniques.

Insurers have contractual rights allowing access to the premises but do not have police powers of investigation. They rely almost totally on the loss adjuster, although a small number of insurers use their own claims staff to visit and investigate as well.

FORENSIC SCIENTISTS

The responsibility placed on loss adjusters means that it is frequently the adjuster who must make the decision whether or not to appoint a forensic scientist. Such an appointment clearly commits insurers to cost and introduces some concern into the relationship with the insured. There is no standard procedure for the method of co-operation between forensic scientists and loss adjusters.

REINSURERS

Reinsurers in general leave the direct insurance company to deal with claims as they think fit. Minimal statistical information is maintained to indicate the extent of fraudulent arson or the capability of the direct insurer to deal with claims.

BANKS

The insured may have finance borrowed from a bank or financial institution. The insurance policy will

therefore be of prime importance for protecting assets against which finance has been provided. Therefore the insured's financial institution has a vested interest in seeing that the claim is paid. Depending on the wording of the policy the bank may or may not have a valid claim for insurance monies even if the fire was started by the insured.

INTERESTED PARTIES

After a fire the policyholder may expect to be involved with enquiries from some or all of the following:

- fire brigade;
- police;
- scenes of crime officer;
- Home Office forensic scientist;
- loss adjuster;
- insurance company;
- insurance broker;
- private forensic scientist;
- bank representatives;
- representatives of other insured interests;
- local authority inspector;
- VAT inspector;
- customers;
- suppliers;
- Health & Safety Executive inspector;
- coroner;
- loss assessors.

Insurers of goods in trust or goods sold subject to Romalpa retention of title clauses may also have an interest.

STATISTICS

Property damage by fire in 1990 produced losses of at least £1000m., 50 per cent of which are thought to have resulted from arson.

Between 10 and 20 per cent of fire damage—i.e., £100m. to £200m.—is thought to be fraudulent, started by or on behalf of the insured. There are no precise details from the ABI to show how this 10-20 per cent figure has been reached. There is also no information either on consequential loss payments arising from fire claims, or on losses to the economy.

INVESTIGATION

On the basis that 10- 20 per cent of arson cases are thought to be the result of a deliberate act or connivance by the insured then conversely 80-90 per cent of arson cases are not the result of any deliberate act by the insured. Insurers must therefore be sensitive in their approach to the investigation given that a large proportion of arson claims are thought to involve innocent Insureds.

Insurers need to balance a detailed investigation to identify the cause with concern for their client who has paid for insurance and may be suffering shock. If conducted properly, a detailed approach can reassure an innocent insured but detect an insured guilty of committing arson to defraud insurers.

A thorough and concerted approach is required to discount the involvement of the insured at the earliest possible moment. This is especially important when interim monies are required and business interruption involved.

The approach must be able to

- detect arson;
- decide if it was arson by the insured.

If arson by the insured is detected then there should be a real possibility of the insurers avoiding payment. If appropriate, pursuing a criminal prosecution may also deter others.

3. FRAUDULENT ARSON

Arson—the criminal offence

In England, Wales and Northern Ireland malicious fire raising—arson—is covered by the Criminal Damage Act 1971. In Scotland the offence is termed 'deliberate fire raising'.

Section 1 of the Criminal Damage Act 1971 is set out below. There are three sections namely:
- the basic offence of criminal damage;
- the aggravated offence;
- the offence of arson.

1. Destroying or damaging property

(1) A person who without lawful excuse destroys or damages any property belonging to another intending to destroy or damage any such property or being reckless as to whether any such property would be destroyed or damaged shall be guilty of an offence.

(2) A person who without lawful excuse destroys or damages any property, whether belonging to himself or another:

(a) intending to destroy or damage any property or being reckless as to whether any property would be destroyed or damaged; and

(b) intending by the destruction or damage to endanger the life of another or being reckless as to whether the life of another would be thereby endangered;

shall be guilty of an offence.

(3) An offence committed under this section by destroying or damaging property by fire shall be charged as arson.

The sentence on indictment under s.l is up to ten years imprisonment but in the case of arson the sentence can be up to life imprisonment.

An insured contemplating arson may lose not only the property destroyed by the fire but also his liberty for a considerable period of time. Greater publicity of the possible sentence for arson might deter some potential arsonists. (Rec. IV. 13)

It is interesting to note that in the Japanese Criminal Code, arson is still among the most serious of crimes and entails the death penalty, based on the grounds that fire can cause considerable loss of life. This penalty has not been applied in recent years although during the Edo period, which preceded modern Japan, the penalty for arson was always burning at the stake![1]

Fraudulent arson

Arson per se is not an excepted peril in insurance policies.

If somebody causes a fire without the knowledge or consent of the insured then the policy would be liable to indemnify the insured. The cause of the fire is immaterial except where the fire was caused by:

- a peril which is excepted in the policy, or
- the wilful act or connivance of the insured.

A claim submitted to insurers following a fire caused deliberately by the insured is known as arson for gain, or fraudulent arson.

4. UNDERWRITING

Competition

Having established the definition of fraudulent arson it is perhaps appropriate to consider the roles and attitudes of insurers and other interested parties. This chapter reviews practices and problems from an underwriting perspective. Competition is often said to be responsible for inadequate information gathering and assessment at the underwriting stage. In the Munich Re publication *Insurance fraud*[1] it is stated:

> It should really go without saying that careful risk assessment is essential in the initial phase of a new insurance transaction. Experience has shown that this is unfortunately more and more rarely the case; the pressure of competition, which can be exceedingly fierce, makes the conclusion of a deal the overriding consideration.

TIME

It seems that at both the underwriting and claims stages insurers are battling against the passage of time. Detailed underwriting enquiries take time; time which the placing broker or prospective policyholder is often unwilling or unable to accept. Has this competition encouraged Insureds to pursue fraudulent or exaggerated claims in the knowledge that the insurer will not look too closely at claims below a certain level or at claims for certain types of loss?

At the claims stage, a proper assessment to confirm authenticity and minimise losses arising from fraud inevitably requires a period of investigation time. However, pressure is often applied to finalise a claim before enquiries are completed.

The trend is towards minimising transaction time and documentation. In the report *Insurance in a changing Europe 1990-1995*[2] 68 per cent of respondents believed that property and casualty insurance will increasingly be seen by the public as a commodity to be judged on price alone. Speed of claim settlement was also seen to be part of the 'quality of service' factor regarded as the most important strategy for sustaining competitive advantage.

SOLUTION

Are insurers really seeking a solution to the conflicts arising from the passage of time?

At the time of a claim it is the lack of underwriting risk assessment information and documentation that can allow the fraudulent claim to succeed. If policyholders and intermediaries demand quicker underwriting and less documentation then the existing terms of the insurance contract may require modification or alteration. To prevent the insurance contract becoming akin to a 'blank cheque' policyholders must be made to realise that by reducing underwriting time and documentation there will have to be a compensating increase in claims investigation and a requirement on them to prove the loss.

REINSURANCE

Decisions in many areas of insurance are based on economics. The costs of doing or not doing something are balanced against the expected advantages or disadvantages. The extent to which, if at all, direct insurers are influenced in their decision-making processes (underwriting and claims) by the existence of reinsurance requires further research. (Rec. I.1).

Chapter 4 deals with the area of reinsurers' involvement. However, mention can be made here of the response to one of the questions put to reinsurers:[3]

> 7a) In your opinion is there a tendency for a direct insurer to pay a suspect fire claim (because the reinsurer will then pick up a percentage of the payment) rather than conduct a detailed investigation (the cost of which might not exceed the direct insurers net retention if successful)?

Most responses were in the negative but several interesting affirmative responses are quoted below:

> Yes, in certain circumstances and in certain areas of the world there is sometimes such a tendency.
>
> Very likely.
>
> In many territories where net retentions are low and reinsurance high, direct companies may be inclined to pay the claim as an easy option.

STATEMENT OF PRACTICE

There is clearly a balance to be struck between a providing a competitive service to the policyholder and conducting a proper investigation (at both underwriting and claim stages). The formulation of a general statement of practice for claim investigation procedures would explain the insurance market's approach to claims and gain sufficient time for the initial investigation to be completed. The insurer would then be in a position to decide how to proceed without having been forced by competitive market pressures to pay before having reached a proper decision. Such an approach should be acceptable to genuine policyholders, shareholders, reinsurers and intermediaries. (Rec. II.5)

CENTRAL ANTI-FRAUD REGISTER

Access to information on suspected or proven fraudsters would help insurers at the underwriting and claim stages. A central anti-fraud register, not just restricted to fire claims, could be established by insurers. It should contain details of:

a) policyholders, and shareholders, directors and managers of policyholders, who have been involved with an insurance claim of a significant size arising under a commercial insurance policy;

b) the amounts claimed and paid;

c) whether the claim was repudiated, the amount of claim and reasons for the repudiation;

d) the insurer and adjuster concerned.

This type of register would raise data protection concerns, which would need early consideration. However, the level of crime and the losses from fraud claims in general, and fraudulent arson in particular, justify legal recognition of the need to maintain such computerised records. (Rec. I.2 & II.1)

Competition can be thought to conflict with the need to underwrite to minimise the risk of arson. Some individual initiatives on arson are discussed next.

Individual initiatives

This section reviews some of the underwriting approaches from insurers and reinsurers that have been encountered during this research.

ASSESSMENT TOOLS

At least one UK company (Provincial Insurance) has developed an arson assessment form to be completed by its surveyors after every survey and re-survey. This form allocates points to various features and attempts to quantify the arson risk and to focus the minds of the surveyors and underwriters on the problem of arson.

Swiss Re has produced a qualitative assessment guide on the identification and weighting of factors that could give rise to arson. This guide, known as the 'Arson risk indicator', endeavours to assess the risk by allocating points to exposure and loss control measures. It is intended as a guide, tool and checklist for the underwriter, and is based on data from the insurance industry, police and fire brigades.

There are two scales:

- Loss control, which assesses factors such as fire and security precautions and insurance measures;
- Exposure, which considers factors such as economic climate, location, neighbourhood, policyholder, and the experience of the insurer.

It is not known how successful this guide has been in practice or the extent to which it is used.

PUBLICATIONS

Two major reinsurance companies (Swiss Re and Munich Re) have issued publications relating to arson and insurance fraud.4 Factory Mutual produces the *Pocket guide to arson & fire investigation*, which is distributed to interested parties and is a useful practical guide.

FINANCIAL SUPPORT

In 1976, Factory Mutual Engineering and Research in the USA established an arson programme. It has since donated over US$ 500,000 to arson control groups throughout the USA. Factory Mutual International established an arson fund in 1990, which has supported various projects, including providing UK fire brigades with funds and a computer. The Factory Mutual International arson fund is available for appropriate projects and organisations throughout the world. The goals of the programme are:

- to improve the quality of fire investigations;
- to improve communications with arson control agencies;
- to increase direct insurance industry input.

Currently the UK fund is £15,000 but this is reviewed each year.

Proposal forms and surveys

Most of the UK insurers that returned the questionnaire also sent a copy of their commercial proposal form. Analysis of the forms showed that there is no standard proposal form. Basic details are generally requested by all insurers. Additional information is requested in areas, which interest the individual insurer concerned. An examination of different insurers' proposal forms by a potential fraudulent claimant or a proposer with something to hide, could indicate which insurer represents the easiest target in terms of minimum questioning. Information should be sought in the proposal relating to all individuals who could be regarded as an *alter ego* of the proposer company. (Rec. I.16)

ELECTRONIC SLIPS

With the increasing use of electronic information exchange and computer underwriting the traditional reliance on a proposal form will diminish. The information will still be required but the actual document will no longer be used to the same extent. The development of electronic underwriting with electronic slips requires a new procedural under-standing between the parties to the insurance contract. Confirmation of information or answer-back sentences, clearly setting out the insurer's attitude to material facts, could become standard and preserve the utmost good faith doctrine within the new electronic underwriting system.

ALTERNATIVES

If the trend continues away from the use of proposal forms then perhaps the general insurance industry should require all intermediaries to obtain and file their questionnaire information. Life insurance brokers often maintain a 'fact find' file of information supplied during meetings, signed by the proposer, to protect themselves against possible claims of negligence. General insurance brokers often maintain such information but may not ask the proposer to sign a copy to vouch for its truth. If an insurer is not able to obtain a proposal completed by the policyholder then perhaps a copy of the questionnaire or internal file note completed by the broker would be a useful second best. The ABI (Association of British Insurers) and BIIBA (British Insurance and Investment Brokers Association) could perhaps agree a format and procedure. (Rec. I.3)

Greater involvement by brokers will increase their responsibility for accuracy and comprehensive transmission of all material facts. Policyholders should be clearly advised that the broker is their agent and that all information provided to the insurer should be verified and approved by the policyholder. (Rec. I.4)

MATERIAL FACTS

The definition of a material fact perhaps needs to be reconsidered. While each insurer might react differently to the same piece of information it is probable that most would react in a similar fashion. The information necessary to underwrite and rate is surely not as wide and diverse in reality as might sometimes be suggested by the insurers.

Information can be categorised under headings such as premises, personnel, processes, etc. With sufficient thought and market consensus, 90 per cent of the information could be categorised. The remaining 10 per cent may always be difficult to define but if a material fact is so significant the insurance industry should be able to produce a list of the areas where the underwriter would require information.

If a proposal is not provided insurers should perhaps respond to the policyholder with a clear explanation of the significance of any non-disclosure. For example, a letter or market agreement similar to the life insurance cooling-off period letters could seek to show the extent to which the onus of disclosure is on the policyholder. Such a letter might read as follows:

Your insurance policy has been accepted by the insurer(s) named above in the absence of a written proposal form. In order to fix the premium and terms for your policy we have been provided with the information shown on the attached sheet from your intermediary: (Name of broker/building society, etc.).

As you will see from the attached list we have not been provided with any information under the headings against which no 'information provided' has been shown. In the event of a claim, our procedure will require you to prove that the information shown on the attached list is correct and that no information has been withheld or modified. Any such withholding or modification could result in the policy being cancelled and any claims not being met by the insurer(s). Please review the information on the attached list closely and inform this office if the information shown on the list requires alteration.

The list referred to in the letter would contain the categories of facts considered by the underwriter to be material to the risk concerned. This suggestion is in effect a reversal of the traditional proposal transaction. Rather than the proposer submitting a form it places the proposer in a position of being informed by the underwriter of the facts which are considered material. This procedure would not only serve to recognise recent consumerist trends, but also provide insurers with solid information for consideration at the claim stage. (Rec. I.5)

The continuing development of expert systems, electronic communication and word processing should be more than capable of dealing with this new form of proposal transaction.

The introduction of this process would of course require considerable thought and consideration. Insurers could lose a certain element of legal protection by providing details of what is regarded to be material. However, the certainty produced at both underwriting and claims stages would outweigh that disadvantage. It would certainly leave the way open for greater use of computerised underwriting systems capable of handling and considering the information under the categories of material facts for the policy concerned.

SURVEYS

It is interesting to consider the implications to the insurer of actually surveying the premises. Unless the insurer precisely states the scope of such a survey it is possible that the insurer could be held to have come in to possession of information which had not actually been disclosed by the insured, e.g., the nature of the building construction, storage of hazardous materials, or previous structural damage. Any proposed changes will doubtless be considered not only by individual insurers, but also by the ABI.

Association of British Insurers

The ABI was established in 1985 to undertake the functions previously performed by a number of associations including the British Insurance Association, the Fire Offices' Committee, and the Accident Offices' Association.

Over 90 per cent of all UK property insurance business is transacted by members of the ABI.

Among its functions, the Property Committee of the ABI liaises with the government and other bodies, establishes standardised practices, administers the market fire statistics, and considers legislation and other issues affecting property insurance such as arson.

J.L. Phillips 5 suggests that the ABI has an important role to play in reporting to its members on such issues without seeking to influence their underwriting attitudes.

As with many trade organisations the received impression of the insuring public is that membership of the ABI is a guarantee or indicator of good practice. However, if an ABI member wished to underwrite without regard to arson assessment factors, and then to pay or repudiate claims without consideration to cause and policy issues, the insurer would not be in breach of any ABI requirements.

ARSON

Other than a video entitled 'Arson alert', the only arson-related publication issued by the ABI is a small leaflet, 'Arson beware!', which contains brief guidelines to policyholders on how to prevent or minimise the risk of arson. There does not seem to be any formal guidance to member companies on assessing an arson risk or on how an arson claim should be investigated.

PERSONAL INSURANCES

The ABI has produced a statement of general insurance practice with regard to personal insurances 6 and while this does not have the force of law, it is taken into account when complaints are made. The insurance

ombudsman may well find in a complainant's favour if he establishes that the insurer concerned failed to abide by the statement. Furthermore, if a case subsequently went to court the statement may be produced in evidence to show what is prevailing best practice in the issue under dispute.

COMMERCIAL INSURANCES

If statements of practice were produced for commercial underwriting and claims investigation insurers could be bound by the statement and subsequently suffer if they deviated from its terms. For this reason insurers may not show much interest in this proposed development.

The present private capacity statement is essentially a list of prohibitions containing phrases such as: 'Should be constricted', 'An insurer shall not', 'An insurer will not' and 'Insurers will avoid'.

Providing that the statement asserts what insurers may do rather than what they may not, it should be possible to produce a statement of practice for commercial underwriting, and claims investigation

CLAIMS INVESTIGATION

It is difficult to understand why insurers should be reluctant to introduce a claims investigation procedure. Is it that they are concerned that they will be 'caught out' by settling claims when they shouldn't? This is doubtful as insurers tend to give policyholders the benefit of the doubt.

Would insurers prefer to have guidelines of a more authoritative nature? The insurer would then be able to refer policyholders to the guidelines as being representative of reasonable market practice. Perhaps insurers should consider this aspect at the highest level where the balancing of shareholder and policyholder interests can be best assessed.

STATEMENT OF PRACTICE

It is probable that the genuine policyholder, and indeed insurers' shareholders, would wish to see in a statement of practice that:

- there is a procedure to be followed for prudent underwriting,
- all claims are subject to an investigation procedure.

A statement of practice containing brief descriptions of all the usual steps of an investigation and the areas that are considered would leave the individual insurer with discretion as to when the investigation should terminate. It may be that a genuine claim will be identified as such at an earlier stage than a suspect claim producing positive information to certain lines of investigation. The statement would however give an insurer the opportunity of showing an insured that the procedure is a standard approach agreed by ABI member companies.

Through collaboration with the Chartered Institute of Loss Adjusters it should be possible to produce a statement of practice relating to commercial claims investigation. (Rec. II.5)

Loss Prevention Council

The Loss Prevention Council (LPC) was formed to continue the work of the Fire Offices' Committee (FOC). The FOC was formed in 1858 and was involved in fire prevention including the testing of fire extinguishing appliances such as sprinklers, building elements, fire proof doors, etc. It also compiled statistics and produced rules for building construction. In July 1985 the FOC ceased to exist and the ABI took over its workload.

ROLE

The report of the Association of County Councils, Arson (1987) contained interesting and constructive recommendations, one of which related to 'Target hardening after a fire had occurred'.[7] The recommendation was that all local authorities should seek a locally acceptable method of integrating fire and architectural expertise. The LPC is perhaps the appropriate vehicle for the insurance industry to control and develop such physical preventative measures against arson at a national level.

It has not been established to what extent, if at all, the LPC is involved in the detection of arson. There would certainly seem to be merit in involving the LPC in post-fire loss investigations specifically to provide 'risk hardening' and' anti-arson' guidelines. (Rec. I6a)

The LPC should also be encouraged to focus on ways to minimise fire damage where the fire has been started deliberately. (Rec. I.6b)

Arson Prevention Bureau

A new organisation which could address the arson problem on behalf of insurers and government is the Arson Prevention Bureau. The Arson Prevention Bureau came into existence in 1991 and is jointly sponsored by the Home Office and the ABI.

TERMS OF REFERENCE

The formation of the Arson Prevention Bureau was proposed in the Home Office Report of the Working Group on the Prevention of Arson.8 The terms of reference for the arson bureau were as follows:

> The main tasks of the Bureau would comprise:
> - working closely with other organisations to ensure that the National Arson Control Programme is implemented;
> - identifying scope for changes in the programme;
> - monitoring progress and issuing an annual report.
>
> Specific activities would include:
> - monitoring the incidence of arson in the UK;
> - seeking to improve the statistical base;
> - drawing together information on arson from all UK sources, in particular on arson prevention initiatives taken by government departments, local authorities, fire brigades and the police;
> - disseminating information on the incidence of arson and on appropriate remedial measures;
> - organising and advising on publicity and educa-

tion to combat arson;
— suggesting areas requiring research, initiating such research or commissioning research projects;
— monitoring the arson situation in other countries;
— providing the UK liaison and input into the Arson Prevention Institute which is being set up by 13 countries represented in the Conference of Fire Protection Associations Europe.

The organisation is envisaged as follows:
— the bureau would operate with a small permanent staff and where necessary be able to draw on the resources of other organisations;
— it would be funded by the government, the insurance industry and the business community. It would report to a governing council representing the main bodies involved in the arson problem.

The business community does not as yet seem to have provided any funding.

PROGRESS

In a report[9] on the first six months of the bureau's activities the director general advised that surveys and discussion had taken place with both the fire brigade and the police on investigation and liaison. The bureau is looking to involve and motivate all those parties which have an interest in identifying and reducing arson in general. It has setup a working group to study fraudulent arson and it is hoped that improved statistical information will enable a remedial programme to be launched.

In a conference in November, 1991[10] the director general of the arson bureau stated that he would be doing his best to change the situation where loss adjusters and insurers are excluded by the police and fire service from any kind of joint discussion. He also suggested that the bureau and the Chartered Institute of Loss Adjusters might co-operate with a view to providing training courses in fire investigation.

There is also scope for improving the information available by integrating data held by the fire brigade, police, insurers. (Rec. III.1)

FUNDING

The creation of the Arson Prevention Bureau must be welcomed, given that the current annual cost of arson claims in the UK is estimated to be at least £500m. without including business interruption and losses to the economy. However, the level of funding to the bureau is minuscule by comparison. It could be questioned whether insurers and the Home Office are really taking the problem seriously. If it is the intention of the insurance industry and the government to delegate responsibility for initiatives on arson to the bureau then the level of resources will not be sufficient.

As the percentage of non-fraudulent arson is thought to be in the region of 80 to 90 per cent of the total by value then it is understandable that the bureau is particularly concerned with issues such as prevention. However, the remaining proportion of arson that is thought to result from the deliberate act or instruction of the insured is still estimated to be in the order of £200m. which is not insignificant. This sum is sufficiently substantial to require greater action to be taken immediately against fraudulent arson.

FIRE LOSS BUREAU

In 1968 the Fire Loss Bureau (FLB) was formed by insurers with the principal purpose of enabling insurers to exchange information on possible fraudulent claims. An informal and confidential basis of operations was intended to assist in the identification and investigation of such claims. Although it was 'restructured' in 1988 the FLB has not been as proactive as the circumstances and level of losses perhaps required. Its effectiveness depends on the active participation of insurers and adjusters in supplying information. Inclusion of the FLB under the control of the arson bureau may enable both to achieve their objectives more easily.

INTERNATIONAL

The approach towards fraudulent arson in other countries varies. Arson investigation teams operate in certain states of America and receive full cooperation from all the related services.

In France the insurance industry funds an anti-fraud organisation Agence pour la Lutte contre la Fraude à l'Assurance (ALFA) which has specialist fire and fraud investigators on call at the request of an insurance company. From interviews with key personnel at ALFA it seems that there is a good level of co-operation between the police, fire brigade and loss adjusters *(experts d'assurance).*

No such organisation as ALFA exists yet within the UK although this is possibly a function which the Arson Prevention Bureau could develop and operate. Such a department (perhaps called the Active Investigation Department—AID), with the ability to work with and co-ordinate the activities of all the other agencies involved, could surely achieve:
— reduced payments for fraudulent arson claims;
— increased prosecution for arson.

With insurance and government support the bureau is well placed to undertake this role. Just as the Serious Fraud Office restricts its activities to suspected frauds of a significant size the AID would select cases brought to its attention by the police, fire brigade and insurers. Delegated authority to the Bureau and AID could improve the level of co-operation. First-hand experience of the difficulties and problems associated with inter-agency co-operation would then be gained. As the AID encounters problems it would, through the Bureau's position of linking both the public and private sector interests, be able to research solutions and lobby for appropriate changes in market practice, procedures and legislation. (Rec. II.19)

FURTHER RESEARCH

Urgent research is required to identify the total cost of arson, including business interruption (Rec. 111.3) and losses to the economy. (Rec. III.4) Further research is required to assess the effectiveness of organisations operating overseas and the extent to

which the UK could follow and benefit from their experience. (Rec. IV.1)

Shareholders and Names

A significant but perhaps overlooked group in the fraudulent arson issue could be the shareholders and Names that invest in, and financially support, insurance and reinsurance companies and Lloyd's syndicates.

Most insurance companies have shareholders. Lloyd's syndicates have Names. What duty does the insurer's management owe to shareholders and Names?

In the case of *Chapman* v. *Pole* 1870[11] Cockburn, CJ, said:

> In consequence of the observations which have been made upon the conduct of the insurance company, I feel it to be my duty to say that I consider that in insisting on a full and searching examination into the case in a court, the defendants, the Sun Fire Insurance Society, have only discharged their duty to their shareholders and the public.

Times may have changed and it is questionable now whether insurers have a duty to the public as suggested in *Chapman.*

SURVEY

Looking at the insurer's duty to shareholders, question 1 in the questionnaire to UK insurance companies12 asked:

> To what extent should policyholders, and shareholders expect their insurance company to investigate and defend claims arising from fire damage where the fire is thought to have been started by the insured?

In the main, replies indicated that an insurance company should investigate and defend to the fullest extent possible. Typical replies were as follows:

> Shareholders have a right to expect that the insurers investigate all claims thoroughly and take all possible steps to avoid paying fraudulent claims.
>
> In claims were there are doubts about the genuine nature of the claim they would certainly demand the in-depth investigation but nevertheless appreciate that there is some difficulty in actually proving arson by the insured.
>
> They should expect insurers to use a level of resources appropriate to the size of the claim to investigate any situation where fraud is suspected. If these investigations produce sufficient evidence to discharge the considerable onus upon the insurers to prove fraud then they should expect the claim to be defended.
>
> Shareholders are entitled to expect that all claims where there is suspicion of fraud will be carefully and vigorously investigated but subject to an awareness that all investigation costs money. In every case a balance has to be drawn at some time between the cost of continuing investigation and the prospect of success in proving fraud.

ECONOMICS

Most of the replies to this question brought out the key judgmental issue of:

Cost of investigation v. Value of claim

Notwithstanding the need to balance the cost of investigation against the expected cost of the claim, responses overall suggested that full investigation should be conducted wherever possible. Unfortunately the apparent lack of detailed statistics held by insurers on suspected fraudulent claims means that in all probability it would be very difficult for most UK insurance companies to prove to their shareholders and others that they practice what they preach.

PUBLICITY

Two opposing consequences were foreseen in publicity terms as possible results of a full investigation and defence:

Deterrence v. Sensitivity to public opinion

(+) **(-)**

The deterrence viewpoint can be seen in the following response:

> The insurance industry must play a full and leading role in seeking to contain the rising crime figures and should be seen by the insuring public and shareholders to be adopting a firm and positive attitude to the investigation and defence of fraudulent or suspected fraudulent claims, not only with a view to conviction of individuals hut also to deter others who may he tempted.

The view on sensitivity to public opinion was well stated:

> Policyholders should expect insurers to take a vigorous stance where a fire is thought to have been started by an insured. There is a difficult public relations balance to achieve here though because no insurance company wishes to attract publicity suggestive of the fact that claim payments are being unreasonably withheld.

EFFECTIVENESS

It is difficult to identify how shareholders and Names could assess the effectiveness of the claims management process within the insurance company or syndicate. Comments relating to underwriting practices are occasionally noticed in both the insurance company and Lloyd's markets. The issue of negligent underwriting has been raised by Lloyd's

Names and it is perhaps only a matter of time before negligent claims management by the insurer might be a potential cause of action by shareholders or Names unhappy with the losses being incurred.

As institutional shareholders, insurance companies have sought to influence issues relating to corporate governance of quoted companies. When and how will shareholders take a closer look at insurance corn panics?

Class-action suits by shareholders are becoming an increasing international occurrence. For example in

1991 Philips the Dutch electronics group reached a US$9.25m. out-of-court settlement with US shareholders who had accused the company of making misleading profit predictions in early l990[13].

Recent underwriting losses have reflected on the management of insurers and syndicates. Senior staff have resigned or been replaced, increasingly by executives from outside of the insurance industry. The press have referred to 'lax underwriting" but do not yet seem to have considered the extent to which claims management has been a factor (for increase or decrease) in the size of reported underwriting losses.

STATEMENT TO SHAREHOLDERS/NAMES

A review of several UK insurance companies' annual reports failed to find any significant statement to shareholders regarding claims management. With the current level of losses sustained by many insurers, and the unclear extent of fraudulent claims, it will be interesting to see whether statements relating to claims management will be publicised to any extent in the future. (Rec. 1.11)

Reinsurers

Reinsurers are vital providers of financial support to direct insurers. How do reinsurers view the problem of fraudulent arson?

SURVEY

A questionnaire (15) was sent to 16 of the major reinsurers operating in the London insurance market. Eight completed questionnaires were returned and one reinsurer responded by letter. The 50 per cent return rate could either suggest that reinsurers did not wish to disclose information or indicate the low priority given by reinsurers to the claims issue.

RESPONSIBILITY FOR CLAIMS

The general impression gained from some of the comments on the questionnaires is that the respondents consider claims handling to be the responsibility of the direct insurers rather than the reinsurers.

Question 1 a) asked:

> To what extent should your shareholders expect you to satisfy yourselves that direct clients are dealing with claims correctly?

Replies included:

- shareholders should but reinsurers do not necessarily do so;
- direct clients should act as if 'unreinsured';
- we can't.

CLAIMS CAPABILITY ASSESSMENT

Question 9 asked:

> When entering a reinsurance agreement do you assess the capability of a direct insurer's claims department?

There was no formal assessment procedure carried out by any of the respondent reinsurers. Some of the replies shown below indicate the diverse, almost informal approach:

- no;
- claims control clause imposed if doubts;
- if the company is DTI authorised should be reasonably competent;
- under development;
- past experience, results and 'reputation' of direct insurer considered;
- no, but abuse by direct insurer will catch up with them.

Rather than rely solely on historical information it has been suggested that reinsurers should consider objectively the claims capability of their direct clients.' If each insurer, reinsurer and underwriter had a rating based on its claims capability, (Rec. I. 15a), then its standing in terms of dealing with claims would easily be identifiable. Such a rating exists for financial institutions.

Factors which could be considered within the rating assessment would be:

- previous claims payment experience;
- experience and qualifications of key claims management personnel;
- the existence of contingency plans to respond to specified 'disasters';
- membership of dispute resolution bodies, e.g., Insurance Ombudsman Bureau;
- education and training programme;
- extent and sophistication of computer claims handling systems;
- extent to which the computer system provides guidance to the claims staff, e.g., by use of expert systems software.

A similar rating could also perhaps be considered for underwriting capability. (Rec. I.15b)

INVESTIGATION SUPPORT

To assess the extent to which reinsurers were willing to support a direct client in the investigation of a fire claim the following question was asked:

> Would you be willing to contribute to costs incurred by a direct client in investigating and legally defending a fire claim thought to arise from arson by the policyholder, when the actual cost of that claim in total would be unlikely to impact on your reinsurance account?

The responses were: Yes: 1, No: 7.

It would seem that reinsurers could provide greater support to, and supervision of, direct insurers especially in terms of trying to identify the level of fraudulent claims in general and those arising from arson in particular.

The policyholder

Having considered the issues from the insurer's perspective it is important not to ignore the needs and expectations of the customers.

EFFECTS OF ARSON

A policyholder that has suffered a loss from fire may or may not have deliberately started that fire. The financial and human trauma suffered by the policyholder that did not commit arson must never be overlooked. The Prevention of Arson report stated that:

Arson does not affect only the premises of a business. The consequent losses of production time and customers, and the effects upon employee morale can be far more serious. Employees will be shocked, may be laid off, may even lose their jobs. The community which depends upon that business for services or for employment will suffer especially if the business does not reopen. Such incidents have contributed significantly to the cycle of deprivation in the inner cities. (17)

We believe that the real need for help is in respect of small companies. There is currently no equivalent of victim support schemes for such businesses. Loss adjusters have a crucial post-incident role to play but trade associations could take a much greater part in providing advice to their members to help them deal with the effects of arson or other serious incidents. (18)

VICTIM SUPPORT

The report went on to recommend various victim support measures including:

That consideration should be given to the establishment of victim support schemes for businesses.[19]

That written guidance be provided to volunteers who help arson victims.20

As discussed in chapter 6, some 80—90 per cent of arson claims (by value) are not thought to involve deliberate fire raising by the insured. There is, therefore, clearly a need for insurers and adjusters to show concern for the insured.

It is, however, questionable whether in the early stages it is possible for an adjuster to be both a counsellor and an investigator. Perhaps therefore the insurance industry should make provision for directing the insured to victim support services. For example, at the 1991 World Insurance Congress the chief executive of Skandia Insurance stated that it was no longer sufficient for insurers to base compensation purely on economic loss. He mentioned offering professional psychological treatment as part of the standard cover. (21)

RACIAL MINORITIES

A further complication is racially motivated arson. The *Prevention of Arson* report stated:

> Although there are no national statistics, racially motivated attacks are seen as a real problem in certain areas of the country. (22)

It is suggested that insurers and adjusters must keep in mind the possibility of a racially motivated arson attack rather than a fire caused by the insured.

The proposed statement of practice for claims investigation could be presented in a positive customer service light to support the expectation that a claims investigation will be on the basis of innocent until proved guilty.

RISK MANAGEMENT ADVICE

Positive support from insurers in terms of education and advice on risk management would probably be well received by most policyholders. (Rec. I.12) Advice could include:

- guidance on preparation of contingency plan in event of loss;
- advice on precautionary procedures such as physical protections as well as personnel;
- procedures (as can be found in brief summary form in the ABI's *Arson beware* pamphlet).

Information produced by the insured in response to such an educational approach would also have value during the claim investigation.

ALTER EGO

The definition of the 'insured' must be considered. An insured corporation can only commit arson through the act of an alter ego, that is, a person with power to make managerial decisions without further reference.[23]

It is therefore important, when insurers request information in a proposal form, that the questions are targeted not just to directors but also to individuals who could be regarded as an alter ego. (Rec. I.16)

BROKER'S ROLE

As discussed earlier the trend towards electronic underwriting demands a reappraisal of the traditional proposal procedure. This will increase the responsibility of the broker for accuracy and comprehensive transmission of all material facts.

Policyholders should be clearly advised that the broker is the policyholder's agent and that all information provided to the insurer should be seen, verified, and approved by policyholder. (Rec. 1.4)

Banks

The involvement of banks in the context of insurance coverage and claims is of sufficient significance to warrant consideration. The questions, concerns and uncertainties raised in this section suggest that there are areas for further research, debate and consideration by insurers and banks.

SURVEY

A questionnaire was prepared and sent to the chief executives of 25 major banks operating in the UK.24 Seven completed questionnaires were returned and while this response is not as high as had been hoped for, the respondents represent significant forces in the UK banking system, including three of the 'big four' clearing banks.

REQUIREMENT TO INSURE

Question 1 asked:

> Do you require your customers to insure their property if such property is the subject of a loan or security in respect of overdraft?
>
> If yes, could you please supply a copy of the wording, condition or agreement setting out your requirement to the customer?
>
> If no, on what basis are you able to protect your investment in the customers business.

All respondents confirmed that they require customers to insure. However in response to the 'if yes' part of the question there was an interesting variety of requirements shown in the answers:

- No set wording—main concern to ensure adequate insurance;
- Re-instatement index linked;
- Insure and keep insured;
- Re-instatement value;
- Premium receipt to be sighted/renewal confirmed.

APPROVED INSURER

In response to question 4 concerning approving the insurer concerned, five of the seven respondents indicated that they do not have an approved list of insurance companies. Three of the five confirmed that they would accept a policy from any authorised UK insurer and the other two said that:

- Individual assessment would be required if not ABI or Lloyd's;
- Any reputable UK company.

ABI/BANKS

An agreement exists between the ABI and banks regarding the noting of a bank's interest in an insurance po1icy.[25] By September 1991 the agreement applied to 96 insurance companies and 26 banking groups.

The agreement details the procedure to be adopted when noting and changing interest details on an insurance policy. There is no mention of any agreement that a bank should disclose information which might be of interest to an underwriter, e.g., that the policyholder has been placed into the bank's 'intensive care' category of financial health monitoring. There does not appear to be any provision for the bank to complete a proposal form or a questionnaire at renewal, or indeed provide any information whatsoever to the insurer.

POLICY INSPECTION

Question 2 asked:

> Do you require sight of a policy showing your interest as a named party?
>
> a) At inception of the loan/overdraft Y/N
>
> b) At renewal of loan/overdraft Y/N

Six respondents confirmed yes to (a) and one said that it would depend on the amount of the finance involved. Four confirmed yes to part (b), two said no and one stated that it would depend on the amount of the finance.

DISCLOSURE BY BANK

The majority of the banks that replied are aware at both inception and renewal stages that the policyholder has insurance coverage with a particular insurance company. Considering that the bank may also be aware of the financial state of the policyholder the question arises as to whether the bank should disclose such information to the insurance company.

If the information would be regarded as a material fact then it could be argued that as a party with an interest in the policy the bank has a duty to disclose this information to the insurance company. Perhaps in the first instance the bank should check with the policyholder to ascertain whether the facts have already been disclosed by the policyholder at inception or renewal.

MORTGAGEE CLAUSE

If the policy contains a mortgagee clause the bank as mortgagee is required to notify the insurer as soon as it becomes aware of an increased risk arising from the act or neglect of any mortgagor.

A typical mortgagee clause states:

> The act or neglect of any (Mortgagor) (Leaseholder) (Lessee) or occupier of any building hereby insured whereby the risk of DAMAGE is increased without the authority or knowledge of any (Mortgagee) (Freeholder) (Lessor) shall not prejudice the interest of the latter party (parties) in this insurance provided they shall notify the insurer immediately on becoming aware of such increased risk and pay additional premium accordingly.

It would be interesting to establish the extent to which changes in the policyholder's (i.e., mortgagor's) financial position could be seen as resulting from the policyholder's act or neglect.

For example, in a commercial context, would negligently maintaining overheads at an unprofitable level, or negligently proceeding with an unwarranted investment by the mortgagor result in the mortgagee coming under a duty to inform insurers, on becoming aware? It is possible that the bank would become aware of such information during the usual financial reporting procedure.

Considering that poor performance and financial difficulties are regarded as possible motives for fraudulent arson it is suggested that if the bank notified insurers the underwriter may well consider either increasing rates or possibly cancelling coverage. This would not be in the interest of the bank concerned but would certainly be in the insurer's interest.

The Munich Re publication *Arson* (1982) stated:

Even if it can be proved beyond doubt that the insured set fire to his own property, the insurer is not relieved of his obligation to pay compensation if it is stipulated in the policy that the beneficiary is a third party, since the insurer is still liable to him. This is

> the case, for example, when the policy contains a mortgage clause. (26)

Two points arise from this extract.

Firstly, in the UK the insurer is not required to prove 'beyond doubt', but on the balance of probabilities which is a slightly less onerous responsibility (See chapter 7).

Secondly, for the reasons already discussed there is a possibility that the bank under a mortgagee clause may have been in possession of information which if passed immediately to the underwriter could well have caused the insurer to cancel the policy or take remedial action.

Insurers should research and form an opinion on disclosure responsibility of a bank in terms of utmost good faith. (Rec. I.13)

A recent report by the Insurance Information Institute in New York drew attention to the problem of banks' interests. The report stated:

> Another issue of concern to the industry is that even when arson/fraud is proved, the Insurer may still have an obligation to pay the mortgage holder the amount of the remaining payments on the outstanding mortgage.[27]

CRIMINAL ASPECTS

Clearly a bank should require insurance security but it does not seem equitable for a bank to profit (or at least avoid making a trading loss) from the crime of the customer who commits fraudulent arson.

A situation arose in the USA when organisations, alleged to have been backed by the Mafia, were insuring derelict tenement blocks on a reinstatement basis. Many were damaged by arson fires so that the policyholders, and therefore their backers, could benefit from the insurance monies.

The banks and other financial institutions clearly have an interest and need to protect their investment. It is not suggested that there is any intent whatsoever by banks to create or provoke fraudulent arson claims. However, the interest of a bank is separate from that of the policyholder and coverage should not therefore be given by the insurer free of charge.

ADDITIONAL PREMIUM

As the insurers may in effect be providing coverage to a separate party, a separate premium should be charged. Either a full rate, or a reduced rate on a contingency cover basis, could be regarded as a reasonable return for the risk. The insurer may be providing cover to the bank even when the policyholder is thought to have committed a criminal act and is seeking to defraud the insurer. (Rec. I.14)

POLICY CONDITION

Not only could it be a separate contract but it could also be a contract with less protection for the insurer than that which exists between the insurer and the insured policyholder.

Could the insurer rely on policy conditions such as fraud, and insurer's rights *vis-a-vis* the bank?

PREMIUM PAYMENT

Replies from the banks indicated that if a policyholder fails to maintain the insurance required by the hank, the banks will effect such insurance themselves and charge the insured policyholder with the premiums. Considering that the bank is concerned with protecting its own interest the question arises as to why the insured should pay to protect the bank. A similar question is currently topical regarding the way that mortgage guarantee policies have been issued and paid for.

NOTING OF BANK'S INTEREST

It does not seem to be current practice for the policyholder to be asked at proposal form or renewal stage to give details on the extent of the hank's involvement.

Question 3 asked:

> Do you have a specific wording relating to your interest in the insurance policy?

Only one respondent confirmed that a specific wording was required. The other six responded in the negative although a frequently noted comment was that the interest of the bank should be endorsed.

Considering that the ABI/banks agreement implies that there is no responsibility on the insurer to endorse the bank's interest this seems to suggest there is an element of uncertainty.

CO-INSURED

In *Samuel & Co.* v. *Dumas* (1924)[28] Viscount Cave stated that:

> …if two persons insured under one policy had interests that were separate and distinct, the wilful misconduct of one would not affect the rights of the other.

In *Woolcott* v. *Sun Alliance* (1978)[29] it was stated that:

> …when more than one person is interested in property, these persons may insure under a single policy; both their interests and their potential loss differ, so theirs is not a joint interest or a joint policy: it is an insurance by two or more persons for their respective interest. In this situation, unlike that now under consideration, these persons are parties to the contract of insurance.

If therefore a bank becomes a named insured on the customer's policy, it is regarded as a co-insured and would not suffer from the wilful misconduct of its customer. However, in the USA such an innocent co-insured is prevented on the basis of public policy from recovering under an insurance policy if the insured has been fraudulent.[30]

Can the bank be regarded as an innocent co-insured? Should insurers allow the situation to continue where co-insureds are provided with this sort of protection in UK law? Would a change to the policy be appropriate

by clearly showing the insurer's intention to deny policy benefit to any party if the claim is fraudulent? Should UK insurers lobby for a similar public policy consideration to be applicable in the UK? If it is a separate contract then surely utmost good faith would apply and insurers should obtain a proposal form from the bank at inception and remind them of their duty to disclose material facts at each renewal.

NEGLIGENT BANKING

Consideration of whether the bank had lent in accordance with prudent banking procedures would also be worth considering. If a bank has lent without following proper and prudent banking considerations should the bank (the financial demands of which could perhaps have been the reason for a desperate act on the part of the insured) be entitled to benefit from fraud by the insured? This would surely allow the bank to obtain from the insurer more than it would have received from the insured as a customer.

Are insurers therefore at risk of underwriting the bank's trading risk? Should any failure to follow prudent practices be regarded as negligence on the part of the bank and therefore taken as a breach of utmost good faith by the bank?

INVOLVEMENT AT CLAIM STAGE

Question 5 asked if the bank would appoint a specialist to represent its interest at the claim stage. Three of the respondents indicated that they would consider appointing a public loss assessor in the event of a claim if the loss was serious or if the insurers intended to contest the claim. By providing and paying for a claims presenter, such an approach by the bank would clearly add financial support to the policyholder's claim. This could result in pressure on the insurer to pay or compromise the claim even though doubts existed about whether the policyholder was responsible for the fire.

Question 6 asked:

> To what extent would you become involved in the actual calculation of the loss payment under the policy?

In general the responses indicated that the banks would not become involved. One, however, indicated that it would rely on advice from the loss assessor and the bank's own insurance advisers and one suggested that it would only become involved in its capacity as mortgagee in possession.

LOSS PAYEE

Question 7 produced an interesting variety of responses. The question asked:

> Would you expect the insurance monies to be paid direct to you if the amount payable was equal to or less than the amount of your charge over the insured property?

Three responded affirmatively, although of these only one had such a procedure included in the wording of its legal charge. Two said that it would depend on the client's requirements and whether the sum was significant *vis-à-vis* the loan. One said that the money would be paid to the bank for the account of the customer concerned. One responded negatively stating that its interest only would be noted and that it would not have a charge over the policy.

There clearly seems to be a divergence of opinion and practice in the way that banks wish to see the claim monies directed.

Considering that past and present financial performance is regarded as an indicator of potential fraud, it is surprising that insurers have not taken steps to create a dialogue with the suppliers of finance with a view to assessing the financial health of the policyholders. This is even more surprising considering that in the event of fraudulent arson the bank may be able, depending on the policy architecture, to pursue successfully a claim for payment even though the insured policyholder is precluded from doing so.

Home Office

Financial loss can also result to the economy from fire damage and this is a problem for the Government to consider through the Home Office.

FIRE SAFETY

The Home Secretary is responsible to parliament for public safety including fire safety in England and Wales. He is the person primarily responsible for taking action against disturbing trends, such as arson, affecting fire safety. The Secretary of State for Scotland has similar responsibilities for fire safety to those of the Home Secretary.

It seems unlikely that the increasing trend in society for criminal damage and disregard for other people's property will, at least in the short term, be reduced by government action. Increased awareness of prevention and a greater emphasis on prosecution may help to improve matters in the medium term. As far as insurers are concerned it would perhaps be best to lobby the government for action while developing ways to cope with the increase in crime and the decrease in civic responsibility.

LOSSES TO THE ECONOMY

There is little information available regarding the loss to the economy through fire damage. A report suggested that it amounted to £144m. in 1973 (measured at 1971 prices).[31] Current figures are not known. It is in the interests of the economy as well as the 'public good' that the Home Office should be actively involved in reducing fire loss.

Additional recommendations

The following suggestions have been developed from information gathered during research for this paper:

1. Fire extinguishing appliances

A minimum level of appropriate fire extinguishing

appliances should be compulsory. Car drivers do not get a discount by fitting brakes to their cars! (Rec. 1.7)

2. Periodic reporting from insured

Certain categories of policyholder in particular classes of business and located in specified geographical locations should be required to produce quarterly reports detailing key factors relating to the performance of the business. (Rec. 1.8)

3. Overnight security

In view of the high proportion of fire losses that occur during the night, consideration should be given to increasing the level, extent and effectiveness of overnight protection of property by security guards and video-taped closed—circuit TV. (Rec. 1.9)

4. Audits—underwriting and claims

Internal auditors and reinsurers should conduct underwriting and claims audits on a more frequent basis than at present. (Rec. 1.10)

5. Approach to fraudulent claims

Insurers should consider the extent to which their shareholders, policyholders and reinsurers should be provided with information on how each company deals with the risk of fraudulent claims in general, and fraudulent arson in particular. (Rec. I.11)

5. DETECTION

Loss adjusters—historical

INSURANCE—CRIMINOGENIC

Fire insurance was said by Daniel Defoe to have originated in 1697.' It is therefore probable that shortly after the creation of fire insurance, claims were being submitted on fires started by, or on behalf of, the insured to claim insurance monies; a crime not previously known. Roger Litton has drawn attention to the criminogenic nature of insurance,[2] i.e., that it encourages crime which would not otherwise be committed in the absence of the insurance policy.

EARLY LOSS ASSESSMENT

Initially, insurance companies instructed their own staff surveyors to deal with damage and claims. This did not always prove successful. An extract from the records of London Assurance (3) recommended in 1776 the dismissal of their surveyor for: 'Submitting an estimate of damage by fire greatly exceeding both the estimate of the insured's own surveyor and the amount at which the claim was finally settled.'

The extract does not indicate the reasons why the surveyor proposed a high settlement although this can perhaps be left to the imagination!

The Sun Fire Office's regulations and instructions for their building surveyors, drawn up in 1792 and amended overtime, stated in 1844 (4) that the surveyor: 'will report to the Secretary the nature and probable extent of all fires which have occurred in buildings insured in this office ... and he will examine and assist in settling all claims on buildings in which this office is interested.

On receiving notice of a fire he shall attend immediately on the spot ... he must satisfy himself that the property is correctly described and insured to the extent of the damage it has sustained by the fire.'

PARTIALITY

As new fire offices developed during the nineteenth century, the claims settlement was dealt with not only by insurance company managers but also by agents. Claim certification was made difficult by a lack of impartiality in some agents and fraudulent abuses were also a problem.

Insurance offices began to use the services of auctioneers and appraisers to adjust losses, and in time they became known as assessors. It was not until 1873 that the insurance industry prepared a private and confidential list of approved assessors acceptable for the adjustment of fire claims. (5)

The heavy burden placed on the surveyors and assessors engaged by insurers has today resulted in a separation of the two main surveying functions. Underwriting surveys have generally remained 'in house' whereas adjustment of claims has evolved into a function sub-contracted to loss adjusters. It is interesting to observe that in recent years UK insurers have begun to reconsider this separation and to deal again 'in house' with certain claims—liability and small personal lines in particular.

DETECTION

It is possible that Sir Arthur Conan Doyle (1859— 1930) might have been aware of the loss adjusting profession, and perhaps it is a disappointment that he chose to make Sherlock Holmes a detective rather than an adjuster. However, during his 'life' Sherlock Holmes made many statements, some of which have interest and relevance to those involved with the detection of fraud and arson. A light peppering of thought-provoking statements by Holmes is contained in this paper for illustration purposes.

The Chartered Institute of Loss Adjusters (CILA)

In 1941 a formal grouping was established known as the Association of Fire Loss Adjusters. A royal charter was granted in 1961 when the association became the Chartered Institute of Loss Adjusters (CILA).

MEMBERSHIP

CILA has a qualified membership in excess of 1100 members (6) and a significant body of energetic, ambitious students. The smaller separate Insurance Adjusters Association was subsumed by the CILA through merger in 1992. This resulted in a single professional body representing individual qualified loss adjusters in the UK.

OBJECTS

Among the objects of the institute are:

> The advancement of the study of the profession of loss adjuster, the security of the association of those engaged in the profession and the promotion of the efficiency and usefulness of the profession by observance of strict rules of professional conduct by members of the institute and by establishing high standards of education and knowledge. (7)

The institute provides technical support to practising adjusters and an examination structure offering specialisations in the disciplines of building, financial, misappropriation, liability and contractors.

QUALIFICATION

The Associateship qualification (ACILA) is essentially a demanding second career examination as the minimum entry for admission to the finals is a professional qualification from one of a number of other related institutes. The candidate must also have completed at least one year's service with a firm in which one partner is a member of CILA.

ANTI-ARSON ROLE

In terms of arson detection and resolution the institute does not play a practical role, although it has organised at least two educational conferences of relevance to the subject. (9)

When the Home Office working group was producing its report on the 'Prevention of arson' it seems to have received evidence from only one firm of loss adjusters and did not receive evidence from the CILA as an organisation. Considering the significant role played by individual adjusters in all forms of arson claims the apparently limited input to the working group's study is surprising.

Individual members are involved in the investigation of fire claims and a confidential system exists of circulating details of suspect claimants between loss adjusting firms and some insurance company claim departments.

The institute liaises with interested parties but in general it is individual loss adjusters and their companies that develop particular styles and approaches to the investigation of claims arising from arson.

INCREASED PARTICIPATION

There are several areas where CILA could perhaps play a more involved part with regard to fraudulent arson claims:

Operation of a database
This would enable individual adjusters to lodge details of claimants, although this may prove to be unacceptable under data protection and more importantly create competition between insurers as well as between adjusters. (Rec. II.1)

Improved training in investigation methods
Considering the income earned by loss adjusters through dealing with claims on fire policies it is surprising to note the relatively small percentage of time and expenditure allocated to CILA for the development of investigation expertise. Training for adjusters to deal with the particular problems of fraud claims arising from fires especially those where arson by the insured is suspected is lacking at institute level. The examination syllabus should be extended to include formal fraud and fire investigation training. (Rec. II.2)

Identification
The introduction of a photo—identity card system for all qualified loss adjusters would enable other organisations such as the police and fire brigade to recognise the bona fide occupation of the individual carrying the card. (Rec. II.3)

Fire liaison panels
A determined effort should be made so that a CILA representative can sit on each and every fire liaison panel in the UK. The panels comprise representatives from bodies such as the police and fire brigade as well as insurance companies. (See chapter 5.) Adjusters would then have the opportunity to communicate, disseminate information, and help to avoid communication barriers and problems. (Rec. I.4)

Impartiality of the loss adjuster
The impartial, independent approach is a fundamental rule of the CILA code of conduct which states: 'A loss adjuster must at all times preserve impartiality.' (9)

ULTIMATE CORPORATE OWNERSHIP

Almost 60 per cent1° of chartered loss adjusters work in adjusting organisations where the final ownership is not wholly or largely held by the UK adjusters themselves:

Owner (in full or majority)	*Approx. % of total membership*
Lloyd's syndicate	5
Reinsurance companies	20
Bank and other financial interests	17
Overseas adjusting or surveying companies	17

These figures are based on press articles and announcements as CILA itself could not provide the information. The figures do not, and may not need to, include a recent MBO of a large firm as details of the structure, ownership and control have not been ascertained at the time of completing this work.

CILA does not regard this outside ownership as a problem because it is an institute of individual members. It is therefore up to each member to maintain his or her impartiality at all times.

ROLE

The institute's publicity brochure11 outlines the role of the adjuster as representing the fund and interests of all the policyholders who have paid premiums to the insurance company that instructed the adjuster.

> Detection is, or ought to be, an exact science and should be treated in the same cold and unemotional manner. (12)

An adjuster's approach should involve the exercise of impartial scepticism; keeping an open mind and constantly reassessing all the information coming from the investigation. The adjuster must show professional concern and courtesy while pursuing all necessary enquiries. Awareness of the customer service aspect of claims handling must be constantly maintained and a balance achieved.

IMPARTIALITY

Alan Cleary, a past president of the Chartered Institute of Loss Adjusters in a press interview during his year of office in 1981 stated that:

> Loss adjusters are people of an independent point of view and the firms to which they belong are firms which are independent (in a financial sense) of their instructing principals but 'independent' is a word

> which does not do justice to what adjusters really are. 'Impartial' is the word you want. It's the impartiality of the chartered loss adjuster that picks our profession out from any other I can think of. The adjuster preserves his impartiality at all times, favouring the interests of neither insured or insurer. If, in any particular case, circumstances arise which might he seen as likely to impair the adjuster's impartiality, the adjuster declares this state of affairs to his instructing principal before proceeding. By instructing adjusters, insurers are providing not only a service for themselves but a service for their policyholders and I think this is all too often forgotten.[14]

The current realty is no longer as outlined above. Some adjusting companies are not now 'independent' according to the definition because they are no longer financially independent from an insurer or reinsurer.

Independent should mean that a CILA qualified member must not undertake adjusting assignments on behalf of the owner of his or her firm, if that owner is also the insurer or reinsurer of the claim under review. This means that the member should find out whether the owner of his or her firm has an interest in each claim, e.g., as reinsurer, banker, broker, shareholder of the insured, etc.

At the least, if such a state of affairs did exist it should be declared to the insured who could then form a view on whether the exercise of true impartiality will occur. This is also an area where brokers may be required as agents of the insured to be sure that their principal's claim will receive impartial assessment.

INTERESTED PARTIES

In addition to providing a service to the insurer and the policyholders the adjuster should also recognise that the following are often dependent on the way in which the claim is dealt with:

- reinsurers;
- insurance company shareholders;
- names supporting a Lloyd's syndicate;
- insurance broker.

FRAUDULENT ARSON

In the context of a fire claim the adjuster must be conscious of the possibility that the insured may well have arranged for the fire to have been started to obtain insurance monies. Differences in style and approach by adjusters can often result in an innocent insured feeling that he or she is being regarded as guilty. This will no doubt lead to complaints to the insurer. A guilty insured may also complain and threaten adverse media publicity to the point where an insurer agrees to a reduced level of investigation or early payment. This situation can seriously impair the progress and likelihood of success of the adjuster's investigation to the detriment of the insurer's funds. The result is often an adverse effect on the value of the policyholders' fund, shareholders' interests and reinsurers' financial health.

The insurance industry is not consistent in its response to complaints and the phrase 'pay up to shut up' is not as rare an instruction as may be thought.

POLICYHOLDER'S PERCEPTION

Little has been done by CILA or insurers to explain to policyholders how a claim will be dealt with. Unfortunately the public's understanding of a loss adjuster is generally that he is a professional engaged so that the insurer can avoid liability or reduce the claim by as much as possible.

Adjusters must pursue a broad range of enquiries during a fire claim investigation with the support of the insurer and the understanding of the insured. General publicity, possibly in terms of a statement of practice for claims investigation issued by the ABI, could help. It would explain the procedure and help reassure the innocent insured while setting out clearly to the guilty the approach that will be applied to his claim. (Rec. I.5)

Service aspect of adjusting

> The punishment of a criminal is an example to the rabble; but every decent man is concerned **if** an innocent person is condemned.[15]

OBSTRUCTION BY THE INSURED

The contractual relationship between the insurer and the insured must be respected. However, any obstruction by the insured to a detailed information gathering exercise should be brought to the insurer's attention and instructions obtained.

GENUINE OR FRAUDULENT?

Several insurers provide service standards to their clients. These are generally measured in terms of response times and give a commitment to speed of settlement.

There is a conflict between an insurer's desire to provide a prompt and trouble-free claims settlement service with the need to avoid paying fraudulent or exaggerated claims. Insurers as a body do not seem willing to grapple with the conflict and it therefore rests with individual insurers to decide how they intend to approach the conflict. Indeed, differing circumstances can cause the same insurer to adopt different standards depending on the size of claim, the historical relationship with the insured or broker, the extent of recovery available from reinsurance, and so on.

STATEMENT OF PRACTICE

It would be helpful for a loss adjuster to be able to refer the insured to a statement of practice. Such a market document should give reassurance that the approach being adopted is in accordance with market practice. (Rec. II.5)

Emphasis on the steps required to confirm authenticity and valid coverage would perhaps he more appropriate than listing all the possible areas of suspicion. Insurance brokers, loss assessors and other intermediaries could also he referred to the proposed statement of practice and this might reduce the extent of broking and tactical pressures placed on adjusters

and insurers during the early stages of a fire investigation.

There is a possibility that if such a statement is too detailed then a fraudulent insured will be able to create the facts in advance of the loss to fit the investigation. Sections worded in general terms detailing the steps required for an insurer to process a claim should solve more problems than they will create.

HOSTILE AND AGGRESSIVE APPROACH?

The conflict between a service-orientated claims handling approach and a detailed fraud detection approach is recognised in Michael Clarke's paper 'Insurance fraud' 1989[16] However, he refers to the fraud detection approach as being: 'Complex, slow, and hostile.' The approach need not be seen in any way as hostile providing the explanation given to all claimants is that a certain set of enquiries have to be completed to satisfy the insurer that the claim should be paid. If every insured recognised at the time of a claim that they were being dealt with in an identical fashion to all other claimants then the innocent insured should not feel disturbed. However, the guilty insureds may well, through complaining and mock indignation, serve to identify themselves as such.

Michael Clarke refers to 'an aggressive policy on doubtful claims'[17] The approach should be detailed, yet sensitive and polite. The answer to addressing doubtful claims is in developing communication between the insurers and their clients.

International loss adjusting

Adjusters operate internationally where the problems become even more complex. Some loss adjusting companies have offices overseas, and members of CILA are often at the centre of major insurance loss investigations throughout the world.

PAROCHIAL?

Despite the internationalisation of what is only a small percentage of the members, CILA is generally regarded as being principally concerned with the UK.

There is an Australasian division and liaisons do exist with other adjusting associations overseas. However, the examinations tend to be based around subjects which only someone who has lived and worked in the UK could fully understand.

EUROPE

In Europe CILA is a member of the Federation of the European Loss Adjusting Experts (FUEDI) and in time it is envisaged that loss adjusting experts in one country will be able to gain recognition in another. The UK adjusting system is, however, fundamentally different from that in Europe where insurers retain closer control of claim handling and policy liability decisions. Linguistic and legal differences present considerable challenges for which CILA and many of its members do not seem prepared.

SYLLABUS GAP

The farther afield that adjusters have to travel the more they are left in a situation of self-reliance. For example, it is easier (and less expensive) to request a forensic scientist to visit a medium-sized fire claim in Surrey than it is to request that a special visit be made to a factory located in an outlying city in South America. To develop and continue to export the UK adjusting approach greater emphasis should be placed by CILA on developing training and examinations in specialist investigative skills. (Rec. II.2)

A recent positive development is the introduction, currently at an experimental stage, of a continuous professional development scheme for qualified adjusters. Early indications suggest that the scheme will not be sufficiently challenging and will not address the issues of fire cause detection and fraud investigation.

INTER-AGENCY INVOLVEMENT

Internationally the approach towards fraudulent arson varies. In certain US states, loss adjusters are part of arson investigation teams where full co-operation exists between all the related services. In France the insurance industry funds an anti-fraud organisation[18] which has specialist fire investigators on call at the request of an insurance company to work with the adjuster. No such organisation exists within the UK although as discussed in chapter four this is possibly a function which the Arson Prevention Bureau could develop and operate.

Arson detection by the adjuster

INVESTIGATION

> How often have I said to you that when you have eliminated the impossible, whatever remains, however improbable, must be the truth?[19]

This essay does not purport to be a work of technical reference providing detailed information on fire cause investigation. A number of publications dealing with fire science, cause investigation, and investigation in general, are available.[20]

Courses are run at several academic establishments in the UK dealing with fire science and cause investigation.2' Essentially the adjuster's assessment of the cause should involve a consideration of all natural and common causes of fire.

ADJUSTER DEVELOPMENT

Claim assignments are allocated within an adjusting office according to the level of experience and qualification of individual adjusters. The size and complexity of a claim will decide the level of experience and seniority required. Just as auditors delegate basic checking to trainee accountants so adjusters train their staff by exposing them to claims on an ever- increasing level of size and complexity. Given sufficient time and on-the-job training a loss adjuster will develop an ability to become suspicious about one or more

aspects of a claim. During this period of learning, however, the adjuster will need to be closely supervised by a senior adjuster. Occasions will doubtless arise though when the adjuster is involved in a claim and useful information is either not gathered or not even noticed. However conscientious senior supervising adjusters may be, they may not be aware of these omissions. As already mentioned there appears to be inadequate examination training for loss adjusters in the UK in terms of fire investigation or fraud Investigation. (Rec. II.2)

FRAUD INVESTIGATION

Following numerous interviews with loss adjusters in the

UK, Michael Clarke stated:

> Whilst adjusters are universally emphatic that they pursue fraud when they find it, and that they develop a nose for it with experience, there is evidently no material incentive **to** find it, and some disadvantages in the structure of their situation to its detection and effective pursuit. Also there is nothing in their professional training examinations which prepares them specifically in fraud detection and control.[22]

He also recognises that:

> Adjusters accept an explicit responsibility to be alert to the signs of a fraudulent claim. Accountants, by comparison, maintain that their concern with an overall evaluation of the company means that compliance work cannot be undertaken simultaneously as quite different methods of evaluation are required.[23]

FIRE INVESTIGATION

It would seem that the last technical paper on fire investigation issued under the auspices of CILA was 'Determining the supposed cause of fire' by E. F. Cato Carter in March *1955.*

The problem is that 'book knowledge' is only part of the training process. Forensic scientists undergo a period of on-site training with a senior scientist before they are considered able and competent to undertake investigations on their own. The author would not wish to give the impression that in terms of fire cause detection in the UK loss adjusters are not effective or accurate. However, it could be argued that the process is more 'enthusiastically amateur' than 'profession ally trained'. At the thirteenth CILA educational conference in 1991 a workshop on arson was advised by a forensic scientist, Peter Cook,[24] of two cases which involved the complete misreading of the fire scene by the adjusters concerned.

The first related to a house fire:

> …where the occupant had been charged with arson because the fire scene indicated that there had been multiple seats of fire. However, after analysis of the way the fire spread occurred there was evidence to show that there had only been one seat of fire.

The second related to a fire in a commercial building:

> ...which the adjuster had considered to result from a fault in the BT telephone control panel. Investigations, however, indicated that the fire had started close to the storage point of the insured's accounting and VAT records. A reconstruction of the remains of carpeting and contents indicated that an accelerant might have been used and subsequent testing confirmed this suspicion. The claim was then repudiated.

CONFLICTS AT THE SCENE

The responsibility placed on the adjuster is heavy. The results of a fire investigation depend on site preservation and evidence integrity. However, these factors conflict with the demands often forthcoming from the insured in terms of agreeing to salvaging operations and debris removal. Pressures arising from requests for payment on account and business interruption considerations must also be attended to at a time when the adjuster is still not in a position to confirm that the fire has arisen fortuitously without any involvement by the insured.

PARTIES INVOLVED

The number of interested parties is considerable and the adjuster maybe involved with all or some of them:

- fire brigade
- forensic accountant
- forensic scientist
- Heath and Safety Inspectorate
- insured
- insured's accountant
- insured's broker
- insured's customers
- insured's suppliers
- landlord
- police
- representative from bankers
- tenants
- third parties and their insurers and adjusters
- utilities
- VAT inspector.

LIABILITY AND QUANTUM

During the claim assignment there are essentially two questions that an adjuster needs to answer:

—Is the loss covered by the policy? and, if so

—How much should be paid? (25)

Other considerations such as possible recovery aspects are involved but for the purposes of fraudulent arson it is the first question which must be addressed.

FRAUD INVESTIGATION TRAINING

Police officers undergo training in recording statements and the psychological aspects and practical techniques of interviewing. Though not seeking to demolish the investigation credentials of experienced loss adjusters, it may be that CILA members, students and insurers should require a greater level of investigation training across the board as part of the increased effort to detect fraud, whether arising under a fire policy or indeed any other policy of insurance.

FINANCIAL INVESTIGATION

Similarly the adjuster is often required to decide

whether a forensic accountant should be called in to review the financial state of the insured company. At least from this point of view the adjuster may be prepared, as CILA's educational syllabus does include subjects relating to accountancy and business interruption.

FORENSIC SCIENTIST

The adjuster is urgently required to form a view as to whether specialists will be needed to assist in the investigation. Therefore the somewhat bizarre situation arises where an adjuster without formal training in fire investigation has to decide whether the cause of the fire is such that a forensic investigation is required.

If the adjusters rely on the fire brigade they may wait several days before being advised of the supposed cause. By then the information to support the finding by the brigade may not be sufficient to enable a satisfactory defence to be prepared on behalf of insurers.

Articles and letters to the insurance press often suggest that adjusters must decide whether or not there is reasonable suspicion to suspect the insured of starting the fire before appointing a forensic scientist. In view of the specialised nature of fire investigation it is probable that adjusters are not competent to decide on all occasions whether the cause or circumstances of the fire are in any way suspicious.

In an article[26] by the 'loss adjusting correspondent' of *Policy Holder* in 1982 three areas of improvement were suggested including:

> Positive action, following the *recognition* that arson has occurred, *by* the adjuster and his principals necessitating an early involvement of solicitors, the involvement of 'experts' both with regard to the forensic side, and possibly accountancy.

Although 'recognition' is a crucial trigger, the loss adjusting correspondent does not mention how the loss adjuster should recognise that arson has occurred.

CAPABLE ADJUSTERS

It is not disputed that many practising loss adjusters have by means of experience and private study developed the capability to recognise arson. What is not clear though is how an insurer can identify such adjusters.

Furthermore, who pays for any mistakes during the period while the adjuster gains that experience?

Investigations

QUESTIONING

> And when they heard the voice of the Lord God walking in paradise at the afternoon air, Adam and his wife hid themselves from the face of the Lord God, amidst the trees of paradise. And the Lord God called Adam, and said to him: Where art thou? And he said: I heard thy voice in paradise: and I was afraid, because I was naked, and I hid myself. And he said to him: And who hath told thee that thou wast naked, but that thou hast eaten of the tree whereof I commanded thee that thou shouldst not eat?[27]

This is one of the earliest references to investigation. When God questioned Adam in the Garden of Eden as to why he was hiding and embarrassed by his nudity, He practised one of the classic strategic approaches in that He already knew the answer. Adjusters will not know the answers to all the questions being put to the person being interviewed but should follow a logical sequence based on some knowledge of the facts. The adjuster should be aware of basic interviewing techniques and the legal considerations that apply.

The purpose of an investigation is to enable the truth of the matter to be established, and if the result is that fraudulent arson is detected then the information gained during the investigation must be suitable for use as evidence.

There are various publications available providing guidance to investigators, many originating from the USA.[28] The Insurance Crime Prevention Institute in America has produced a useful guide of 'Arson-for- profit indicators'.[29]

Loss adjusters are not required to study formally investigation techniques, statement recording procedures or any aspects of psychological assessment. (Rec. II.2a)

OTHER SPECIALISTS

> *Salus ubi multi consiliarii—Where* there are many advisers there is safety

The adjuster should involve specialists, such as forensic scientists, solicitors, and private inquiry agents, when appropriate to assist in investigations and to advise the adjuster and insurer. The use of independent accountants is currently fashionable and several adjusting firms also have accountants on their staff actively involved in claim assessment.

There seems to be a minimal use of independent marketing consultants. This is surprising considering that they can provide information on the markets in which the insured operate. Information can be gained on the opportunities and threats to the insured business not just in the country where the loss occurred but also internationally.

AREAS OF INVESTIGATION

Investigations by the adjuster can he considered under the headings of cause, motive, opportunity, means of investigation and extent of loss.

Cause

The cause investigation will involve the adjuster in forming an early view on whether a forensic investigation should take place. However, the adjuster should not lose control of the cause investigation. team approach with the adjuster and the forensic scientist working closely together will enable the forensic scientist to gain the information required while at the same time enabling the loss adjuster to maintain full awareness of the cause investigation.

Motive

Cui bono?—\Who stands to gain?!

Considerable thought and enquiry needs to be exercised. Possible motives with regard to arson by the insured include:
- reduced performance of business;
- requirement to upgrade machinery;
- requirement to change and modernise premises.

It is advisable to secure the accounting records as soon as possible. The insured company's insurance files should be located not only for the current period of insurance but also for the previous three years or so. These files will enable the adjuster to gain a picture of the insurance history and the extent of coverage. Any discrepancies between the insured's copy of the current policy and the information from insurers should therefore be identified at an early stage. Previous correspondence and policies will also assist in producing information relating to sum insured levels and claims history.

Opportunity

The adjuster's investigations can be of vital importance not only in terms of the insurance claim but also to support the police investigation. Close and careful questioning of all parties together with detailed enquiries into any significant changes in behaviour must be conducted.

The police may be able to give assistance from their records and knowledge. Police records are in two parts. The first contains details of actual convictions. This information can usually be obtained on the request of any individual to see his or her own record. The individual completes a police form. In due course the police write to the individual and confirm that a print-out of the criminal record, or a nil-return, is available for collection from the station.

Inappropriate underwriting and claim circumstances it is suggested that insurers and adjusters should ask individuals in the insured company to produce a current copy of the police print-out. This procedure would confirm the situation with regard to disclosure, and could also be of wider application (e.g., fidelity guarantee proposals and claims). Due consideration should, however, be given to the effect of the Rehabilitation of Offenders Act 1974 on any convictions revealed. (Rec. II.6)

The second part of the police records relates to 'intelligence' information. This is not available to the public but is of considerable help to the police in their ongoing detection work. Details of known associates, suspected activities and soon are collated and available for police reference. Such information is clearly sensitive and confidential and its actual existence can produce allegations of a 'police state'. If the adjuster is able to develop a confidential and trusting relationship with the police then the opportunity of being guided in certain directions will undoubtedly present itself.

The issue is extremely sensitive but potential fraudulent arsonists should be aware that if they are already known to the police then that information may well enter the domain of the adjuster's knowledge. It is clearly of paramount importance that any information received in such a fashion is dealt with confidentially by the adjuster. It should serve to point the adjuster in the right direction rather than form the basis for rash comments or premature and unsound policy repudiation.

Means of investigation

The means used should serve the detection as well as resolution aspects.

A full photographic record should be secured shortly after arrival at the site, but this information should not be relied on to the detriment of scene preservation. This is especially important where minute objects of considerable significance such as electrical wiring and particles contaminated with accelerant may still be in the debris.

If possible a video recording should be made at the earliest opportunity. At the time of such recording the significance of the areas being recorded may not be clear. However, if a full video record is prepared it can be referred to as other information becomes available during the investigation.

Statements recorded in writing at the scene as soon as possible after the incident with careful attention to timings and whereabouts should prove to be most helpful. (See section 5.10 for further discussion.)

Extent of loss

Site preservation will not only enable a comprehensive forensic investigation to proceed but also produce valuable information relating to the quantities and quality of property destroyed or damaged in the fire. As a forensic investigation proceeds the adjuster should 'shadow' the forensic scientist and produce a plan indicating the identity, potential quantity and any identifying features of the debris. A particular characteristic of fraudulent arson fires is that substandard or out-of-date stock has been placed in the building and quite often sufficient identifiable debris is available to reveal inconsistencies when the claim is submitted.

RESERVATION OF INSURER'S RIGHTS

From the moment they are instructed to deal with a claim adjusters will be faced with pressures from all directions. The insurer will want to know whether the claim is genuine and what reserve should be established. The insured will be pressing for advice on salvaging and interim payments. Until such time as the investigations produce an indication as to the cause and involvement of the insured it is recommended that the insured be advised that the adjuster's involvement does not affect or waive insurers' rights under the policy. This is a particularly popular and important feature of investigations conducted in the USA and the following is a standard reservation of rights letter which adjusters there are recommended to issue at the outset.

> We wish to advise you that we have been requested by the XYZ Fire Insurance Company to investigate

the facts and circumstances of the loss alleged to have been sustained by you on the 15th day of March, 1992 to the property located at 212 Main Street, Any Town.

We are proceeding to obtain the information and your co-operation will facilitate our efforts. In making this investigation, all the conditions specified in the policy are expressly reserved and the rights of our client are not to be deemed waived in any way.

In the event that the adjuster finds a very strong question of Ii ability or breach of condition is clearly in existence, then it is a recommended practice in the USA to procure a non-waiver agreement at once.

Any insured, whether innocent or guilty of starting the fire, will undoubtedly feel an amount of concern on receipt of such a letter. The innocent insured could be worried regarding possible lack of coverage as a result of 'small print' whereas the guilty insured will recognise that a full investigation is going take place which may well result not just in lack of claim payment but also possible criminal proceedings. The adjuster should therefore liaise closely with the insurance company which should provide co-operation and support.

Insurance intermediaries should recognise the necessity for a reservation of rights letter and reassure the insured as to the need for an investigation.

COLLATION OF INFORMATION

Until recently the collation of information relating to evidence required a considerable amount of photocopying, paper shuffling, scheduling and listing. Recent developments in software have produced programs capable of collating and cross referencing for criminal cases.[30]. Although some use is made of relational software, there is not as yet a software program available off-the-shelf specifically for loss adjusters to input and analyse information obtained during an investigation. (Rec. II.7)

Taking possession of premises and property

Insurance policies contain a condition often termed 'Insurer's rights following a claim'.

TYPICAL WORDINGS

There is no standard wording. Three different wordings are given below:

The Company
(i)(a) may start, take over, defend an conduct any legal action in the name of the insured, or prosecute in the name of the insured, for its own benefit any claim for indemnity or damages and shall have full discretion in the conduct and settlement of any such action.
(b) may enter any building where loss or damage has occurred and take possession of the building and take and keep possession of any property insured by this policy but the insured may not abandon property to the Company.
This policy shall be proof that the insured have given the Company authority to exercise its rights under this condition.

#
On the happening of any *damage* in respect of which a claim is made the Insurer and any person authorised by the Insurer may without thereby incurring any liability or diminishing any of the Insurer's rights under this policy, enter take or keep possession of the premises where such damage has occurred and take possession of or require to be delivered to the Insurer any property insured and deal with such property for all reasonable purposes and in any reasonable manner. No claim under this policy shall be payable unless the terms of this condition have been complied with. No property maybe abandoned to the Insurer whether taken possession of by the Insurer or not.

On the happening of any loss, destruction or damage in respect of which a claim is or maybe made under this insurance the Insurer and every person authorised by the Insurer may without thereby incurring any liability and without diminishing the right of the Insurer to rely upon any conditions of this insurance enter take or keep possession of the building or premises where the loss, destruction or damage has happened and may take possession of or require to be delivered to them any of the property hereby insured and may keep possession of and deal with such property for all reasonable purposes and in any reasonable manner. This condition shall be evidence of the leave and licence of the insured to the Insurer so to do. If the insured or anyone acting on behalf of the insured shall not comply with the requirements of the Insurer or shall hinder or obstruct the insurer in doing any of the above-mentioned acts then all benefit under this insurance shall be forfeited. The insured shall not in any case be entitled to abandon any property to the Insurer whether taken possession of by the Insurer or not.

PURPOSE

The reason for this condition is generally explained as being to the benefit of both the insured and insurers in terms of damage minimisation, salvaging, etc. However, an important purpose as far as the adjuster is concerned is that this condition can be used to support action to:

— secure the premises;
— gain access to all such property that is required for a full and objective investigation;
— establish any involvement of the insured.

POST-LOSS SECURITY

It is not uncommon for a repeat attempt at fire raising to take place, especially if the first attempt was not as successful as it could have been. (31) The adjuster should decide quickly whether the premises needs to be secured to protect it not only against strangers but also from the insured or his agents. In appropriate circumstances premises can be sealed by means of padlocks, etc., and an outside security company can be engaged to provide 24-hour guard patrols.

DOCUMENTATION

By virtue of this condition the insurer and adjuster

have in certain respects greater powers than the police to trawl through documents to discover whether they are relevant. At the earliest opportunity documentation should be examined to assist in assessing the status of the insured company, personnel policies and problems, and order book and general matters that will become apparent during a review of papers. It should be established whether the condition and prospects of the insured company were such that, in the absence of the fire, proper and healthy trading could have actually continued.

> Deus ex machina—An unlikely and providential intervention. An unexpected occurrence that rescues someone or something from an apparently hopeless predicament!

USEFUL INFORMATION

Accounting and management information that could be useful includes:
- audited accounts
- auditors reports and correspondence
- bank statements
- board meeting minutes
- budgets
- bank debentures and guarantees
- cash flow forecasts
- company register
- creditors
- cashbook
- correspondence with authorities over corporation tax, PAYE and VAT
- cheque book counterfoils
- debtors
- paying in book counterfoils
- payroll summaries and records
- stock check papers.

COMPUTER DATA

Use of computers by many businesses means that early steps should be taken to secure details in computer memory, if necessary by removing hard copy or disks. Details of back-up and off-site storage procedures should be obtained.

At all times the integrity and chain of evidence should be maintained.

DELAY

> *Periculum in mora*—Danger in delay.

Any resistance from the insured encountered by the adjuster could be interpreted firstly as failure to comply with the condition resulting in loss of the right to claim, and/or secondly as a tactical refusal to gain time. This time could be used to falsify information which would then be provided to insurers.

Such delaying tactics are adopted by insureds even when advisers are involved to assist in the claim preparation. Adjusters and insurers should be conscious of the activities that may be taking place, during such delays, which could strengthen the insured's case possibly through falsification or destruction of crucial evidence and documents.

Security of the premises

An important aspect to be considered is the security of the premises, under normal circumstances and at the time of the loss.

DETAILED ENQUIRY

At the earliest moment the adjuster should establish details of all possible entry and exit points not only to the building in which the fire occurred but also to the site in which the building is located.

Details should be obtained of all key holders as well as all alarm or access system code holders. These people should be interviewed as soon as possible. Statements recorded during the interviews should then be signed by interviewee and interviewer. Neighbours and attending fire brigade and police officers should be questioned regarding the condition and operation of the premises normally as compared with what was observed at the time of the fire.

Details of the theft insurance coverage can be of considerable interest especially with regard to security recommendations and warranties. Co-operation from the theft insurer should be sought for obtaining access to any survey reports that may have been prepared and alarm specifications that may have been supplied. If the fire insurer also insures theft then this information should be more readily available.

LEGAL VALUE

The existence of good security measures was raised in Watkins v. Legal & General (1981)[32] where the insurers described the premises as 'virtually a fortress' with the only explanation being that the fire was started inside.

In *S & M Carpets v. Cornhill* (1982)[33] the insured's shop manager left the premises and locked the door and there was no suggestion raised in the case that entry had been gained by strangers.

In the recent case of *Blackmans Glass v. NZI*[34] the actions of the insured's directors in relation to the presence of an intruder alarm within the premises were central to the success of the insurer's defence.

RECONSTRUCTION OF EVENTS

The following can provide important information to assist a reconstruction of events, verification of fire development and spread, timings in general and security in particular:

- alarm devices and circuitry;
- clocks, flexitime/clock card systems;
- vehicle tachographs;
- premises and mobile telephone call sheets;
- electrical wiring and fuses;
- memory chips in alarm and other control panels;
- debris and partly damaged property;
- fire brigade, police and central station records.

Care should be taken to avoid prejudicing the integrity of anything that might be used in evidence.

Statements

Significant information relating to security should be included in the statements, which must be recorded as soon as possible.

SEARCH FOR THE TRUTH

> *Mendacem memorem esse oportet*—It is fitting that a liar should be a man of good memory.

The recording of detailed statements from all possible parties and witnesses is of paramount importance in finding the truth and identifying lies and inconsistencies.

All directors and senior managers of the insured company should be identified and interviewed, as should all key holders and alarm access code holders.

USA

Adjusters in the USA are able to conduct interviews with the insured under oath where each party is represented by an attorney. This provides an insured with some protection but also allows for a detailed statement made under the gravity of an oath.

Use of a lie detector is also a feature of investigations in the USA although the results are regarded as inconclusive and not legally acceptable as evidence.

PARTIES FOR INTERVIEW

Parties to be considered for interviews would include:

- directors and staff of the insured company: home addresses, previous occupations and address, other directorships and employments running concurrently, basis of shareholding and remuneration;
- previous staff: including reasons for dismissal and last known address and occupation;
- insured's broker
- insured's accountant
- insured's auditor
- insured's shareholders
- other companies connected by shareholding
- Health and Safety Executive
- security guards
- sub-contractors: who may have been on the remises at the material time or previously;
- other visitors to the premises: who could independently confirm details such as smoking arrangements, stock heights and layouts, machinery operations, lighting layouts, etc.;
- fire brigade officers: especially the officer that attended first;
- police and scene of crime officer
- Companies House: for details of the company;
- information agencies: who can provide additional information relating to the insured as well as any judgments that may have been made against the insured company.
- neighbours
- local authority
- landlord
- customers
- suppliers
- competitors.

MOVEMENTS AND TIMINGS

> *Non semper ea sunt quae videntur*—Things are not always what they appear to be.

Detailed accounts of movements and precise timings recorded as soon as possible after the incident can be compared against other witness accounts and produced at a later stage as part of the circumstantial evidence. Timings can be crucial and a detailed and patient enquiry should take place to establish a precise chronological sequence of movement and whereabouts. Timings were important in cases such as *Broughton v. CU,*[35] *S & M Carpets v. Cornhill,*[36] *Polivitte v. CU*[37] and *Blackmans Glass v. NZI.* [38]

A standard pattern of handwritten statement recording should be agreed on by the adjusting team with key times and locations being constantly collated and reviewed, possibly with the use of relational software. (Rec. II.7)

Interviews conducted in separate rooms at the loss location simultaneously by members of the adjusting team should help to reduce the risks of collaboration. However, a carefully prepared story could make detection difficult. Use of tape recording would assist subsequent assessment of information and attitudes.

DIPLOMACY AND TACT

It should be recognised that statistics indicate that the majority of arson claims by value are not thought to result from a deliberate act or connivance by the insured. (See Chapter 6.) Therefore the approach in recording such statements requires tact and diplomacy. Insureds, as well as brokers, and loss assessors acting for the insured should therefore recognise the need to protect insurer's funds from a fraudulent claim and support a fair but detailed interviewing phase. The recording of statements should bean essential element in the initial investigations section of the suggested statement of practice. (Rec. II.5)

WITNESS CREDIBILITY

When recording the statement it is important to observe critically the behaviour of the person being interviewed, bearing in mind the importance with which the court will consider the credibility and performance of that person in the witness box.

In *Watkins v. Legal & General*[39] Neill, J, stated that:

> I found Mr Watkins an unsatisfactory and unconvincing witness and I am unable to base any finding on his evidence. He is no doubt an able and quick-witted man, but he did not create a good impression in the witness box.

In the Privy Council case of *Tricanipillay* (1990)[40] account was taken of the 'inherent improbability that a man of good character and mature years would resort to such a wicked act as to order his employee to set fire to an occupied building for such a motive' (to remove an unwanted tenant).

In *Broughton* Simon Brown, J, found that two aspects of the insured's manager's evidence coupled with the general impression of him in the witness box left him

ultimately with the clear impression that he must be regarded as an unreliable witness whose evidence he could not accept.

The two aspects of evidence were the time of his departure from the premises and inconsistencies from him relating to the possibility of an electrical fire.

In *Blackmans Glass* the evidence of a senior employee of the insured was found to be 'wholly unconvincing'. Herrod, QC, found that:

> Throughout his appearance in the witness box he was highly nervous and I had difficulty in determining whether this nervousness was due to the experience of giving evidence in Court or because he knew he was not telling the truth.[41]

The adjuster must realise that at the time of recording the statements the significance of timings, activities and whereabouts may not be at all clear. However, as the general and forensic investigations proceed, and theories are produced on the starting of the fire, the time details provided in the statements may assume significance. Considering that a fire can take hold in a matter of minutes, statement recording should be on a minute-by-minute basis with common sense being applied to the time grouping, e.g., five minutes doing x, 20 minutes doing y, etc. The location of activity x and y and witnesses to the activity should also be recorded.

FURTHER TRAINING

Adjusters may need training and examination in the psychological aspects of personality assessment and interviewing techniques rather than just relying on gut feeling developed through practice. (Rec. II.2)

Claim form

The claim form should be completed as soon as possible and signed by the insured. Policyholders are often reluctant to complete the form immediately as they may feel that it is not possible to quantify the loss. However, a claim form completed and signed confirming the circumstances and nature of the loss should be obtained even if the amount claimed section is completed marked 'information to follow'.

DETAILED QUESTIONS

The extent to which insurers are willing to seek detailed underwriting information from the insured varies from oral details to a fully completed proposal form together with supplementary information. If a proposal form is not on their file, insurers might wish to ask detailed questions in the claim form which they would have asked in the proposal form had such a document been completed by the insured. Even if a proposal form is on file the extra questions on the claim form could serve a verification purpose. Examples of claim form questions could be with regard to:

- previous insurers
- previous claim experience
- directors
- managers
- shareholders
- key holders
- name of bankers.

A request for the claim to be sworn under oath can also be a test of the insured's determination and faith in the claim.

Documentation, statements and the claim form will prove to be of vital importance during the investigation if the claim proves to be fraudulent.

Fraudulent claims

INSURERS UNDER PRESSURE

Fraud is a problem for insurers but the extent and cost is not at all clear. Fraud against insurers is a criminogenic problem which would not exist in the absence of insurance.[42] Considerable pressure has been applied in recent years in an attempt to force insurers to reduce the protection available to them under the utmost good faith doctrine. For example, personal lines insurance in the UK is now subject to a statement of practice (appendix E) restricting the opportunity for an insurer to use defences of nondisclosure or breach of policy condition when not relevant to the loss in question.

PUBLICITY

An apparent reluctance by insurers to become exposed to publicity, and also perhaps to make competitors and investors aware of fraud problems within the insurance company, seems to have resulted in insurers being seen by the public as a soft touch or fair game. Procedures, of differing levels of effectiveness, undoubtedly exist within insurance companies, but these can often be neutralised and overcome. For example, experienced claimants are aware of the way in which appealing to head office or a consumer champion can cause an insurer to waver in its original resolve to investigate closely and dispute a suspected fraud claim.

EXAGGERATED CLAIMS

There has been minimal research into the subject of insurance fraud.[43] There are no reliable data to indicate the extent of fraud and the varying degree to which it is perpetrated.

Inflating a claim to provide scope for negotiation purposes is regarded as a normal procedure by most claimants. If, however, the insurer takes no action to remove that 'negotiating fat' then it is unlikely that the insured will draw to the insurer's attention what is essentially an over payment. As the scale of a claim increases so the opportunity to inflate and pad out the claim increases. Indeed, it is often on 'professional advice' that insureds submit claims containing items which they realise will be deleted during the adjustment. Differentiating between acceptable negotiating tactics and fraudulent intent is a difficult but overdue aspect requiring early consideration by insurers. (See chapter 7.)

Payment of a doubtful claim is often seen as the only option open to the insurer. Although there may be suspicion that part or all of the claim is fraudulent, insufficient evidence or a reluctance to investigate enables the fraudster to succeed.

STATISTICS

The extent of fraud is difficult to identify and there is very little statistical recording maintained. The writer's questionnaire survey to UK insurers asked for details of the extent to which they maintained statistics on fire claims which were paid even though they were regarded as doubtful or suspicious. The overwhelming response to this question was that no such information is maintained. (See chapter 6.)

It would therefore seem that insurers are not only presented with a difficulty in identifying fraudulent claims in the first place, but also keep no adequate records of the amount of fraudulent/suspicious claims actually paid. There is a difficulty therefore in identifying the extent of the problem as well as assessing the extent to which insurance companies, their shareholders and policyholders in general should recognise the problem and take remedial action. In view of the potential amount of fraudulent claims being paid by insurers it is suggested that:

- a detailed inquiry should be undertaken (Rec. 11.8)
- shareholders and policyholders should be provided with information on the insurer's approach to fraudulent claims. (Rec. 11.9)

DIFFERING APPROACHES

The insurance industry as a whole does not seem to provide a unified front in its approach to fraudulent claims. Some insurers are known to be concerned with the problem and their concern will reflect a lower claim payment level (and possibly, by reputation deter potential fraudsters from insuring with them). A higher claims handling expense will result though, both internally and externally, which will need to be compared against the savings achieved. However, a full record of paid and repudiated fraudulent claims would be needed for this comparison to be properly undertaken.

Other insurers appear to view claim payment very much from a marketing consideration with a lower requirement in terms of investigation.

As the size of a claim increases, however, the two attitudes do begin to merge and the results of the survey suggest that most insurers tend to become concerned about the possibility of fraud as the size of the claim increases.

ADJUSTER: INVESTIGATOR OR SETTLER?

Adjusters should play a vital part in identifying fraudulent claims. However, the extent to which the adjuster should be just a settler of claims rather than an investigator of claims is uncertain.

There is at present considerable debate over the responsibility of a company auditor for discovering fraud. The position taken by accountants is that an auditor is a watchdog rather than a bloodhound and that auditors should not be blamed for failing to discover fraud. Providing sufficient verification has been completed on the accounts and trading position then the opinion of the accounting industry is that the auditor has fulfilled his role.

In loss adjusting some adjusters regard themselves as watchdogs, who will settle the claim as soon as sufficient information has been provided but will not investigate for fraud, whereas others are clearly in the investigator or bloodhound mould. Blatant cases of fraud should be obvious to even the most inexperienced loss adjusters, their supervising adjuster, or indeed the habitual settler. However, more complicated and devious fraudulent claims may well require more than the proverbial 'nose for the dodgy claim' if they are to be identified.

During their qualifying examinations adjusters are not required to display any knowledge of fraud investigation. The training syllabus appears to be 'settler' or 'watchdog' based, working on the assumption that claimants are genuine and that the adjuster should display a sound and broad technical knowledge in the assessment of policy coverage and settlement issues. Members of the Chartered Institute of Loss Adjusters would be well advised to review the role and training of the loss adjuster in this regard, perhaps by means of a poll.

Views should be also be canvassed from the ABI and Lloyd's on whether the educational syllabus should be extended to include training in investigation techniques, e.g., fire cause and origin, fraud detection, interviewing and statement recording techniques, (Rec. 11.2) and whether the loss adjuster should be a watchdog or a bloodhound. (Rec. 11.10

A PUBLICISED ANTI-FRAUD APPROACH

Specific procedures and lines of enquiry may or may not be conducted in each case. Indeed, the insurer may cause the hard work of the adjuster, claims department and other specialists to be negated because of the absence of a proposal form or lack of obvious questioning that should have been raised at underwriting stage.

The latter problems may well increase with:

- the development of electronic underwriting;
- the expectation that property insurance in Europe is likely to become more of a commodity than a professional service.[44]

This may produce uncertainty about the way that insurers intend to protect themselves against fraudulent claims, assuming that that is their intention. Shareholders and genuine policyholders have a clear interest in learning how their insurer approaches fraudulent claims, although this is an area which does not yet appear to have been much publicised.

Most claimants should be willing to respond to a professional investigation providing they are aware that such an investigation procedure applies to all claimants. The genuine claimant would possibly regard

the investigation as a waste of the insurer's time and money but a necessary evil for the claim to be paid (similar to completing an annual tax return perhaps). A fraudulent claim ant would probably complain more about having to follow the procedure and would no doubt seek to invoke the assistance of a consumer champion, as well complaining to the insurer's chief executive.

DEVIATION FROM USUAL PROCEDURES

> *Repente dives nemo factus est bonus*—No one who is rich is suddenly made good.

There is often pressure from a large commercial organisation or a seemingly respectable well-known individual for quick settlement with minimal investigation. However, as recent cases have shown, it is often such large organisations or 'rich' individuals, (such as BCCI, Maxwell) which should receive a closer investigation.

The extent to which insurers are able to deviate from usual claims- handling procedures without approval from reinsurers, shareholders, or indeed other policyholders, should be questioned.

STATEMENT OF PRACTICE

Insurers have a duty to their policyholders, and more importantly to their shareholders, to investigate claims fully. They should be encouraged not to pay up for a quiet life or to keep claims handling expenses down. However, unless a standard industry-wide initiative is publicised and actually followed, the fraudster will always be able to apply pressure to an individual insurer to pay more than necessary. The introduction of a UK direct insurance statement of practice relating to the investigation of claims, (commercial and possibly also private) would perhaps help to reduce fraudulent claims.

UNDERWRITING DEFICIENCIES

Competition between insurers is strong and insurers often seem to be unable to obtain the full information which they would normally require at underwriting stage. Rather than regularly bemoan this development the insurance industry should perhaps make up for the underwriting information deficiency by a more concerted and determined effort at the claims stage.

CENTRAL ANTI-FRAUD REGISTER

A central database of claimants would provide insurers with the opportunity of a central reference point which could be consulted at underwriting stage. As discussed in chapter 4 this database could include not only repudiated claims and cases that have been contested in court, but also those that have been paid even though there was suspicion of fraud. Data protection considerations exist and there is a clear risk that by having an entry on the database an individual or business might find it difficult or more expensive to obtain insurance coverage. The information on 'suspected but paid' claimants would be to some extent similar to the intelligence collated and maintained on record by the police. The insurance industry's anti-fraud database would therefore need to be in at least two sections.

Section 1 should contain repudiated claims which had not been disputed as well as claims that had been successfully denied through legal process. Such information would undoubtedly be provable and should not be the subject of complaint by the individual or company concerned.

Section 2 would cover claims where fraud was suspected but never proven and a payment was made. This is clearly sensitive information. An entry on the list made accidentally by a claims official could have serious effects on the insurability and perceived moral hazard of that individual or company for the future.

Early consideration should be given to developing such a two-tier system. Through co-operation and consultation with the government, and application of the innovative and organisational strengths of insurers, any obstacles could be dealt with, and suitable safeguards agreed on, to protect the majority of policyholders from the theft of insurance monies by the minority of fraudulent claimants. (Rec. 11.1)

WHEN DOES EXAGGERATION BECOME FRAUDULENT?

Insofar as exaggerated claims are concerned, perhaps the insurance industry should no longer rely on UK case law but seek to alter the fraud condition in the policy to draw clearly the line between exaggeration purely for negotiation as against gross exaggeration. (See chapter 7.)

PUBLICATION OF ANTI-FRAUD PROCEDURES

The current perceived dichotomy between the customer service lobby and the claims investigation approach could be overcome so that with the application of proper investigation techniques all claimants will get what they deserve. However, there are two schools of thought on the extent to which details relating to fraud investigation procedures should be made public. On the one hand concern is expressed that a detailed procedure could enable a potential fraudulent arsonist to avoid detection. On the other hand there is the view that by clearly indicating that investigations will take place a deterrent effect is produced.

The author supports the latter view. It is submitted that, providing the procedures are worded in general terms, they will serve to:

— warn potential fraudsters of a difficult task ahead;
— show honest policyholders that action is being taken to combat fraud;
— reassure genuine claimants that the investigation is a standard procedure;
— provide shareholders, Names, and reinsurers with confidence in the claims management approach.

Financial aspects of fraud

The motive for fraudulent arson can often be found in the financial state of an insured company.

An assessment of the financial position and future prospects of an insured company is an important part of the investigation process after afire. The information revealed will be of interest in the assessment of motive. It may be that the business was not performing as well as expected in which case the insured may have decided to 'sell' the stock and property to the insurer. Alternatively the business may have been doing extremely well to the point when a competitor decided to interfere and destroy the insured's business. In recent years accountants have sought to develop their services to help adjusters and insurers with investigations into these financial aspects. Using the policy condition requiring the insured to provide all appropriate information, the adjuster can on behalf of insurers gain access to the business records to produce what must be an impartial assessment.

SPECIALIST AREAS

There is a limit though to the extent to which insurers can obtain information. Customers and suppliers are not obliged to co-operate. It may therefore be necessary to engage specialist financial investigators to conduct company searches and other information-gathering exercises. Useful information can also be gained by a review of the markets in which the insured company operates. Details gained from a trade association or marketing consultancy can provide information relating to the insured's market share, product potential and any changes in market conditions or technology.

Some chartered adjusters will have taken the accountancy related subject 'The financial dimension in claims adjustments' (previously called, perhaps more appropriately, 'Accounting relating to loss adjusting'). This is of considerable benefit to the adjuster in this aspect of enquiry. Independent financial analysis and comment should also be sought to supplement the adjuster's knowledge when necessary.

Working as part of a team the claims accountant can provide specialist support. Just as a specialist engineer may be required to deal with a technical problem so an accountant can be of value when dealing with the financial assessment.

The involvement of specialist forensic accountants can give the insured the impression that the claim is suspect. This is especially so if the accounting personnel are not sensitive to the fact that many claimants are genuine. Enquiries therefore need to be conducted properly, fully, but in a sensitive and courteous manner. As with all outside specialists the brief for the accountant should be clearly set at the time of instruction to avoid unnecessary activities, duplication and cost. Communication channels should be established, with the accountant reporting frequently to the adjuster.

DUPLICATE RECORDS

Often the financial records are destroyed or partially damaged in the fire. This may or may not have been an accident from the insured's point of view. It is recommended that for certain insureds in specific classes of business and certain geographical locations it should be compulsory for a complete set of duplicate business records to be stored safely at an alternative premises. (Rec. IV.2)

BANKS

As mentioned in chapter 4 there will often be a bank or institution with a financial involvement with the insured company and probably an interest noted in the policy. The accountant should pay close attention to the relationship between the insured company and its bankers especially with regard to the provision of overdraft, finance, capital and security requirements during the previous years.

Experience in recent years has shown that banks have not always exercised the prudence which traditionally has been expected of them. Lending has sometimes been to excess and often at levels well beyond the ability of a business to meet repayment and interest charges. The basis of asset valuation as security for finance should be checked for authenticity and accuracy. Close attention should be paid immediately to the wording of the insured company's agreements with the financial institutions concerned. The way in which the bank's interest has been noted in the policy should also be examined.

The forensic scientist

> Perhaps when a man has special knowledge and special powers like my own, it rather encourages him to seek a complex explanation when a simpler one is at hand.[45]

The cause of the fire is the most important issue, and assistance may need to be sought from a forensic scientist.

The *Lexicon Webster Dictionary* defines 'forensic' as:

> Pertaining to, connected with, or used in Courts of Law.

The forensic scientist is generally engaged by the adjuster on behalf of the insurer with the intention of establishing the cause of the fire with as much certainty as possible. As the law reports clearly show, forensic scientists do not always agree on the probable cause. Quite often the forensic scientist acting for the insured endeavours to submit alternative causes so as to cast doubt on the view of the insurer's forensic scientist. This is especially so where deliberate ignition, possibly by the insured, is at issue.

IMPARTIALITY

Being 'forensic' clearly shows that that scientist will be conducting all work in the knowledge that a report and testimony might have to be given in court. Forensic scientists who try to be selective with the facts or biased in their view are essentially of no use to the insurance industry. Insurers are in business to pay valid and genuine claims arising from fire and the forensic scientist should pursue the truth in an impartial way. Any bias or selective investigation

might produce an incomplete conclusion. This could lead to a genuine insured being unfairly accused of fraud and possibly suffering considerable financial loss, not to mention the costs to the insurer.

PROFESSIONAL NEGLIGENCE

As highly qualified professionals, the subject of professional negligence must be considered, especially if a party (insurer, insured or an interested party such as a bank) relies on the scientist's report and spends time and money either pursuing or defending a claim which hinges on that expert's conclusions. There is no doubt that this prospect must be constantly in the mind of a forensic scientist although disclaimers are not often included in reports. The interesting question arises of how an aggrieved party would pursue a claim for negligence. Presumably by engaging another forensic scientist for expert opinion on the methodology of the original forensic scientist.

As experts forensic scientists have a duty to give an independent opinion on the cause at issue, or any other matters which they have been asked to comment on, rather than to plead their clients' cases. In Whitehouse v. Jordan (1981)[46] Lord Wilberforce said:

> Expert evidence presented to the court should be, and should be seen to be, the independent product of the expert, uninfluenced as to form or content by the exigencies of litigation.

SELECTIVE REPORTING

The recent case of Derby & Co. Ltd v. Weldon[47], however, confirmed that the expert is not obliged to include in his report all of his views—both the good parts for the client's case and the bad. The Court of Appeal has now made it clear that the defence is not under an obligation to put forward any points which might be against the client. Essentially if the plaintiff has not spotted the point, the defence expert is not obliged to point it out. However, during cross examination, points not previously mentioned may arise.

Forensic scientist and loss adjuster

Forensic scientists firstly have to conduct independent investigations to arrive at an opinion. Secondly, however, once they have formed an opinion the individual elements and strengths and weaknesses need to be analysed in conjunction with the insurers, adjusters and legal advisers.

> *Felix qui potuit rerum cognoscere causas*—Fortunate is he ho has been able to learn the causes of things.

In recent years there seems to have been a blurring of responsibilities of the forensic scientist. The two stages of a fraudulent arson investigation are ascertaining whether the fire arose from a deliberate cause and deciding whether on the balance of probabilities it was the insured's act or connivance that caused the deliberate fire.

The first stage is clearly within the role of a forensic scientist. However, the extent to which the forensic scientist should stop being an independent expert and become an investigator seeking to answer the second point is debatable. The argument for each party having their own forensic scientist probably therefore hinges on the extent to which the second point should remain within the responsibility of forensic scientists.

ALLOCATION OF RESPONSIBILITIES

Two questions need to be answered by the private forensic science and loss adjusting professions: Does the forensic scientist do work which the adjuster could do? Does the loss adjuster do work which the forensic scientist should do?

Lines of enquiry of a non-technical nature could be performed by the adjuster who should be able to relate and collate information being received from different sources. Communication is vital as forensic scientists appear to be developing more and more into the role of forensic investigator, seeking to answer not only the question of whether the fire was started deliberately, but also whether it was the insured that started the fire. The answer to the second point may well emerge from necessary technical enquiries but the more that forensic scientists are perceived as searching to prove involvement of the insured the less they can be regarded as independently searching for the true cause of the fire.

The link between arson and the insured may not exist because the insured had nothing to do with starting the fire. Alternatively, the link might exist, but because professional arsonists started the fire the forensic scientist may have immense difficulties in proving the link, even though proving arson is possible. Other non-scientific aspects could well provide information enabling a link to be made between the arson and the insured such as:

- identification of persons or objects at the scene; timing inconsistencies;
- unsatisfactory financial performance;
- a wish to redevelop contrary to preservation/listing arrangements;
- a preconceived plot from outset.

Just as the areas of co-operation between the adjuster, the police and the fire brigade are not clear, the roles of the forensic scientist and the loss adjuster have not been clearly defined. (Rec. II.11)

EFFECTIVENESS OF PRESENT APPROACH

All these relationships hinge on the abilities of the individuals concerned to work together. Perhaps it is now appropriate for loss adjusters, insurers and forensic scientists to assess the effectiveness of the approach adopted to date.

Questions worth discussing include:

Who should take final responsibility for deciding the limits and scope of the investigation?

Who should take responsibility for collating information being received from different sources and disciplines?

Who should form a view with regard to the insured company directors, managers and employees in relation to the fire?

While the forensic scientist is obliged to prove conclusions on scientific grounds making expert supposition to fill in the gaps, who should take responsibility for expert supposition on non-scientific aspects?

Should the adjuster form a view on the credibility of the insured? If so should there be an objective procedure to form such a view?

FAILURE TO INSTRUCT FORENSIC SCIENTIST

How many cases of arson are missed when adjusters do not consider a forensic scientist to be necessary because

- they feel they have sufficient technical ability (and this may or may not be the case) to discount the possibility of arson; or
- they find a reasonable accidental explanation readily available, and look no further; or
- they believe that the insurer would not wish to incur the extra expense of a forensic investigation?

ACCESS TO FORENSIC SCIENCE SERVICES CAREFUL EXAMINATION

It is unlikely that loss adjusting companies will employ forensic scientists on the payroll as this might possibly be seen as impairing their impartiality. There does however seem to be a need for adjusters to have access to the services of forensic scientists more frequently, even if just to conduct a brief site inspection to discount the possibility of arson (and also to comment on recovery claims inwards or outwards). There is a limited supply of qualified experienced forensic scientists but it should surely be possible to reach agreement between the private forensic science profession and the insurance industry for different levels of investigation. Just as a doctor of medicine will have a varied workload from patients who are critically ill to those requiring a prescription so the private forensic science services should perhaps be organised to respond in accordance with their clients' requirements and needs.

A two-tier response is suggested. (Rec. II.21)

Level 1 response

This would be a brief but prompt site inspection followed by a one- or two-page standard report (possibly using a standard layout agreed between the professions) indicating whether or not a more in- depth enquiry is required. There would be a need to match brevity with a lower level of responsibility for the investigation and a fee in keeping with the time and expertise involved. This response would allow the cost-effective inspection of fires where the likely cost of the claim would not usually be sufficient for an insurer to incur the costs of a forensic scientist.

Level 2 response

This would involve a full site investigation either immediately, or after a level 1 visit Agreement would be reached at the start of the investigation on the scope of the forensic scientist's intended enquiries. It is most common for professionals and consultants to agree at the outset with their clients the extent of their involvement and the basis of charging. It is surprising to note that forensic scientists do not generally seem to be given a written brief for discussion and agreement at the start of an investigation. Such an agreement would help the forensic scientist who would be aware of the responsibilities resting with him within the overall allocation of professional resources conducting the investigation.

At both levels responsibility would be agreed for taking and recording statements, and obtaining background information. This would avoid complaints from forensic scientists relating to the delays experienced in being provided with statements that were supposed to have been recorded by the adjusters.

Forensic scientist and the insured

The arrival of a forensic scientist at the scene can lead to suspicion of the insurer's motives by the insured.

CAREFUL EXAMINATION

> The more outre and grotesque an incident is the more carefully it deserves to be examined and the very point which appears to complicate a case is, when duly considered and scientifically handled, the one which is most likely to elucidate it.[48]

The argument could be raised that a genuine insured need not retain a forensic scientist as the forensic scientist engaged by insurers should produce an independent conclusion. However there is an element of risk that the forensic scientist might reach a conclusion which is wrong. A genuine insured would then be left in the situation of having to pursue a claim through the civil court against the insurers without the benefit of expert evidence to dispute that of the insurer's forensic scientist.

The argument for each party having their own forensic scientist probably therefore hinges on the extent to which proving the link between arson and the insured should remain within the remit of forensic scientists.

CAUSE ARBITRATION

In the process of seeking to prove or disprove the link it is suggested that the independence and impartiality of the forensic scientist is placed under considerable pressure. Given the adversarial nature of the legal system, and indeed the way in which a claim is dealt with under a policy, it should be considered whether forensic investigations could be approached along the same lines as arbitrations. That is to say that the insured and the insurer agree on the forensic scientist who would conduct the investigation and agree to accept the findings on the cause of the fire. The reality is that probably neither party would be willing to accept such an arrangement and that therefore the existing use of forensic scientists acting for and being 'sympathetic' to individual parties rather than

independently searching for the truth is likely to continue.

FORENSIC SUPPORT FOR THE INSURED

Obtaining forensic scientific assistance through criminal legal aid is, according to Stockdale,[49] difficult because of the problems experienced with the taxing of costs. In his view some of the properly qualified independent forensic scientists have been persuaded to refuse legal aid work in favour of more lucrative business elsewhere, for example in the insurance claims market. He expresses the hope that the Royal Commission, which is currently examining various aspects of the criminal justice system, will provide the opportunity for a strong independent source of forensic science advice available to the defendant. Considering that the insured may face criminal charges at some stage, forensic science support would be needed by the defence.

PROFESSIONAL FEES COVER

Most insurance policies provide coverage for professional fees. For example, in the event of a subsidence claim insurers are willing to pay the cost of an engineer's appointment to investigate the cause of the subsidence. Although approaches vary, a frequent arrangement is that the insurer asks the insured to obtain a report from an independent consulting engineer. This report is then sent by the insured to the insurer for consideration. At that stage a second opinion might be sought. Considering that 80 to 90 per cent (by value if not by number) of arson claims are not thought to involve fire setting by the insured, the present approach to fire cause investigation may have to be altered.

If the insured has to engage a forensic scientist from an approved list the co-operation received by the forensic scientist from the insured could well be far greater than usual. The suspicion and distrust created by the appointment of a forensic scientist by insurers would be dispelled because the insured would also expect to receive the scientist's report.
At this stage of the investigation the forensic scientist would be approaching the first question, i.e., 'How did the fire start?'

Information relating to the second question, i.e., 'Did the insured start the fire?' would be gathered by the adjuster who is able to relate to the forensic scientist and receive details of his investigations. Forensic scientists would therefore be able to operate independently to pursue the probable cause of the fire. They will be aware that insurers will be ultimately paying their fees and that they have a duty to both the insured and the insurer to seek the truth.

A problem, however, would arise if a 'guilty' insured sought to interfere with the forensic scientist's investigation through obstruction or distraction. At the point when it becomes apparent to the forensic scientist that there is a possibility that the insured has been involved in starting the fire difficulties arise with the arrangement outlined above. Should the forensic scientist on discovering that a crime has possibly taken place report the incident direct to the police? Should any doubts be reported to the insurer confidentially? Or should he switch to working directly for the insurer and inform the insured that a second forensic scientist should become involved to represent the insured?

While it is not ideal it can perhaps be concluded that the present practice of insurers instructing 'their' forensic scientist is likely to be regarded as the best approach in terms of protecting the insurance fund from fraudulent arson claims.

It could be argued that insureds should be notified of the way in which the claim will be investigated and given the opportunity to retain their own forensic scientist from outset at their expense.

The question arises as to when the insured should be informed that insurers suspect arson. Insurers were criticised in Watkins & Davis Ltd v. Legal & General (1981)[50] for not raising the issue of arson immediately. The fire occurred on 29 April 1978 but it was not until March 1979 that the issue of arson was raised by way of an amendment to the defence. The result was that the forensic scientist engaged by the insured did not have any opportunity to visit the premises. Although there was criticism of the delay there does not appear to have been a detrimental consequence to the insurer concerned. For example no consideration of estoppel seems to have been raised.

In his article 'Fraudulent claims',[51] R.H. Dulwich suggests that a letter should be sent to insureds informing them that certain disturbing features have come to light. Dulwich considers that this would give insureds the chance to have their own forensic investigation. But why would an insured who had set fire to his property, or arranged for someone else to set fire to the property on his behalf, wish to have a forensic investigation? Surely such an insured would already be aware of the expected findings. Assuming that the forensic scientist conducts an impartial investigation, without influence from the insured, the report's conclusions would be incriminating from the insured's point of view. If the insured were innocent and did not in any way cause the fire to start deliberately then the benefit of a forensic report commissioned by the insured is questionable.

STATEMENT OF PRACTICE

A publicised approach to the way a fire is investigated by insurers may help to place the innocent insured at ease (even though at that stage the insurers may not have concluded that the insured is in fact innocent). At the same time the guilty insured would be placed on notice that a procedure is in progress which will in all likelihood prevent payment of the claim and could possibly lead to criminal conviction.

Forensic scientist, fire brigade and police

Outside of the insurance relationship, forensic scientists also operate on behalf of the fire brigade and

police forces. Essentially though their enquiries would he related to ascertaining how the fire started. Police detectives would then endeavour to produce evidence of a non-scientific nature to support the allegation of arson.

Enquiries with private forensic scientists indicate that informal lines of communication exist to facilitate the acquisition of information. Formal procedures are also in place enabling the interviewing of fire brigade officers, at a cost.

From the discussions held during this research it is possible to summarise the private forensic scientist's attitude towards the police and fire brigade as: 'Liaise, co-operate, but do not rely on the police and fire brigade.'

Criticisms levelled at the fire brigade involve disruption at the fire scene during extinguishment and damping down as well as indiscriminate removal of debris.

There would seem to be grounds for improving and formalising relations between the private forensic science profession and the public services.

The central and regional fire liaison panels

A forum is required to allow loss adjusters to improve communication and co-operation with other agencies.

The Central Fire Liaison Panel (CFLP) is said to provide a forum for the exchange of ideas and the discussion of problems. This organisation co-ordinates the work of the regional fire liaison panels. The regional panels have the objective of bringing together all those interested in fire safety and of providing facilities and information for individuals and firms to reduce fire waste.

CILA

The CFLP and the individual regional fire liaison panels appear to be appropriate vehicles for the active and positive involvement of representatives from CILA. In view of the role played in detection, resolution and risk improvement by loss adjusters it is suggested that urgent consideration should be given by CILA to be represented on each regional fire liaison panel as well as the CFLP. The CILA representatives should also perhaps meet to liaise as a group or elected committee to review difficulties, propose solutions and communicate developments to all CILA members. (Rec. II.14)

Fire brigade

The fire brigade plays an important role in the arson issue but, surprisingly, only up to the point that arson is identified as the cause.

HISTORY

It is known that there were firemen in ancient Rome, the 'vigiles', and a similar force was prob ably established in Londinium during the lengthy reign of the Roman Empire. After a four century lull, William the Conqueror implemented his couvre-feu (curfew law) in the eleventh century. This required the dousing of all fires and lights at nightfall and severe penalties were imposed on anyone disobeying the curfew.[52] If insurance companies had existed at that time then no doubt the astute fire underwriter would have imposed a warranty requiring compliance with the curfew!

The years leading up to the seventeenth century saw varying efforts in the field of fire protection often initiated by the Lord Mayor of London. Primitive fire appliances appeared around 1600 although these were not very effective. Following the devastation caused by the Great Fire of 1666 insurance companies were granted charters to provide fire insurance.

The first fire brigades in the UK were organised in London by the fire insurance offices. Originally these brigades would only deal with fires in buildings insured by their company, identified by a fire mark on the building. In 1833 the brigades were amalgamated with the London Fire Engine Establishment. Municipal brigades had by that time also been formed in Edinburgh and Manchester.

In 1866 the London fire service was established by the Metropolitan Fire Brigade Act 1865 which for the first time placed the duty of extinguishing fires in London on a public authority. Only London had a brigade with statutory protection until 1938. Up until that time voluntary brigades operated in other parts of the country. The Fire Brigade Act 1938 created fire authorities throughout the country and required local authorities to provide fire fighting organisations. However, the Second World War prevented the Act from becoming fully effective. In 1941 the National Fire Service was formed under the direction of the Home Office and the Scottish Office. After the war the Fire Services Act 1947 returned the brigades to a reduced number of local authorities while retaining an element of central control.

ROLE

The role of the fire brigade is clearly set out in the Fire Services Act 1947 which states that:

> At any fire the senior fire brigade officer present shall have the sole charge and control of all operations for the extinction of the fire.[53]

The safeguarding of people's lives is the prime duty of fire fighters. Brigades have four main functions:

Fire fighting—fire authorities are required by law to make provision for fighting all types of fires from major chemical hazards to chimney fires.

Minimising damage—steps are taken to minimise the damage caused by fire and fire-fighting operations.

Legal enforcement—fire precautions in existing buildings are legally enforced.

Fire protection advice—provision of advice on fire prevention and means of escape is a statutory duty imposed on the brigades. Advice is given freely to

anyone. Inspections of premises also acquaints the brigades with contents and layout which can prove useful in the event of fire.

CAUSE OF THE FIRE

The Home Office has requested fire brigades to provide information to assist in the preparation of statistics. One such item of information is the supposed cause of each fire. There is no statutory duty to investigate fires and produce a supposed cause. However, brigades develop their own fire investigation techniques and procedures depending on the demands of their area.

A report, FDR1, is available for a fee on application to the fire brigade. This provides information under the following headings:

1) General
2) Location of fire
3) Construction of building
4) Extinction of fire
5) Damage and spread
6) Supposed cause of fire
7) Life risk
8) Explosions and dangerous substances.

The information shown under 'Supposed cause' is:

- source of ignition;
- material or item ignited first;
- defect, act or omission giving rise to ignition;
- material or item mainly responsible for development of fire;
- further information.

A Home Office circular issued in September 1985 stressed that in terms of the supposed cause to be entered on the FDR1 report:

> The description 'doubtful' should only be used (in this context) where malicious or deliberate ignition is suspected but not established beyond reasonable doubt. This description should not be used to indicate general uncertainty about the cause of the fire. In such circumstances cause 'unknown' should be entered if necessary but, where possible, the most likely cause on the evidence available should be given.

The significance of the words 'doubtful' and 'unknown' should be noted as confusion is often encountered in the interpretation of information shown in section 6 of the FDR1 form.

At the 1991 CILA educational conference a senior fire officer[55] clearly explained that the supposed cause is exactly that. It is not the definite cause but the most likely and can be based on a percentage of probability.

It is generally the fire officer in charge who is responsible for writing up the supposed cause. If, however, he suspects the cause to be doubtful then attendance by the fire brigade's fire investigation team or the police may be requested. A more detailed internal report may also then be produced, but the fire brigade is unlikely to release this to anyone other than the police.

Often considerable reliance is often placed by adjusters, insurers and others on the information contained in the FDR1 report. Given the statistical purpose for which the supposed cause in the FDR1 is being established, insurers should perhaps be more concerned to obtain an independent cause investigation conducted specifically from the outset for legal purposes.

SCENE DISTURBANCE

The fire brigade recognise that in fulfilling their duty of saving life and preventing damage to property they can in fact produce difficulties for the subsequent forensic investigation. Training courses stress the need to keep scene disturbance to a minimum.

IMPROVED COMMUNICATIONS

Concerns have been expressed within the fire brigade about the professionalism of insurers, loss adjusters and loss assessors. Considering the close involvement and need to co-operate on a professional basis it is suggested that loss adjusters, through CILA, should on a regional basis seek to develop improved understanding. The recommendation in this paper relating to involvement on fire liaison panels (Rec. 11.12) would, perhaps, enable such co-operation to develop. The forum would also then exist to discuss reasons for refusal to release detailed reports and to debate possible changes in this position. This would dovetail with the recommendation contained in the 'Prevention of arson' report which recommended that:

> Training at the Fire Service College and elsewhere should reinforce and emphasise the requirements of' joint investigation of arson and the close co-operation with other agencies that is entailed.

Assuming, that is, that the reference to 'other agencies' was intended to include loss adjusters and other professionals representing insurers.

Fire brigade and insurers

The present distance between the insurance industry and the fire brigade is a far cry from the initial formation of brigades. Considering the original relationship between insurers and the fire brigade, it is disappointing to note, at least in the claims context, that the insurance industry appears to have moved farther away from the fire brigade authorities than perhaps should be the case. The interests of the fire brigade and the insurance industry are similar both at underwriting stages, in terms of fire prevention, and at claim stage, in terms of cause investigation and damage mitigation.

CLOSER CO-OPERATION

Much closer co-operation should be sought with claims arising from fires started deliberately. A fire thought to have been started deliberately requires investigation at the earliest opportunity. The fire brigade are generally at the scene before any other party, and are certainly best placed to trigger a private forensic investigation.

At the present moment the insurer will often not learn of a fire for hours or possibly days. Any time lapse can severely prejudice site investigation from the insurer's perspective.

FIRE MARK NOTIFICATION SYSTEM

Might it be possible to introduce a notification system, perhaps code-named 'fire mark'? Essentially the fire brigade would take responsibility for notifying a national or regional central point that a fire had occurred at a particular premises. The central point, possibly a privately operated 24-hour staffed facility akin to a security company central station, would have details of the insurance in force at the premises concerned. Urgent telephone communication could then be established with the insurance company claims manager or a nominated loss adjuster or forensic scientist and the insured. (Rec. II.13)

There are problems with this recommendation that would need to be resolved:

1. The central point will, through the computer records, have access to sensitive insurance market information which could be abused. For this reason the central point could perhaps be operated under the auspices of the Association of British Insurers or the Arson Bureau. Confidentiality could also be preserved if individual schemes were established by insurers themselves or in conjunction with outside organisations, but this would possibly cause difficulties with the fire brigade.

2. At what time should the fire brigade notify the central point? Various trigger points could be considered, for example:
—*size of fire*: a loss involving the immediate attendance of more than say four pumps could produce a significant insurance claim and therefore, whatever the cause, insurers may wish to respond rapidly.
—*supposed cause*: either the blaze will be one at which the senior fire officer will relatively quickly be able to suppose that the fire is doubtful, or it will be so complex that the investigation will require the involvement of the fire investigation team. Insurers could react quickly at this stage because the loss may not be arson but could perhaps involve a recovery.
—type of risk: selected risks known to be in the high risk arson categories could be identified, e.g., textile warehouses.
—location of risk: certain areas in major cities are known to suffer a higher incidence of arson.

3. The fire brigades may not wish to co-operate with such a system, because of extra cost, administration, complexity etc. However, if the fire mark system was shown to have advantages, and perhaps even involved an administration payment from insurers to the brigade for each call, then this problem could possibly be overcome.

The establishment of a fire mark notification system could perhaps produce a deterrent effect. It would certainly be a method of enabling rapid response by insurers to preserve the scene and commence investigations.

Fire investigation teams

The development of specialist fire investigation teams should be seen as one of the most positive steps forward in the identification of arson in the UK. However, the teams operate under the control of individual fire brigades and there does not seem to be a standard nationwide approach.

LONDON'S INVESTIGATION UNITS

In London there are five fire investigation units, one in each of the operational area commands. In 1990 approximately 2600 cases were investigated and the cost of running the units is estimated to be in the region of1m. The teams can be requested to go to an incident by the senior fire officer in charge and will in any event investigate fires:
– attended by four or more fire appliances;
– involving death or serious injury;
– of special interest;
– in buildings of special interest.

A full fire investigation report is completed for each incident attended by the London fire investigation units.[56] If arson is suspected the police take over the investigation. The detailed brigade fire investigation reports are available to the police to be used as part of the evidence in the course of the criminal investigation.

INFORMATION WITHHELD

Insurers do not benefit from the investigations conducted by brigade fire investigation teams.

For an adjuster it is frustrating to know that a fire investigation team is investigating but that information relating to their investigations is being withheld from insurers.

Interviews can be arranged with officers but this involves the insurer in expense and needless delay. Informal discussions with officers at the scene are all well and good but a more formalised relationship would he beneficial.

IMPROVEMENTSTO RELATIONSHIP

Some arson investigation units in America are organised differently and often involve insurance and police personnel operating together with the fire brigade officers. Ideally the adjuster and private forensic scientist service should meet and establish a working relationship with the fire investigation team within hours of the fire being notified. Such close cooperation would clearly involve the need to establish levels of expertise and professionalism.

Considering that the fire investigation team would often be called to attend urgently at the premises there is the time-lag problem to consider from the insurers' point of view. A delay will occur before the adjuster and private forensic scientist can arrive at the scene. However, if there is an understanding in existence it should be possible for the forensic scientist

and the adjuster quickly to obtain details relating to the period that the fire investigation team and brigade were in attendance. Not all attendances by fire investigation teams relate to arson and there would therefore he advantages in other areas of fire insurance claims for developing a suitable liaison arrangement.

Involvement with the fire investigation team will also enable continuity of information to be retained by the adjuster and private forensic scientist during the handover from fire brigade to police in the event of suspected arson. (Rec. II.14)

Fire brigade—liaison with police

If the fire officer in charge at the scene suspects that the cause of the fire may be arson it is reported to fire brigade control, which immediately informs police control. Forensic evidence will be handed over from the fire brigade to the police and the police take responsibility for pursuing enquiries further.

LONDON'S LIAISON REPORT

Since April 1991 in the London area the fire brigade have had to complete a liaison report which is passed onto the police whenever a fire:

—requires the attendance of the police;
—requires the attendance of the brigade fire investigation team;
—involves a serious injury/fatality;
—is of a suspicious nature.

Section 2 of the form is completed by the police when a crime has been classified and is then returned to the fire brigade's fire investigation team.

The effectiveness and extent to which this procedure is being followed has not yet been established.

FURTHER RESEARCH

The Prevention of arson' report recommended in 1988 that:
research should be undertaken into improving methods of examination of scenes of fire so that police and fire officers may be able to identify more effectively and quickly cases that involve arson.[57]

The extent to which further research has been conducted is not known.

Three years earlier in September 1985 a Home Office circular [58] relating to the investigation of fires of doubtful origin stated that:

It is clear that the investigation of fires of doubtful origin entails a multi-disciplinary approach and that, in the sequence of events from the first suspicions that the origin of a fire may have been other than accidental to subsequent investigation and successful criminal prosecution, the closest liaison, co-operation and mutual assistance between the police, fire and forensic science services is called for. This requires not only an appreciation of the legal responsibilities of the respective services hut also of the special qualities and different skills, experience and support facilities which are available to them. Roles and responsibilities must be clearly identified.

Considering the information which the insurance industry can provide to assist in preparing a criminal prosecution it is disappointing to note the absence of any reference in this part of the circular or indeed in the recommendation in the Prevention of Arson report to the insurer concerned, the loss adjuster or the private forensic scientist.

POLICE INVOLVEMENT

On receiving a call from fire brigade control regarding a fire of doubtful origin, police control will despatch a scene of crime officer and will notify an officer of the rank of inspector or above. That senior police officer then becomes responsible for the conduct of the investigation into any crime which is suspected or identified in relation to the fire. He or she will liaise with the senior fire officer as well as the fire brigade investigation team and the forensic science service.

If police officers are at the scene of the fire and feel that the fire is of doubtful origin the procedure is that they should not wait for the fire brigade to contact police control but should contact their own police operations room immediately.

The police may become involved therefore at a fire scene through:

— notification by the fire brigade of a doubtful origin fire;
— a request from an attending police officer notifying a fire of doubtful origin;
— suspicion raised from any source that the fire is of doubtful origin.

DETECTIVES

Police detectives are not trained in fire investigation techniques, although scenes of crime officers do receive such training to varying degrees. Without formal fire investigation training the detective is therefore in a similar position to the loss adjuster. Both also have the responsibility placed on them of deciding whether or not a forensic scientist should be requested to attend the scene. Specific guidelines exist with regard to the deployment of forensic science resources to the police and in some cases it is the responsibility of the scenes of crime officer to deal with investigations at the site and to package materials requiring examination at a forensic science laboratory.

POLICE AND BRIGADE LIAISON

The Home Office has stressed that the fullest possible liaison between police and fire services is desirable in the course of fire investigation and that it should include:

— the passing to the fire service of all relevant information for recording purposes and any appropriate action

— the opportunity for a senior fire officer to participate in briefings and conferences held by the senior investigating officer with his team and other invited experts, especially in the case of a major investigation

—a full and free exchange of information between the police, fire and forensic science services.

It would appear that the insurance industry has failed to impress on the Home Office the benefits that could be gained by the police and fire brigade from cooperating with insurers during the course of an enquiry.

It is recommended that a procedure for co-operation between loss adjusters, police and fire brigade should be established. (Rec. II.15)

FINANCIAL SUPPORT

The official position at present is that there is something of a 'them and us' relationship between the public services on one hand and the insurance industry on the other. This not only benefits a fraudulent claimant (divide and rule) but also means that duplication occurs with consequent increased costs. It would be interesting to establish the extent to which the UK insurance industry would be able and willing to sponsor or contribute towards particular public service investigation expenses. (Rec. II.16)

Police

LAW AND ORDER

> I have been down to see friend Lestrade at the Yard. There may be an occasional want of imaginative intuition down there, but they lead the world for thoroughness and method.[60]

The police forces in the UK have the primary responsibility for law and order. Each force decides on the policy for its particular area with guidance being given by the Home Office. The Police Act 1964 provides the structure and organisation details for the forces.

ALLOCATION OF RESOURCES

In the Home Office report 'Prevention of arson' it was stated that:

> Arson is predominantly a crime against property rather than against people. For this reason, and perhaps because it is difficult to investigate and prosecute, it is not always being given high priority in the allocation of resources by the police and the forensic services.[61]

It may be that insurers, through their involvement with the Arson Prevention Bureau, should seek current information to discover whether the allocation of resources has increased and been given a high priority.

INVESTIGATION DIFFICULTIES

In a paper 'Arson—the police perspective[62] John Dellow, of the Metropolitan Police summarised the difficulties faced by the police in terms of investigating a fire.

> The investigation into the causes of fires differs from the majority of crime enquiries and duties undertaken by the police for a variety of reasons. For example the police are not usually the first persons to examine the scene. This creates problems not only in the destruction or contamination of potential forensic evidence but also with the movement or removal of articles connected with the fire. Often the building collapses or the property is damaged by the fire making the examination very difficult. I have already mentioned the destruction of evidence by the fire fighting authorities but, of course, there s also the destructive power of the fire itself There is also the problem of the motive that incites the fire raiser to commit the offence. This is often particularly obscure and difficult to discover. Finally there is the problem of finding sufficient convicting evidence to institute proceedings, apart from any statement of admission the fire raiser may make when interviewed. The investigators' problems do not end there. Even after surmounting these difficulties he then has to convince a jury of the arsonist's guilt. There is a growing tendency in criminal trials for the defence to attack not only the prosecution evidence, but the procedures by which that evidence was obtained. The phrase 'trial within a trial' is featuring more and more so we in the police service must ensure that all possible steps are taken to preserve the integrity of the evidence. In arson cases one of our biggest problems is the continuity of exhibits. For example unless we can prove to the satisfaction of the court that the empty can of petrol removed by a fireman from near the seat of a fire and thrown into a pile of debris in a corner of a room, is the same can that may have been moved again before police find it and hand it to a scientist in the laboratory for examination, then that can, and any evidence emanating from it, may be ruled inadmissible. This is a problem that is going to increase and can only be tackled by those who are lawfully present at the scenes of fires being made aware of their responsibilities in this matter. It is only from this greater awareness that the problem may be overcome.

INTEGRITY OF EVIDENCE

Fire brigade officers and loss adjusters in particular must therefore exercise great care in preserving the integrity of the evidence. The police appoint an exhibits officer who records details of each piece of evidence, who it was found by, and who it was passed to. Records should be kept of the progress of the evidence as it passes from hand to hand and the special police labelling has provision for each person to sign his name on it as he receives the item.

The information on the label, which has to be securely fixed to the object includes:[63]
— police force and division;
— description of item;
— location it originated from;
— name of discoverer;
—date and time.

In the course of a crime investigation the police will conduct a systematic search for clues. A clue is any piece of evidence which might help in proving how, when, where, why or who committed the offence.[64]

In a talk [65] to the CILA fraudulent arson workshop in 1991 Detective Superintendent Andrew Brown discussed the police role. He advised that detectives

are trained to look at four key aspects during the course of their investigation: motive, opportunity, preparation, and subsequent conduct.

PREPARATORY OFFENCES

If the police are able to apprehend suspects before they have actually committed arson it is sometimes possible to pursue criminal prosecution for preparatory offences such as:

- conspiracy: (Criminal Attempts Act 1981, s.5 (1));
- incitement: if the crime is committed the inciter may be dealt with as a criminal (Common Law);
- attempt: (Criminal Attempts Act 1981, s.1 (1)).

PROOF

The police require proof from their forensic service that the fire was definitely arson before it is recorded as a crime of arson even if the brigade has found evidence to suspect arson as the cause.

CROWN PROSECUTION SERVICE

The police retain the responsibility to decide on an arrest and charges but responsibility for the prosecution of offenders rests solely with the Crown Prosecution Service (CPS).[66]

The CPS will expect there to be a likelihood of a successful prosecution and will also take account of public interest criteria.

In a lecture to the CII Society of Fellows in October 1989 James Anderton mentioned that

> There is growing concern in many quarters about the weakening influence and increasingly doubtful primacy of the police. The Crown Prosecution Service has largely removed that special function (the prosecution of offenders) from police.[67]

The relationship between the police and the CPS is a factor which may influence the police force's enthusiasm for investigating and prosecuting arson. It would be interesting to assess the priority and resources allocated by the CPS to the prosecution of arson. (Rec. II.12)

Police, insurers and adjusters

INVESTIGATIONS BY INSURERS

I go into a case to help the ends of justice and the work of the police. If I had ever separated myself from the official force, it is because they have first separated themselves from me. I have no wish ever to score at their expense.[68]

The Munich Re publication Arson (1987)[69] suggested that:

> Insurers should only set investigations of their own in motion, if—for whatever reason—the police are making no progress in their own investigations.

It is, however, suggested that insurers in the UK should in reality set their own investigations in motion immediately and look after their own interests first. Whatever the police and CPS decide to do by way of investigation and prosecution, insurers should take care of their own investigations to assess whether or not the claim should be paid or repudiated under civil law because of arson or any other policy reason. If insurers wait for police investigations to progress before starting their own enquiries severe prejudice may result and if the case is fraudulent arson then the chances of a successful civil defence may be considerably reduced.

Having said this, however, there must be greater cooperation between the police and insurers and loss adjusters. The guidelines issued by the Association of Chief Police Officers (ACPO) in 1982 on the supply of information to insurance companies unfortunately deprive insurers of information. Police forces will take no action on enquiries from insurance companies or adjusters relating to requests for:

- confirmation that matters have been reported to the police;
- their interest to be noted;
- information on the recovery of property;
- information regarding the arrest of offenders;
- information on awards by courts of restitutional compensation.

In effect the police have to a great extent isolated themselves from the insurance industry, and opportunities for insurers to detect fraud are greatly reduced. The only saving grace is that enquiries relating to non-routine matters or possible fraudulent claims will be 'dealt with as necessary'. Adjusters should therefore assess whether their enquiry is non- routine or related to a fraudulent claim and if so press the police for a response. Clearly the expense of responding to a tremendous quantity of correspondence is a drain on police resources. To some extent though it is perhaps a false economy for the police to isolate themselves from the insurance industry considering the resources possessed by the latter.

The 'Prevention of arson' report contained a recommendation that:

> Suspected fraudulent arson cases should be subjected to close, joint investigation by the police and loss adjusters.[70]

It is regrettable that since that recommendation was published in 1988 there have not been any positive developments to achieve a mechanism for such close joint investigation. All the while the costs of arson claims have been increasing.

Joint investigation could have benefits beyond the area of fraudulent arson. It is recommended that CILA opens a dialogue with ACPO to assess whether closer co-operation can be achieved between the police and loss adjusters. (Rec. II.17)

RESOURCES

The problem of resources was recognised in the 'Prevention of arson' report:

> The police suffer from a manpower resource problem in tackling arson. Since 1983 when prosecutions were already at a low level, there has been a manpower decrease by around 17 per cent, whilst at the

> same time arson offences are recorded by the police have increased by 12 per cent. If better results are to he obtained in the apprehension and conviction of arsonists, it will be necessary to find some means of developing more resources to the task.[71]

Insurers have an interest in minimising the extent of fraudulent claims whether arising from arson or any other cause. If greater co-operation with the police can help to produce an identifiable saving then perhaps insurers would be responsive to allocating a part of that saving towards improving police resources. In the UK, for example, at least one insurer has supported crime prevention activities by providing crime prevention officers with property marking kits.[72] An example from overseas is the support by an insurer of a police department in Australia through the purchase of a computer.[73]

BENEFITS OF CO-OPERATION

In his paper, John Dellow recognised the benefit to the police of co-operating with the loss adjuster:

> The detective who is dealing with an alleged case of arson is the same man who more regularly deals with cases of serious assault, robbery and sexual offences. He will require the benefits of your experience and expertise, and, of course, your more detailed knowledge of the history and financial stability of both the premises and the owner. This is especially important in establishing motives for arson.[74]

There are clearly areas where adjusters can obtain greater access to information than the police. The powers of the police to obtain evidence are in some areas less than the contractual rights of an insurer. In many cases the police need to show reasonable grounds for suspicion before searching for evidence. Loss adjusters however can ask the insured for all reasonable information and form a view with regard to suspicion after having actually obtained the information.

CIVIL PROCEEDINGS

The case of *Marcel v. Commissioner of Police* (1992)[75] considered whether the police could be required to produce for use in civil proceedings documents seized using their powers under the Police and Criminal Evidence Act 1984 without the consent of the person from whom the documents had been seized. It was held that the documents could be produced by the police on a *subpoena duces tecum* for use in civil legal proceedings if they were necessary to ensure a fair trial on full evidence, as the documents remained the property of the person from whom they had been seized, and that person would be liable to produce the documents under a subpoena.

Insurers have the 'Insurers rights' policy condition to support their request for information from the insured. Circumstances may arise where the police have documents which insurers have not been able to obtain but would like to do so for use in civil proceedings. Presumably the current position is that if insurers are in the course of civil proceedings and require documents from the police which had been obtained from the insured then that information can only be provided if the insured gives permission, a *subpoena duces tecun* has been served on the police, or if the court compels the police to produce the documents.

The true owner of the documents can exercise the right to challenge the subpoena on grounds such as legal professional privilege, privilege against self incrimination, or that it was oppressive.

Closer co-operation before proceedings could perhaps help to avoid technicalities relating to documentation adversely affecting the insurer's case.

RESEARCH

If co-operation between the police and insurers is to develop and produce beneficial results for both parties greater communication will be required. A dialogue between CILA and ACPO has already been suggested and perhaps one of the first items on the agenda could be research into the reasons for unsuccessful criminal prosecutions for arson and other fraud related charges. This could include cases where the CPS have declined to proceed with a prosecution. Shortcomings and inadequacies could be identified and help to indicate where strengthening of cooperation or an allocation of roles would be appropriate. (II. 18a)

Similarly an analysis of successful prosecutions would help to indicate whether the insurance industry has in fact been of assistance to the police. (Rec. II. 18b)

Research into large fire losses which have occurred during the past 24 months could also assist in drawing up an effective approach. (Rec. II.20)

Identifying the profile of an arsonist is of interest but as it would be likely to be based on the arsonists that have been caught it will not provide a full picture. The most interesting people to speak with would be the successful fraudulent arsonists who for obvious reasons are not readily identifiable!

ANTI-FRAUD INSTITUTION

To further co-ordination between insurers and the criminal investigation authorities, Munich Re71 has suggested that an anti-fraud institution should be set up by insurers to combat insurance fraud. Its role would be to:

Support the loss adjustment activities of insurance companies by:

- establishing the necessary lines of communication with the criminal investigation authorities;
- assisting the work of the criminal investigators through the supplying of information and by coordinating further procedure;
- helping the experts to detect the causes of loss; and
- co-ordinating the investigation work in the case of serial losses.

A further recommendation is that the staff of the antifraud institution:

Should intervene only in those cases in which the authorities are unable to pursue their enquiries further for one reason or another.

In view of the problem associated with the higher burden of proof for criminal prosecution any anti- fraud institution operated by insurers should not remain at a distance from enquiries. If it intervenes at too late a stage then the chances of a successful civil defence may be considerably reduced.

The proposed Active Investigation Department of the Arson Bureau (see chapter 4 and Rec. 11.19) could perhaps concentrate on large losses initially and formalise the current informal and relatively ineffective relations between the police and the insurance industry.

The lack of co-operation and information-sharing can also be seen in the various ways that statistics are maintained separately by the different parties involved with the issue of arson.

6. STATISTICS

Statistics—general

SOURCES

This chapter considers the statistical information on the incidence and cost of fire damage. The information was supplied by the following sources:

- Association of British Insurers
- Home Office
- Fire Protection Association
- police
- individual insurers and reinsurers.

Each body has its own reasons for recording the statistical information and it is unsafe to rely on statistics taken out of context.

The separate information-gathering processes of the individual bodies exemplifies the lack of co-operation and information exchange that is seen as a fundamental obstacle to detecting, prosecuting, and avoiding claims arising from fraudulent arson. There is a need for integration of the statistical information currently maintained separately by the different agencies. (Rec. III.1)

NATIONAL STATISTICS

The 'Prevention of arson' report 1988' which conceived the Arson Bureau as part of a National Arson Control Programme, made the following recommendation on national statistics:

> (2) We recommend that national arson statistics he improved and that the Arson Bureau investigate the possibility of establishing a national arson database.

Such an improvement in arson statistics seems unlikely without a co-ordinated assessment of the information and methods of the separate bodies listed above. It is not clear what information the arson database is to contain and whether it will extend beyond statistical data.

FIRE LOSS TOTAL

The 1990 material damage loss by fire is at least £l000m.2 A sum for business interruption should be added to this (which must be a guess) of say £750m. Losses to the economy also result from fire loss and an estimate of £500m. would seem conservative.

The total 'guesstimate' for fire loss is therefore:

	£ millions
Material damage	1000
Business interruption	750
Losses to the economy	500
Total fire loss guesstimate	2250

Arson guesstimate

The costs of arson are not at all clear. As discussed in the next section, material damage payments for arson damage could be in the region of500m. for 1990, i.e., 50 per cent of the total fire loss.

Business interruption payment statistics are not available. An estimate of750m. for fire-related losses would not appear unrealistic considering the total material damage fire loss. Assuming 50 per cent relates to arson then £375m. can be included in the arson guesstimate.

Losses to the economy are also not quantified although they can be expected. If fire losses to the economy were estimated at £144m. in 1973, a conservative estimate for 1990 could be £500m. with 50 per cent resulting from arson, i.e., £250m.

The arson guesstimate for 1990 comprises:

	£ millions
Material damage	500
Business interruption	375
Losses to the economy	250
Total arson guesstimate	1125

Fraudulent arson guesstimate

Fraudulent arson has been estimated to be about 20 percent of all material damage by fire. The guesstimate of total fire loss is £2250m. Therefore fraudulent arson costs £450m.

Unfortunately there are no hard, reliable figures or percentages for arson losses, let alone fraudulent arson. The figures for business interruption and losses to the economy also have to be approximations. Considering that records have been kept for at least the last 30 years it is a most unsatisfactory situation.

Association of British Insurers

1990 STATISTICS

The ABI collates statistical returns from insurers for fire claims on domestic and commercial policies. The figures relate to material damage costs. No account is taken of payments under business interruption policies or the wider losses to the economy caused by disruption of business and employment, lost overseas markets and lost production

Figure 1 shows that in 1990 the total estimated cost of all fire claims exceeded £l000m.

The director general of the Arson Prevention Bureau stated in September 1991 that:

Insurers estimate the cost of arson to them at around £500m., that is, half the total cost of fire claims.[3]

This has also been reported in *Post Magazine:*

The ABI believes that up to 50% of all fires can be attributed to arson.[4]

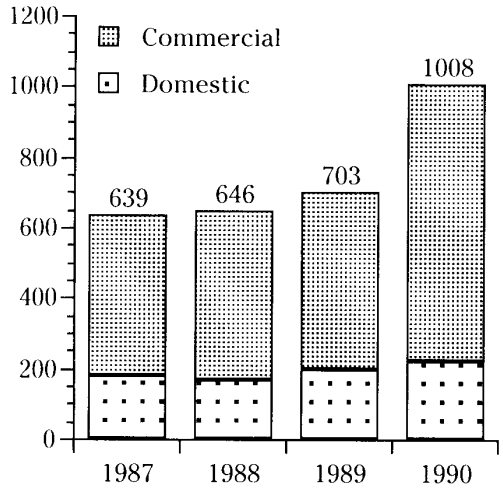


Fig. 1. Estimated fire claims 1987–1990 (£ millions).

Fraudulent arson

The ABI has been reported in the Daily Telegraph[5] and Lloyd's List[6] as stating that fraudulent fire claims are thought to have accounted for up to 20 per cent of the total material damage cost of fire in 1990.

The estimate of material damage costs from fraudulent arson is therefore over £200m. calculated as follows:

Total fire claims £1,000,800,000
Fraudulent arson @ 20% £201,600,000

As mentioned earlier the material damage loss is only part of the total fraudulent arson loss which could be as high as £450m.

Disappointingly, in view of the size and extent of the problem, the ABI publication Insurance statistics,[7] does not provide a percentage for suspected fraudulent arson but merely notes that an 'increasing incidence of large fire losses, many of which are believed to be arson, affected the commercial property account'.

1991 STATISTICS

The figures available at the time of writing relate to the first half of 1991. A comparison of the ABI figures for the first half of 1991 with the first half of 1990 is shown in figure 2.

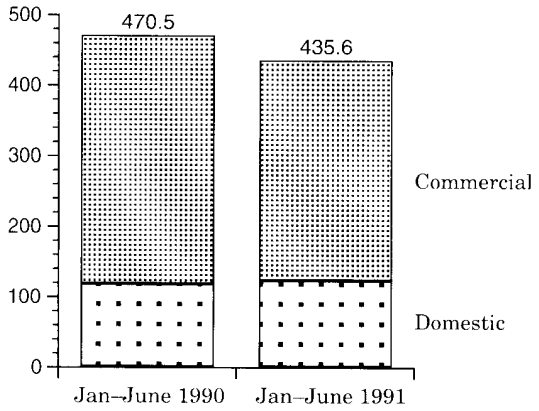


Fig. 2. Fire statistics—gross incurred claims (£ millions).

Source: ABI press release 6 September 1991

It seems that there has been an overall reduction in fire costs of 7.4 per cent. Although commercial losses have reduced by 11.1 per cent, domestic losses have increased by 3.5 per cent.

On the assumption that the second half of 1991 will not be greater than the first half then the total fire damage claims for 1991 could be as much as £871,200,000.

Arson

Based on the estimate that 50 per cent of fire losses are due to arson, then arson may have accounted for losses of £435m. in 1991.

Fraudulent arson

If the estimated 20 per cent fraudulent arson is applied to the total fire loss then insurers in 1991 may have paid out £174m. which should not have been paid. This does not include business interruption payments or losses to the economy.

LACK OF STATISTICS

There does not appear to be any solid basis on which the percentages of fire losses attributable to arson have been calculated. Indeed, they seem little more than guesses. Considering that statistics have been collected on fire losses since 1958, it is surprising, and a matter of considerable concern, to note the lack of detail relating to the extent of arson and of the important sub-group of fraudulent arson.

A statistical gathering exercise has been initiated by the fraudulent arson working group of the Arson Prevention Bureau. This will depend on the cooperation of insurers and loss adjusters. The information gathered will be subject to a decision about the cause of the fire by a loss adjuster and possibly also the fire brigade. However, for the reasons outlined in chapter 5 the adjuster may not be fully competent to make such a decision.

ADDITIONAL ASSESSMENT

It is suggested that a retrospective survey of claims over say the last two years should be conducted, perhaps starting with larger losses, to help improve the identification of the extent of arson and fraudulent arson. (Rec. III.2a) This exercise may also help to assess the accuracy of cause identification by loss adjusters and the fire brigade. (Rec. III.2b)

BUSINESS INTERRUPTION LOSSES

Although it is understandable that there would be a time lag in obtaining details of payments under consequential loss policies it is difficult to understand why these figures are not published as part of the fire damage statistics. (Rec. 111.3)

Home Office

The Home Office fire statistics contain information from local authority fire brigades on fires and casualties from fires. A major concern relates to death or injury.

These statistics are prepared from fire brigade reports and provide details of probable cause. This is based on probability and opinion, and not always proved conclusively by the brigade before preparing the report.

DELIBERATE FIRES

The latest available information from the Home Office at the time of writing is contained in the statistical bulletin entitled 'Summary fire statistics UK 1990'. Two key points mentioned are that deliberate and possibly deliberate fires increased from 2 per cent in dwellings to 15 per cent and from 5 per cent in other occupied buildings to 31 per cent. (Dwellings are premises occupied by households, excluding hotels, hostels and residential institutions, and since 1988 include mobile homes. Occupied buildings are buildings which are in use although not necessarily having people in them at the time of the fire.)

The increasing trend since at least 1979 has been attributed in part to improvements in identifying arson as a cause.9 This suggests that perhaps the true extent is even greater, but is not being identified.

The percentages of fires caused deliberately or possibly deliberately can be seen from table 1:[10]

Table 1: Deliberate and possibly deliberate fires in occupied buildings

Year	Total	Deliberate	Accidental	
	Number (=100%)	or possibly deliberate (%)	Total accidental (%)	Misuse of appliances (%)
Dwellings				
1981	56,000	8	92	42
1984	59,000	11	89	41
1989	65,000	15	85	42
1990	63,000	15	85	42
Other occupied buildings				
1981	39,000	21	79	13
1984	43,000	27	73	14
1989	46,000	29	71	14
1990	45,000	31	69	13

LOSS QUANTIFICATION

Information relating to the amount of the loss following a fire is not collected by the fire brigade. However, matching takes place with the Fire Protection Association records for fires costing in excess of £50,000.

LARGE LOSSES

A Home Office report in 1980" suggested that large loss fires comprise the majority of the total cost of fire damage each year. The report drew attention to the fact that:

> It is not only the nature of the occupancy and the source of ignition which cause a fire to become a large loss fire. Very often it is the delay which ensues between ignition and discovery. It is not surprising therefore that about two-fifths of large loss fires occur between 2200 and 0600 hrs, a period when fire incidence generally is light.[12]

Effective overnight guarding and surveillance may help to avoid or reduce the cost of large fires. (Rec. 1.9)

In his 1988 fire research lecture, Douglas Woodward, then director of the FPA, stated:

> Such fires tend also to be more expensive than accidental fires—on average about four times—and of course the reasons are not hard to find: the fires are begun in more than one place; accelerants are frequently used; fire protection equipment is often rendered ineffective.[13]

It is suggested that a study be undertaken of all large losses (whether paid or denied), starting perhaps with claims which have occurred in the past two years. If a consistent set of questions were to be applied to each large loss then it should be possible to analyse the data produced and identify the extent to which the large loss fire claims fall into the arson and/or fraudulent arson categories. 'Prevention of arson' reported that half of the large fires were believed to have been caused by arson. Considering that the large loss fires account for a significant cost but represent a relatively small number of losses a study could produce extremely useful information within a short time scale. (Rec. III.2)

Furthermore, any initiative to foster greater cooperation between insurers, adjusters, police and fire brigade should start with large loss fires where the incentive for all parties to succeed will probably be the greatest. (Rec. II.20)

LOSSES TO THE ECONOMY

The subject of consequential losses to the economy was studied for the Home Office by consultants in 1977 and the results issued in a report entitled 'Investigation of consequential losses to the economy from fires in industry, the service sector and commerce'.[14]

Consequential losses, and gains to the economy were considered to be the after-effects of fires on national income and output. The effects were said to arise from the adverse balance of trade movements, changes in the efficiency of resource use, and the diversion of resources from other productive activities.[15]

The report suggested that consequential losses to the economy stem very largely from the effects of a relatively small number of fires. Findings indicated the following:

> Fires in chemicals and allied industries and in gas and electricity have very large consequential loss to the fire-hit company, as they do to the economy.
>
> Consequential losses to fire-hit companies in manufacturing excluding chemicals are also large though less than those recorded for chemicals and gas and electricity.
>
> Fires in the service sector are associated with significant consequential losses to the fire-hit companies,

whereas the equivalent losses to the economy are negligible.[16]

Generally consequential losses to fire-hit companies were found to exceed consequential losses to the economy. However, two reasons for this not being the case were where:

> …sales lost by the fire-hit company pass to foreign competitors, when the company only loses the profit element of these sales, whereas the economy loses the equivalent of the full sales value in foreign currency earnings.
>
> sales lost by the economy pass to foreign subsidiary or parent companies of the fire-hit company; the economy loses the full sales value, the fire-hit company may lose very little at all.[17]

The following reasons for large consequential losses to the economy were given:

- the need to maintain supplies whatever the cost;
- loss of a major part of total UK capacity for producing a good or importable service;
- fire-hit company has foreign subsidiaries, partners or owners and 'buys in' from its foreign manufacturing base;
- damage, and consequent disruption of production, in a continuous process industry working at full capacity (24 hour day);
- product is unique and firm decides to maintain production at high cost;
- product faces strong foreign competition;
- fire-hit company is in manufacturing, has a number of plants working below capacity, and chooses to incur extra transport costs by shipping goods in from its other plants whilst the fire damaged establishment is producing below target.'[18]

The report identified spare capacity in the economy as the main reason why many large fires only produce a zero or low consequential loss to the economy.

Consequential gains to the economy were discovered in the form of long-term increases in efficiency where the following factors existed:

- absence of general overcapacity in the sector;
- buildings destroyed by fire;
- old building inefficient;
- management wise enough to replace the building with a more suitable one."[19]

For the years under consideration (1971 and 1973) total losses to the economy from fires in manufacturing, chemicals and the service sector were £60m. in 1971 and £144m. in 1973.

The extent to which the Home Office currently assesses the loss to the economy is not known and would be worth investigating especially if the losses can be traced to causes such as arson and categorised by value. (Rec. III.4)

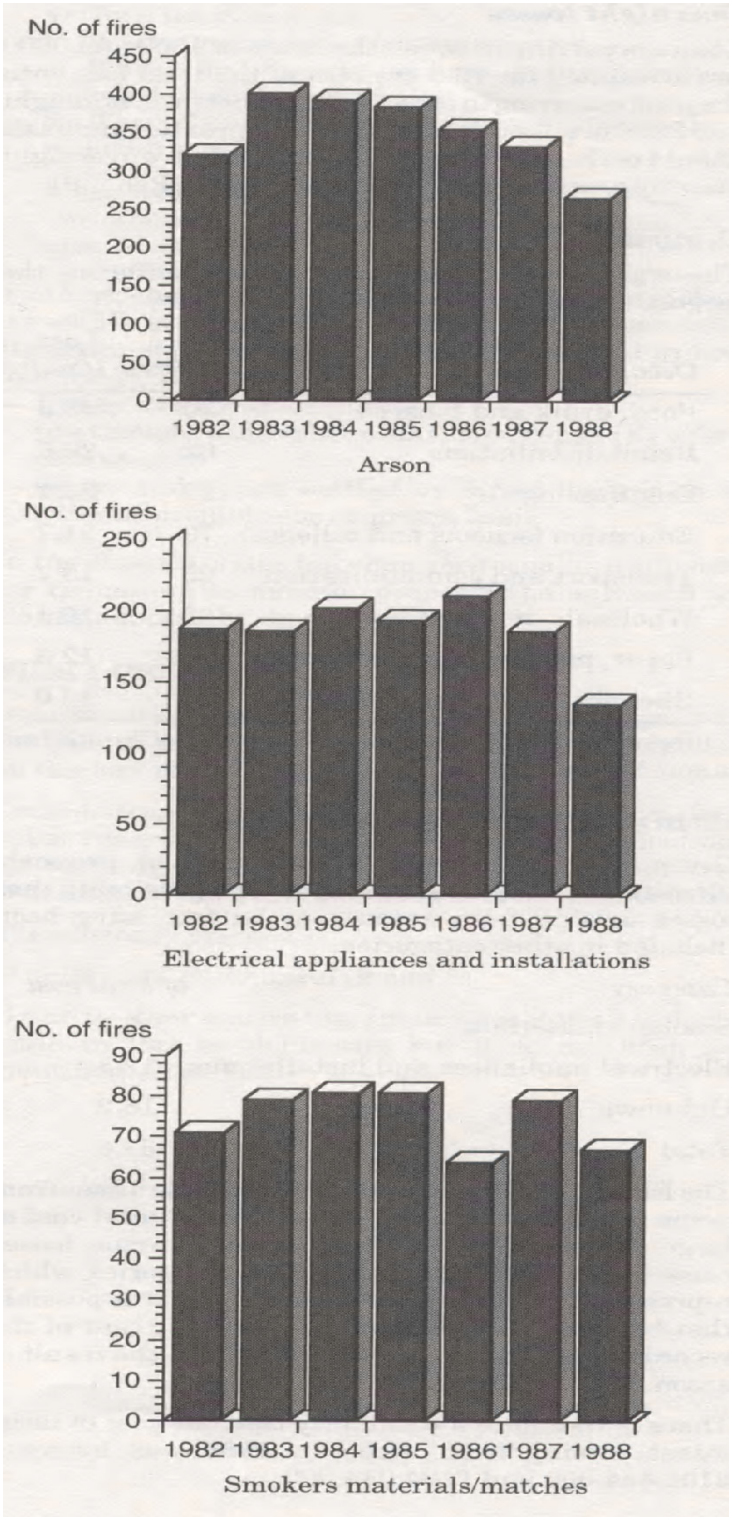
Fire Protection Association

ANALYSIS

The FPA annually issues an analysis of large fires, i.e., those costing more than £50,000. The last issued analysis appeared in January/February, 1991 for 1988. The time lag in publishing this information makes it difficult to assess its significance in current terms.

The total number of large fires decreased by 23.6 per cent from 920 in 1987 to 703 in 1988. There was a 16 per cent reduction in loss estimates from £315,984,000 to £263,360,000 in 1988.

While the incidence has become less frequent, the average cost of a large loss has increased by 9 per cent



from £343,000 to £375,000. Losses due to fires costing over Lim. increased from 51.5 per cent of all fires in 1987 to 53.7 per cent in 1988. However, one fire alone cost £33m. and this has undoubtedly distorted the figures.

Arson was by far the most common source of ignition for large fires in 1988 with electrical appliances/installations second and smoking materials/matches in third place as shown in the charts above.

Overnight losses

Losses occurring between the hours of 1800 and 0600 hrs accounted for 76.5 per cent of the total loss with the peak occurring in the early hours between midnight and 0200 hrs. As mentioned earlier, greater emphasis should perhaps be placed on comprehensive overnight guarding and surveillance to premises. (Rec. I.9)

Occupancy

The eight leading occupancy groups suffering the largest estimated losses are shown below.

Occupancy	*No. of fires*	*Loss (£m.)*
Food, drink and tobacco	30	43.3
Retail distribution	62	23.6
Engineering	23	23.1
Education (schools and colleges)	79	21.7
Transport and communication	25	18.7
Wholesale distribution	28	16.1
Paper, printing and publishing	20	12.3
Chemical and allied industry	13	12.0

Unfortunately no indication of the extent of fraudulent arson claims is given.

ERRORS IN CAUSE IDENTIFICATION

Given the problems and difficulties of properly identifying the cause of fire, there is a possibility that losses arising from arson may in fact have been included in other categories:

Category	% of total cost
Smokers materials	5.1
Electrical appliances and installations	12.3
Unknown	16.2
Total	33.6

The FPA figures indicate that identifiable losses from arson amounted to 40.8 per cent of the total cost of large fires in 1988. As there could be arson losses classified incorrectly in the other categories which represent 33.6 per cent of the total cost, it is possible that between 40.8 per cent and 74.4 per cent of the recorded large loss fires could have been the result of arson.

There is therefore a possibility that the cost of large losses arising from arson in 1988 was between £106,454,000 and £194,044,000.

It is recommended that a detailed analysis of large loss fires be undertaken. (Rec. 111.2)

Police

OFFENCES OF ARSON

The Home Office has published the following information relating to offences of arson recorded by the police in England and Wales:[21]

Year	*No. of offences recorded*
1985	19,003
1986	19,240
1987	18,920
1988	21,045
1989	23,710

CLEAR-UP RATE

Only 24 per cent (5642) of arson cases were cleared up in 1989.

An offence is said to be cleared up if:

- a person is charged, summonsed or cautioned for the offence (irrespective of any subsequent acquittal);
- the committing of the offence is attributed to a child under the age of criminal responsibility;
- the offence is taken into consideration by the court;
- a person thought to be guilty cannot be prosecuted or cautioned (e.g., because he has died);
- there is sufficient evidence to bring a charge but no further action is taken (the latter includes further offences admitted by convicted prisoners).

INCREASING TREND

An increasing frequency can be seen. There is some concern that the number of recorded offences is below the reality, as the police will not record a crime as arson without almost definite proof that arson has been committed. The real trend and number of arson offences could therefore be much greater than official figures suggest.

REQUIREMENT TO REPORT ARSON

Insurers already require an insured in certain circumstances to report a loss (usually theft or travel loss) to the police. A side-effect is that police statistics more closely reflect the true extent of such losses.

To improve police involvement insurers may wish to impose a requirement on policyholders to report a fire formally as arson if so required by the insurer. While this may not result in the police actually recording the fire as a case of arson, it would serve to bring the police into the case, something which a fraudulent insured may not relish. (Rec. III.5a)

QUANTIFICATION OF OFFENCES

It is not clear whether the police are able to quantify arson offences based on estimates in their files of the

damage caused. Co-ordination with fire brigade and FPA estimates might help to produce quantification of offences recorded and those cleared up.

UNDER-RECORDING OF ARSON

It is worrying to note that the 'Prevention of arson'[22] report stated that:

> We believe that arson is currently under-recorded in the United Kingdom. *A study needs to be made to determine the real extent of the crime.* It should focus in particular upon fraudulent arson, racial attacks and arson committed against business premises, in order to produce a more detailed and relevant prevalence statistics and to aid in the development of measures to prevent arson. The study of fraudulent arson needs to take place within a study of the extent and nature of commercial crime in general.

This seems to suggest two studies, both of which would be of significant interest to the insurance industry and the government. The first study would determine the extent of the crime of arson. The second would look at fraudulent arson within a general study of commercial crime. It is hoped that the Arson Bureau will consider both as suitable for priority attention and action. (Rec. III.7)

Individual insurers and reinsurers

INSURERS

Of the 32 respondents to the questionnaire to UK insurers[23] only 17 answered 'yes' in response to Question 6(a) as follows:

> 6. Are you able to categorise your fire claims statistics into:
>
> (a) Fire caused deliberately—persons unknown?
> (b) A sub-group of (a) where fraud is suspected by the insured?

Surprisingly, only five respondents said that they could identify the fraudulent arson sub-group mentioned in 6(b).

It would seem that at individual company level the UK insurance industry has not on the whole been recording and collating details of claims arising from fraudulent arson.

REINSURERS

In so far as reinsurers are concerned, the questionnaire[24] sought information on the extent to which the reinsurer maintained detailed claim statistics.
Questions 5 and 8 asked:

> 5. Please provide the following information relating to commercial fire claims:
>
> 1989 (£) 1990 (£)
>
> a) Total net claims paid
> b) Where fire caused by deliberate means
> c) Where fire thought to have been started/arranged by direct policyholder
> d) Where claim settled by direct insurer on without prejudice or ex gratia basis.'
>
> 8. Do you maintain records separating fire damage into categories of cause? If yes please list the cause categories.

The overwhelming outcome from the response is that it would be extremely difficult for reinsurers to generate statistics specifically identifying claims paid in the following categories:

- fire by categories of cause;
- fire thought to have been started/arranged by original insured;
- where claims are settled by direct insurer on a without prejudice or ex gratia basis.

In the absence of this information it would be difficult for reinsurers to monitor properly the approach to claims adopted by direct insurers.

FIRE LOSS BUREAU

Insurers are expected to report via the loss adjuster to the Fire Loss Bureau details of fire losses and values on the loss report form.[25]

Considering the concerns expressed earlier in this paper regarding the accuracy of cause identification by loss adjusters it is suggested that random examination should be undertaken of cases which are:

a) malicious (1)

b) deliberate or doubtful (2 and 3)

c) due to other causes (e.g., smoking materials) which could in fact be deliberate but have not been so identified. (Rec. III.6)

7. RESOLUTION

This section deals with the resolution of a claim by civil law and then looks at the criminal law aspects. The intention is to review key areas relating to the resolution of fraudulent arson rather than producing detailed comment on the effect of all policy terms.

Insurers have to confirm that various points have been complied with. Any non-compliance by the insured will strengthen the insurer's position to the extent that fraud and arson might not be used as a defence because another defence not subject to such a high balance of probabilities requirement will be more readily available, e.g., breach of warranty or nondisclosure. However a sophisticated, knowledgeable, and well-advised insured wishing to commit arson and obtain insurance monies is likely to pay careful attention to all the terms of the policy, to avoid the fraud failing from non-compliance with a policy term.

FUNDING INVESTIGATION

An important factor is the extent to which an insurance company is willing to commit funds to the investigation and defence of a suspected fraudulent arson claim. Question 4 of the questionnaire to UK insurance companies asked:

> Should the insurance company be prepared to fund and conduct all the enquiries necessary to successfully defend a claim arising from fraudulent arson?
>
> If yes, why?
>
> If no, why?

All the respondents were in favour of the insurance company resisting fraudulent claims, although the need to balance the cost of such investigations against the value of the claim was mentioned.

The theme of deterrence emerged from several responses, and the following are representative of such views:

> As discouragement to other potential fraudulent arsonists.
>
> Successful well-publicised cases should help to discourage others.

Several respondents considered that their companies had a duty to policyholders, shareholders and the public:

> We have a duty to resist fraudulent arson claims, to policyholders, shareholders and the public in general.
>
> Insurers have a duty to the community, shareholders and policyholders to defend vigorously (fraudulent arson) claims.

PUBLIC/CENTRAL FUNDING

A small number of respondents raised the subject of public funding and financial support from a central fund. Attitudes were at variance as the following two extracts indicate:

> It could be argued that access to a public fund and/or investigation facilities should be made available—especially as the costs of litigation/detailed investigation may put commercial pressure to compromise.
>
> Complications could arise if a central fund were set up to meet the relevant costs. Firstly, presumably there would have to be some vetting of individual insurer's decisions before the central fund would be committed as otherwise cases could be defended which would not have been if that insurer had had to pay the relevant costs. Secondly, there could criticism of such a fund.

While these responses support a tough approach to the resolution of fraudulent arson claims, it is unfortunate to note that insurers do not seem to have adequate records and statistics to confirm the effectiveness of their approach and the extent to which fraudulent arson claims are either successfully avoided or paid.

CO-ORDINATION OF ENQUIRIES

The marshalling of professional resources by the insurer during the detection and resolution stages was queried in question 8 of the questionnaire to UK companies which asked:

> During the investigation of a substantial claim thought to result from fire set by the insured do you:
> a) Co-ordinate all enquiries through a member of the claims department acting as co-ordinator?
> b) Expect the appointed loss adjuster to co-ordinate all enquiries?
> c) Instruct a solicitor to act as co-ordinator?

The responses numerically were:

Co-ordinated by	*No.*
claims dept	15
adjuster	13
solicitor	1

Six further positive replies were received with regard to solicitors on the basis that they were required to coordinate the0020case once legal proceedings were imminent.

The companies that indicated that the claim would be co-ordinated by their claims department generally mentioned that the actual enquiries would, however, be conducted by a loss adjuster reporting to and liaising closely with the claims department.

One insurer's view on the appointment of a solicitor is shown below:

> As far as instructing a solicitor is concerned, frankly we consider that to be a waste of money despite what certain practices would have us believe. We feel that we have more than sufficient expertise within our claims department.

TEAM APPROACH

The desire for a team approach involving all three parties was mentioned occasionally as the following example shows:

> Whilst the co-ordination would be through the claims department, the whole objective is that all parties would work as a team.

Although there is a certain similarity in approach to the investigation and resolution of fraudulent arson claims through the use of loss adjusters, the control of co-ordination is not standard throughout the companies that responded to the questionnaire.

The policy fraud exclusion.

DEFENCE OF FRAUD AND ARSON

Fire damage caused by arson is in itself covered by a fire policy. However, if the insured has been involved in some way with starting the fire then it is for the insurance company to set up a defence of fraud and arson. Typical fraud exclusions are:

> If a claim is fraudulent in any respect or if fraudulent means are used by the insured or by anyone acting on his behalf to obtain any benefit under this policy or if any DAMAGE is caused by the wilful act or with the connivance of the insured all benefit under this policy will be forfeited.
>
> If the claim be in any respect fraudulent or if any fraudulent means or devices be used by the insured or anyone acting on his behalf to obtain any benefit under this policy or if any destruction or damage be occasioned by the wilful act or with the connivance of the insured all benefit under this policy shall be forfeited.
>
> This Policy shall be voidable by the Insurers ... if any claim be in any respect fraudulent or if any false declaration be made or used in support thereof or if any loss be occasioned by or through the procurement or connivance of the insured.

BREACH OF UTMOST GOOD FAITH

The insured is required to observe utmost good faith which also means that any claim put forward must be honestly made. If it is fraudulent the insured will forfeit all benefit under the policy whether there is a condition to that effect or not.[1]

In *Britton v. Royal Insurance Co*. (1866) Willes, J, stated:

> The contract of insurance is one of perfect good faith on both sides, and it is most important that such good faith should be maintained. It is the common practice to insert in fire policies conditions that they shall be void in the event of a fraud, and there was such a condition in the present case. Such a condition is only in accordance with legal principle and sound policy. if there is wilful falsehood or fraud in the claim the insured forfeits all claim whatever upon the policy.[2]

EXAGGERATION

In considering the subject of fraudulent claims Ivamy[3] considers that an exaggerated claim is to be considered fraudulent in the following cases:

> 1) Where the insured clearly intended to defraud the Insurers
>
> 2) Where the over-estimate of his loss is so excessive as to lead to the inference that the insured cannot have made the claim honestly but must have intended to defraud the Insurers.
>
> 3) Where the over-estimate, though not deliberately put forward with the directly fraudulent intent of inducing the Insurers to pay the full amount claimed, is designedly made for the purpose of fixing a basis upon which to negotiate with the Insurers.

Cases referred to in support of the above points are:

1) Chapman v. Pole (1870)[4] where the insured claimed inter alia £30 for the contents of a room, the real value of which was £3, and £33 for crockery worth a few shillings.

2) Goulstone v. Royal Insurance (1858)[5]: where the insured claimed £200 for property worth £50.

3) London Assurance v. Clare (1937)[6] where Goddard, J, in directing the jury said that:

> Mere exaggeration was not conclusive evidence of fraud for a man might honestly have an exaggerated idea of the value of the stock, or suggest a high figure as a bargaining price.

Method of trial

If the insurer delays or refuses to pay the claim then the insured will be obliged to issue legal proceedings.

The onus of proving fraud as a defence to the insured's claim rests with the insurer. A claim by the insured submitted against the insurer in the form of a writ will result in a defence by the insurer and eventually a trial.

The trial will be heard by a judge and as it is a civil case there is no jury. However, considering that insurers are required in their defence to prove arson to a high degree of probability (which can be regarded as almost but not quite attaining the criminal standard of beyond reasonable doubt) it would perhaps benefit both parties if such cases were heard by a jury. One of the main functions of a jury is to form a view on the character and honesty of the parties involved.

Sir Denis Marshall in a paper 'Arson and fraud—the role of insurer's lawyers',[7] stated:

> Impartial though our Judges are expected to be, many regrettably have had brushes with insurers during the course of their career either in their personal insurances or when acting for or against insurers prior to their elevation to the Bench. While they may be relied on to interpret the evidence and the law fairly and impartially, it is difficult wholly to ignore their own experiences, and it is surprising when one sits in judgement on the matter how the evidence coming before them appears in a rather different light to the way in which it appears to the parties to the proceedings and their legal advisers.

A problem with having a jury trial is that insurers are sometimes regarded as having deep pockets as the experience of US jury trials have shown in such areas as damages for liability and actions for bad faith.

A civil case concerning arson, Slattery v. Mance[8] was, however, heard in 1962 in the Queen's Bench Division by a jury. The jury seems to have been able to cope with the technicalities of the case and found that:

1) The plaintiff (policyholder) did not cause or connive at destruction of his yacht.

2) The representation of the value of the yacht made by the plaintiff in the proposal form was untrue.

3) That the representation in 2) was material.

4) That the representation was not made fraudulently.

The jury had an opportunity of seeing the policyholder and other witnesses during the trial and seems to have formed a view on their character and honesty without being influenced by the depth of the insurer's pockets.

Onus of proof

It is for the insurer to prove that the insured started the fire or caused it to be started.

Slattery v. Mance[9] held that once it was shown that loss was caused by fire, the plaintiff had made out 'a prima facie case and the onus was therefore upon the insurer to show that, on balance of probabilities, the fire was caused or connivanced at by the plaintiff.'

If arson is found to be the probable cause then it may be preferable for insurers to then require the insured to show that he did not start the fire. This reversal of the burden of proof was found in exception 19 (civil commotion etc. peril) of the insurance policy in the case of *Spinneys (1948) v. Royal Insurance Co. Ltd* 1980[10] where the clause stated:

> *In any claim*, and in any action, suit or other proceeding to enforce a claim under this insurance for loss or damage, the *burden of proving* that such loss or damage does not fall within this Exclusion shall be upon the assured.

It was decided that the insurer must prove evidence from which it can reasonably argued that:

i) an event occurred falling within the exception, and

ii) that excepted peril caused the loss.

In appropriate cases (e.g., trade or geographical area) a reverse burden clause could be inserted into a fire policy so that fires caused by arson would not be covered unless the insured could prove that he or she did not cause the fire. (Rec. IV.5)

BALANCE OF PROBABILITIES

The distinction between achieving success in a criminal prosecution and success in a civil defence by insurers can be seen in the case of *Broughton Park Textiles v. Commercial Union Assurance*[11] where Simon Brown, J, stated:

> It is clear that to succeed in their defence the defendants have to discharge the burden of proving that fraud and indeed proving it to a high degree of probability, a degree of probability commensurate with the seriousness of the charge which they allege against Mr Cohen. They do not, however, have to prove their allegation of arson beyond all reasonable doubt to criminal standard and in fairness to Mr Cohen I make clear that if I was sitting in a criminal jurisdiction I would not be prepared to find the case proved.

HEAVY BURDEN OF PROOF

Whereas the police are obliged to satisfy the criminal onus of proof, i.e., 'beyond reasonable doubt' insurers will only need to prove on 'a balance of probability' basis. However, there is a 'heavy burden of proof which rests on the insurers' according to Neill, J, who also said in *Watkins v. Legal & General*[12]

> I should not make a finding that Mr Watkins deliberately set fire to this warehouse unless I am satisfied that there is a high degree of probability that he did so.

As Lord Denning said in *Hornal v. Neuberger Products Ltd*[13]

> Most people would say that where there is a serious allegation such as arson there must be a very high degree of proof.

In *Bater v. Bater*[14] Lord Denning, stated, and this was repeated and affirmed in *Hornal* that:

> The difference of opinion which has been evoked about the standard of proof in recent cases may well turn out to be more a matter of words than anything else. It is of course true that by our law a higher standard of proof is required in criminal cases than in civil cases. But this is subject to the qualification that there is no absolute standard in either case. In criminal cases the charge must be proved beyond reasonable doubt, but there may be degrees of proof within that standard. As Best, CJ, and many other great judges have said, 'in proportion as the crime is enormous, so ought the proof to be clear'. So also in civil cases, the case may be proved to be a preponderance of probability, but there may be degrees of probability within that standard. The degree depends on the subject-matter. A civil court, when considering a charge of fraud, will naturally require for itself a higher degree of probability than that which it would require when asking if negligence is established. It does not adopt so high a degree as a criminal court, even when it is considering a charge of a criminal nature; but still it does require a degree of probability which is commensurate with the occasion.

DEGREE OF PROBABILITY

In July 1990 the Judicial Committee of the Privy Council delivered a judgment in Tricanipillay[15] which arose at first instance from the Supreme Court of Mauritius and had in the interim been considered by the Court of Appeal. The Court of Appeal judgment indicates that counsel acting for the insured argued that the standard of proof applicable to the insurance

company, in a case where a criminal act or else complicity in a criminal act is alleged against the insured, would have been that which applies in a criminal prosecution. The Court of Appeal refused to accept this proposition and confirmed that the standard of proof which lay on both parties for their respective contentions always remained that applicable in civil proceedings, that is to say a standard that is based not on conclusive proof but rather on a balance of probabilities. The Privy Council judgment stated:

> The Court of Appeal were right to reject the submission that the burden on the insurance company was the criminal standard of proof. But, nevertheless, bearing in mind the gravity of the allegation, which was arson of an occupied building, a high degree of probability was required to discharge the civil burden of proof.

SOURCE OF EVIDENCE

In the publication Arson it is suggested that:

> The main source of evidence on the insurer's side is that given by the police.[16]

Taking into account the problems experienced by the police, discussed in chapter 5, the author would respectfully disagree and suggest that the main source of evidence on the insurer's side is that obtained by the loss adjuster and the forensic scientist.

Arson continues in the same paragraph:

> His (the insurer's) chances of success lie in the offender already having been convicted of arson by a criminal court.[17]

This is not the case in the UK because the police have to prove a criminal prosecution to a higher level than that required by insurers in a civil defence.

The greatest chance of success perhaps lies in a detailed investigation by the loss adjuster and forensic scientist with the sole aim of preventing a payment by insurers if the loss results from arson by or with the connivance of the insured. An insurer can successfully defend the claim on balance of probabilities even when the insured had avoided criminal prosecution.

Arson also states that:

> When it comes to arson, in particular, the interests of the fire insurers and the police are identical.[18]

It is hoped that the exposition above has indicated that as far as the UK is concerned, the interests of insurers and the police are not identical.

INSURER'S INVESTIGATIONS

In *Arson* it is suggested that:

> Insurers should only set investigations of their own in motion, if—for whatever reason—the police are making no progress in their own investigations.[19]

This proposal represents a very serious risk to the insurer resulting from delay in starting investigations. While the police and insurers should certainly work together, their aims and resources are different and, although co-operation can be advantageous to both parties, it is in the insurer's interest to control from outset all aspects of the investigation. The terms of the policy provide the insurer with powers similar to, and in certain respects greater than, those enjoyed by the police. Possibly only the insurer's customer care considerations provide a check on the way the insurer's investigations proceed.

UK SITUATION

The situation, as far as UK law is concerned, would not appear to be as stated in the following extract from a later Munich Re publication, Insurance fraud:[20]

> In a case of fraudulent arson, the insurance company is not liable to pay compensation, since the loss was deliberately perpetrated. The company is therefore relieved of any obligation:
>
> 1) if arson is determined beyond all doubt as being the cause of the loss,
>
> 2) and if it can be proved that the policyholder is guilty of the crime.

It is submitted that the correct position, for the reasons outlined earlier, is that the insurance company is relieved of any obligation if arson by or with the connivance of the policyholder is on the balance of probabilities proven by the court, taking into account the high probability required given the nature of the allegation.

Connivance

DEFINITIONS

Webster's Dictionary defines connivance as:

> The act of conniving; feigned ignorance or tacit encouragement of wrong doing.

And connive as:

> ….to overlook a fault or other act and allow it to pass unnoticed; to conspire.

The word conspire introduces conspiracy which is one of the criminal elements considered in the general discussion of fraud later in this section.

WHO DID IT?

In S & M Carpets[21] the crucial question of who started the fire was considered. Ormrod, L J felt that 'looking at it in perspective there really is no-one else who could have started this fire except somebody acting on behalf of the plaintiffs.'

The Court of Appeal in *Tricanipillay*[22] allowed the appeal from the insurance company holding that it had proven that the appellant (insured) had at least connived at setting the fire. This finding (which was then overturned by the Privy Council) appears to relate to the insured's employee, Idriss Gopal, who was suspected of setting fire to the premises. However, no criminal proceedings were ever brought against Gopal or any other person.

Connivance might be suspected for example if there were no signs of any forcible entry into the premises. Providing that key holding was strict (which should

be required by a properly organised insured) the inference could be drawn that either the insured's keyholders or another party (e.g. a professional arsonist) had entered the premises with keys. However, an expert thief could possibly have entered a building without forcing entry, and issues such as this have to be very carefully considered and balanced.

The case *of Exchange Theatre* v. *Iron Trades* (1983)[23] found that the origin of the fire and subsequent explosion had been deliberate but the judge was not satisfied that the directors of the insured company had connived or conspired at the fire. The judge profiled the arsonist as 'X' and on the balance of probabilities was not convinced that the insured's manager was 'X'. The possibility that a professional arsonist may have been involved does not seem to have been raised as an issue.

Non-disclosure and other coverage issues

An insurer may defend a claim if a non-disclosure is discovered during the investigations.

VITAL FACTS

> It is of the highest importance in the art of detection to be able to recognise, out of a number of facts, which are incidental and which vital. Otherwise your energy and attention must be dissipated instead of being concentrated.[24]

The adjuster's enquiries should bring to light vital information which will indicate whether there has been a non-disclosure of a material fact, i.e. that the insured is in breach of the utmost good faith doctrine. This was defined in Carter v. Boehm[25] (1766) by Lord Manfield:

> Insurance is a contract upon speculation. The special facts upon which the contingent changes to be computed lie most commonly in the knowledge of the assured only; the underwriter trusts to his representation, and proceeds upon the confidence that he does not keep back any circumstances in his knowledge to mislead the underwriter into the belief that the circumstance does not exist ... although the suppression should happen through mistake, without any fraudulent intention, yet still the underwriter is deceived and the policy is void; because the risk run is really different from the risk understood and intended to be run at the time of the agreement.

The avoidance of policy liability due to a non-disclosure which is irrelevant to the loss is often referred to as a technical defence. Indeed a Law Reform Committee report published in 1957 felt that in practice it was thought unlikely that a reputable insurer would rely on a technical defence to defeat an honest policyholder. In a case where arson and fraud are suspected, however, the insurer may decide to use every available valid defence.

PRIVATE CAPACITY CLAIMS

The ABI Statement of General Insurance Practice[26] states:

> 2. (b) An insurer will not repudiate liability to indemnify a policyholder:
>
> (i) on grounds of non-disclosure of a material fact which a policyholder could not reasonably be expected to have disclosed;
>
> (ii) on grounds of misrepresentation unless it is a deliberate or negligent misrepresentation of a material fact;
>
> (iii) on grounds of a breach of warranty or condition where the circumstances of the loss are unconnected with the breach unless fraud is involved.

However, the statement of practice applies only to general insurances of policyholders resident in the UK and insured in their private capacity. There is no similar statement of practice for commercial insurance. Disputes over personal lines insurance can be referred to the insurance ombudsman who does not at present have any involvement with commercial insurance. Therefore the resolution of a commercial claim depends on the terms of the policy and the law, rather than on statements of practice or the insurance ombudsman's body of previous decisions.

There has been mention of extending the role of the ombudsman to include commercial insurance, although the complexity and values involved would result in a significant increase in the ombudsman's workload. The amounts involved in commercial claims could in any event cause one of the parties to issue legal proceedings if unhappy with the ombudsman's finding.

Possibly the rewording of the arbitration clause to allow for or indeed require arbitration on policy liability rather than just quantum might produce a more satisfactory mechanism for all the parties involved. (Rec. IV.6)

CONSUMER PRESSURES

Consumer pressure on the non-disclosure issue is causing insurers to lose protection against fraudulent claimants. While recognising that genuine injustice should be prevented, the insurer surely needs access to some form of legal defence against a claimant who:

—inadequately explained the risk, and/or
—failed to follow agreed procedures and/or
—seeks to submit a fraudulent claim.

The consumer lobby should perhaps give more thought to ways of protecting the funds of innocent policyholders against fraudulent claims.

Is the current approach of indulging the individual to the detriment of the group of other policyholders correct? Should insurers, possibly through the ABI, seek support from the consumer lobby on ways to protect policyholders' funds from fraud? (Rec. IV.7)

PROPOSAL FORM

The absence of a proposal form is often regarded as a major obstruction to the insurer's opportunity to raise a non-disclosure defence. However, absence of a form may not be a total handicap. The case of *Woolcott v. Sun Alliance* (1978)[27] held that the mortgagor

when he completed the form for a loan was under a duty to disclose his criminal record, for by that application he was accepting that the building society would effect the insurance on his property on his behalf as well as on their behalf. The mortgagor became a policyholder without filling in a proposal form and was considered to be under a duty to disclose.

OTHER COVERAGE ASPECTS

In addition to the non-disclosure issue, there are other aspects which should be dealt with during a full and conscientious investigation by the loss adjuster. These will include:

—compliance with warranties;
—insurable interest;
—retention of title by suppliers;
—mis-description;
—alteration of risk.

Completed proposal forms, supplementary information requested from the insured, and even insurers' surveys of the premises will not remove the risk that the property will be damaged by fire. That is the purpose of the protection provided by the insurance policy. However, such documents describe to the insurer the physical risk and confirm information provided by the insured. If this information is later found to be incorrect then the insurer may have a defence to a claim.

Repudiate or pay?

If insurers decide to repudiate they need to consider properly the method of advising the insured. An insured that succeeded in a claim against insurers where insurers had raised the defence of arson might try and proceed against the insurer, and possibly the insurer's agents such as the adjuster or forensic scientist, for damages for defamation. The success of such an action would depend on the circumstances and whether the insurer's opinions and repudiation were transmitted to other parties.

In his article 'Fraudulent claims', R.H. Dulwich[28] recommends that counsel should settle (draft) the letter of avoidance setting out the grounds for rejection which will also form the basis of the defence. He suggests that the insurer should write direct to the policyholder although if a solicitor has already been instructed by the insured then it is preferable for the letter to be written to them by the insurer's solicitors. He also suggests that the possibility of a future allegation of libel could possibly be minimised by addressing the letter to the senior partner marked 'strictly confidential'.

Insurers should seek an opinion or legal guidance in this area as well as the wider issue of providing information to the police. (Rec. IV.8)

The majority of insurers who responded to the UK company questionnaire (questions 6 and 7), do not keep any form of statistics indicating when a claim has been paid even though there was suspicion that it was fraudulent. (See chapter 6)

DECISION PROCESS

Decisions are undoubtedly made every day in the claims departments of insurance companies and Lloyd's syndicates as to whether a claim should be paid even though certain aspects are unsatisfactory and tend to indicate a fraudulent element. The extent to which there is an objective test to be applied to such claims is not known but considered unlikely.

The questionnaire responses suggest that suspect claims are referred upwards within the insurer's hierarchy. A senior claims supervisor or manager will usually decide whether a case should be defended. However, this depends on such cases being spotted in the first place by the adjusters and the claims staff dealing with the case supervision. Personal judgments will be based on knowledge and experience which will of course vary. Marketing and client relationship considerations will also be taken into account. It is therefore possible that individual companies may differ significantly in the way a particular claim would be dealt with.

FINAL RESPONSIBILITY

Given the subjective approach to considering a doubtful claim perhaps the directors and shareholders of individual companies should take final responsibility for deciding to pay a suspect claim. The management will undoubtedly have internal guidelines. However, it could be questioned whether external shareholders, reinsurers and genuine policyholders fully appreciate the subjective nature by which claims are considered and paid. This is especially important as the control and management of funds outwards is a significant factor in achieving underwriting profit and increasing shareholder value. (Rec. 1.11)

Solicitors

As discussed earlier in this chapter, most respondents indicated that they tend to rely on an adjuster to deal with the claim investigation. The responses to question 3 (iii) suggest that the appointment of a solicitor is predominantly at the legal advice stage by which time important evidential aspects may have not been given sufficient attention.

> 3. At what stage would you instruct: iii) legal adviser, solicitor/attorney?

The answers fell into four clear categories:

1) To assist in investigation	9%
2) On advice from adjuster	19%
3) When legal advice necessary	34%
4) When litigation likely	38%

There is perhaps merit in instructing a solicitor immediately the adjuster becomes suspicious about the possible cause and involvement of the insured. A conference between the adjuster, forensic expert and solicitor at an early stage would enable tactics to be decided and a future strategy agreed. As information then becomes available the solicitor can provide legal

input and advice in a timely fashion. There are several advantages to this method of operation:

1) The adjuster and solicitor develop a relationship of trust and co-operation.

2) The solicitor does not have to climb a learning curve on the circumstances of the case (which often happens if the solicitor is not instructed for weeks, months or years later).

3) The solicitor takes more responsibility for identifying evidence for collection in the knowledge that it is the solicitor who will be responsible for defending the claim in litigation.

4) The protection of privilege can be applied to communications at an early stage. This will apply to communications:
—between insurer and solicitor of a confidential nature giving legal advice;
—from other advisers (e.g., adjusters) where the dominant purpose for preparing the document is in contemplation of litigation.[29.]

It is suggested that insurers should clearly set out a brief for the solicitor at the outset to establish the advice and involvement required and the relationship between the other advisers involved. A time and cost budget should also be agreed.

Policy wording changes

Insurers could perhaps give consideration to changing the terms of the insurance contract.

DIFFERENCES

The UK insurers that replied to the questionnaire also in general supplied copies of their fire policy, proposal form and claim form. A review of the policy wordings revealed differences in layout, format, and wordings for particular clauses. Such differences must make life difficult for the insurance intermediaries but no doubt profitable for the legal advisers!

A review of policies in use overseas revealed one condition, used in policies in Asia, but not found in UK policies. This condition, usually General Condition 19, reads as follows:

> TIME LIMIT FOR COMPANY'S LIABILITY
>
> 19. In no case whatever shall the Company be liable for any loss or damage after the expiration of twelve months from the happening of the loss or damage unless the claim is the subject of pending action or arbitration.

This clause seeks to provide a long-stop and perhaps places more certainty on the future handling of the claim. The policyholder is left in little doubt of the need to commence proceedings or place the claim into arbitration within 12 months of the loss date.

UNCERTAINTY

A common concern expressed by insurers relates to the uncertainty over whether a repudiated claim will be challenged by the insured. Often files are kept in abeyance and reserves are maintained against such claims for several years while a low profile is maintained. Incorporation of a condition similar to that shown above would provide insurers with the protection of a one-year contractual limitation period. If the insured did commence court or arbitration proceedings the matter would still be relatively fresh and evidence perhaps more readily available and reliable.

The condition would be a useful protection against suspect claims in general, not just those arising from fraudulent arson. (Rec. IV.9)

SHORT-NOTICE CANCELLATION

A suggestion by the Insurance Information Institute of New York'° is that the wording of the insurance policy should be amended so that it can be cancelled at short notice, for example when key warning signals are triggered indicating a potential for arson fraud. However, as most UK policies contain a seven-day cancellation clause there is no need to amend the UK wording. Perhaps a monitoring system to identify key warning signals would be worthwhile although it would undoubtedly increase the expense ratio of the insurer.

PERIODIC REPORTING

It is not uncommon for financial institutions to require periodic reporting from their clients with regard to trading, asset values, etc. Such an overt monitoring system by insurers might encounter resistance, but a precedent exists already in the use of periodic declarations of stock value.

Neil Kelly[31] suggests that a proposer's accounts should be studied carefully in advance of the insurer accepting the business. Perhaps in addition insurers would benefit from periodic (say quarterly) reports from certain insureds dealing with key factors of the business concerned. (Rec. 1.18)

Periodic reporting would serve the dual purpose of highlighting any adverse change in the risk and providing a record of information for analysis in the event of a loss.

If post loss inquiry shows that the information was false or incorrect then policy coverage may be in jeopardy.

SURVEILLANCE

A covert monitoring system, using the resources of a third party for selected insureds, might also be worth considering. On receipt of information indicating a potential increase in the factors likely to produce arson or fraud, the insurer might consider contacting the insured. If such contact failed to reassure the insurer then the cancellation condition is an option.

IMPACT OF CANCELLATION

The insured should recognise that the insurer deserves the courtesy of a response and should be made to realise that the problems flowing from the policy being cancelled will include:

— difficulty in arranging alternative cover in a short *space* of time;
— the stigma of having had a policy cancelled, a fact which will have to be disclosed in the future to all potential insurers probably for at least three years.

It is also in the insurer's interest that an insured suffering difficulties overcomes them satisfactorily. Just as banks operate 'intensive care' treatment for customers in difficulty, perhaps insurers especially in times of recession should develop such an approach. While intended fundamentally to protect the insurer's position the approach could be seen in a supportive light. The potential fraudulent insured may be dissuaded from using the insurance policy as a means of escape from a trading problem, but if not will recognise that the insurers are already aware of the condition of the business. This interim detection approach (i.e., between underwriting and claims stage) could if organised properly and widely publicised, act not only as a deterrent but also as a source of valuable information in the event of a claim.

Criminal prosecution

WOULD INSURERS BENEFIT?

Given the higher burden of proof required for a criminal prosecution it is perhaps questionable whether insurers would benefit from handing over to the police evidence which could be significant in a civil case. If an insured is successfully prosecuted then that insured may think more carefully about the merits of pursuing a civil case. The evidence to secure a criminal prosecution should be more than sufficient to secure a civil defence by insurers. Indeed the insured might feel precluded from pursuing a civil case by reason of being in prison!

Recent cases indicate that even though criminal charges have failed against the insured it is still possible for insurers to successfully defend a civil case. For example, in *Blackmans Glass* v. *New Zealand Insurance*[32] the insurers alleged that the fire had been started deliberately by two members of the insured company. This allegation was made despite the fact that criminal charges against both men of conspiracy to commit arson had been dismissed by magistrates at the committal stage in January 1990.

The earlier case of S *& M Carpets*[33] also resulted in a successful defence for the insurers despite the fact that the CID decided not to prosecute two key suspects, one of which was the insured company's managing director.

LEGAL COSTS

Even with a successful defence, the insurer still suffers a loss because of the high costs of mounting such a defence and the limited prospects of recovering these costs from the claimant.

If insurers are to minimise costs from fraudulent arson claims then consideration should perhaps be given to the way in which criminal prosecutions are assisted by the insurer. If there is a prospect of helping to achieve a successful criminal prosecution, and if that will deter the insured from pursuing a civil case at all, then insurers will clearly benefit because they will not have to pay the attendant costs involved in defending the claim at court (which can run into tens and hundreds of thousands of pounds).

There is some concern however that an unsuccessful criminal prosecution could affect the value of evidence gathered by insurers for a civil defence.

SUPPORT FOR THE POLICE

At the 1991 CILA educational conference[34] delegates at the fraudulent arson workshop were informed by a senior police officer that the police would benefit from support from insurers and especially loss adjusters. Background information to assist in the assessment of motive and opportunity would be of particular interest.

As discussed in chapter 5, there does not seem to be any formal arrangement for co-operation between insurers and the police. In the absence of an agreed procedure, it is probable that the views, attitudes and time constraints of individual officers will influence the extent to which the police will seek and make use of information available from the insurance claim investigation. Insurers and the police need to cooperate but the financial reality is that the police have limited resources and it is insurers that have most to gain by avoiding the cost of an unnecessary claim payment. Perhaps this financial aspect requires realignment possibly in the form of insurance sponsorship of police enquiries either on a case-by- case basis or at a national market level. (Rec. 11.16)

SURVEY

The response to question 5 of the questionnaire to UK insurers showed general agreement to offer reasonable assistance to the police. The question asked:

> 5. Would you be willing to support the police force in their efforts to obtain a criminal prosecution of the insured? If no, why? If yes, how?

A selection of responses is detailed below:

> —Our files will be made available together with any individuals who might have dealt with the insured. We would offer reasonable assistance to the police in such circumstances.
>
> —It is important to co-operate fully with the police to enable them to bring about a criminal prosecution. We would always be prepared to release to them copies of whatever information may be of use.
>
> —Access to any file / reports / evidence / investigations that we have which they may wish to see. If the police feel that they are in a position to prosecute, it would be the correct action for us to support them.

A minority indicated a sceptical approach, typical responses being:

> —Yes, exchange of information provided it was two way.
>
> —Yes — we see it as the duty of insurers to support the police in their efforts to bring criminals to justice. However, in a case where the evidence may not be

> sufficient to discharge the criminal onus of proof but is sufficient to meet that required by the Civil Law we may discuss with them the possibility of their charges not being pursued. An unsuccessful criminal prosecution could have some effect upon a civil action.

It is doubtful whether the police are fully aware of the apparent desire of some UK insurers to provide information to support a criminal prosecution. However, the police have indicated that insurers tend to be reluctant actually to act as the complainant.

IMMUNITY

No insurer mentioned any possible action that an insured might take on learning of the insurer's cooperation with the police prosecution, especially if the prosecution failed. As discussed earlier, it is suggested that insurers should clarify the legal position and lobby for immunity from any potential action from an insured resulting from such co-operation. (Rec. IV.8)

REWARD

Question 9 in the questionnaire to UK insurers asked:

> 9. Would you consider offering a reward for information leading to conviction of person(s) responsible for setting the fire?

The respondents were in favour of a reward by a ratio of 2:1. Of those in favour 30 per cent stressed that any such reward would have to be arranged with the agreement of the police concerned.

Several insurers questioned the benefit of a reward bearing in mind that a recovery would be unlikely (as against say a theft reward where often all or part of the stolen property is recovered).

Two responses of particular interest are shown below:

> —Each case would have to be treated on its merits but we do not find favour with this type of reward system as inevitably it must attract the person who has actually committed or has been involved in the said arson. We cannot think of any cases where we have offered such reward.
>
> —We would be very hesitant in taking this course of action and certainly, we would seek legal advice before doing so. Paying for information which it is a citizen's duty to provide does not appeal to us. The payment may 'taint' the evidence of such a person if called as a witness and would place us in a somewhat dubious position if they had to provide evidence in a civil action on our behalf. There is also the question that the only way we can gain is if the information relates to the conviction of our insured. If anyone else is proved to have started the fire then, in the absence of connivance with our insured, it is most unlikely that we will obtain any financial advantage.

These responses do not consider the deterrence aspect.

THE AUSTRALIAN EXPERIENCE

In general while insurers expressed an interest in the idea of a reward there were some reservations. Insurers in the UK as a group do not have any form of arson reward scheme in operation.

In assessing whether such a scheme would be of benefit it is worth examining the Arson Reward Scheme operated by the Insurance Council of Australia Ltd (ICA). In the mid 1980's arson in Australia escalated dramatically and was attributed to the start of an economic recession. The police appear to have approached the insurance industry with a request for funds to pass on to informants.

This request was considered unacceptable, but rather than ignoring the request ICA developed the Arson Reward Scheme. This began in the state of Victoria about four years ago and has now been expanded to all the states in Australia.

Briefly, the scheme provides for a reward with an upper limit of Australian dollars A$25,000 (approx. £10,400) for information 'leading to the conviction of any person for destroying or damaging property in the State, insured by a participant in the scheme, through an act of arson'.

There are three situations:

1)—Conviction of the insured (Arson Fraud)

2)—Conviction of a fire setter (Insurance fraud is not involved)

3)—Successful denial/reduction of the insurance claim following civil court proceedings.

N.B. In each of the three cases an insurance claim must be involved and the property must be insured by a participant in the scheme.

Payment of the reward will be from ICA funds in the first instance. In cases 1 and 3 the ICA member who insured the property will reimburse ICA. In case 2 the reward will be paid from ICA funds and therefore it is in effect a levy on all the property insurers.

Less than 10 payments have been made under the scheme. One was to a person who at the request of the police infiltrated a group of young men carrying out serial arson; and another led to a conviction and subsequent avoidance of a claim of A$85,000 (approx £35,400).

The Australian police have confirmed to ICA that the scheme is worth continuing with as it allows them the opportunity to offer an inducement to an informer. To date all convictions achieved as a result of this scheme have been of people other than the owners of the property concerned. The existence of a market scheme shows a spirit of mutual co-operation and indicates a willingness to share the cost of apprehending persons involved in arson and possibly deterring others.

Traditionally in the UK rewards have been restricted to individual losses usually arising from theft, where the offer appears to have produced some success. The ICA Arson Reward Scheme represents a market initiative rather than an individual insurer approach. In view of the 2:1 support for the use of a reward in certain circumstances the insurance industry should perhaps consider developing guidelines on reward in arson cases either by individual insurers or through a centrally controlled and funded agency. (Rec. IV.10)

Fraud-related crimes

There is no crime known in English law by the name of fraud. There are, however, several offences, which can be committed during what may be described as a fraud.

Fraud essentially is a concept relating to the character of the act. The question of normality of the transaction should not be taken as a test for dishonesty as held by Widgery, LJ, in *Sinclair* (1968)[35] where he stated:

> The normality of the transaction is not the test and was never intended so to be. The distinction is between honesty and dishonesty…

Dishonesty is a central feature measured by the standards of ordinary people. The word 'fraudulently' appeared in the Larceny Act 1916 but given the changes that have since occurred in the law of theft insurers could now consider changing the fraud policy condition to reflect the requirement of dishonesty. (Rec. IV.4) What matters is whether most people would think that the act was dishonest.

DEFINITIONS

The classic definition of fraud is:

> I shall not attempt to construct a definition which will meet every case which might be suggested, but there is little danger in saying that whenever the words 'fraud' or 'intent to defraud' or 'fraudulently' occur in the definition of a crime two elements at least are essential to the commission of the crime: namely, first, deceit or an intention to deceive or in some cases mere secrecy; and, secondly, either actual injury or possible injury or an intent to expose some person either to actual injury or to a risk of possible injury by means of that deceit or secrecy[36].

Fraud is defined in the *Shorter Oxford English Dictionary* as:

> Criminal deception; the using of false representations to obtain an unjust advantage or to injure the rights or interests of another.

To constitute fraud, a deception should lead to a loss being suffered by the victim. An insured who has deliberately set fire to his property to obtain insurance monies is intending to deceive the insurance company (victim) that the fire was fortuitous.

PECUNIARY ADVANTAGE

Section 16 of the Theft Act 1968, as amended by the 1978 Act, allows for the crime of obtaining a pecuniary advantage by deception. The section states:

> (1) A person who by any deception dishonestly obtains for himself or another any pecuniary advantage shall on conviction on indictment be liable to imprisonment for a term not exceeding five years.
>
> (2) The cases in which a pecuniary advantage within the meaning of this section is to be regarded as obtained for a person or cases where -
>
> (b) He is allowed … to take out any policy of insurance or obtains an improvement of the terms on which he is allowed to do so…

The inclusion of 'or another' might possibly be construed as providing an opportunity to charge any intermediary in the insurance transaction who may have dishonestly deceived the insurance company.

The most common fraudulent devices encountered in claims handling are the falsification of documents, records and accounts.

In pursuing enquiries the adjuster may be presented with a document to support an aspect of the claim or circumstances surrounding the loss. If this document is produced by a third party especially, then the adjuster should be aware of the potential that exists to involve the criminal process.

FORGERY

The Forgery and Counterfeiting Act 1981 creates in s. 1 the offence of forgery:

> A person is guilty of forgery if he makes a false instrument, with the intention that he or another shall use it to induce somebody to accept it as genuine, and by reason of so accepting it to do or not to do some act to his own or any other person's prejudice.

Section 9.(1)(g) states that:

> An Instrument is false for the purposes of this Part of this Act — (g) if it purports to have been made or altered on a date on which, or at a place at which, or otherwise in circumstances in which, it was not in fact made or altered:

The case of *Donnally (Ian)* 1984[37] for example relates to a valuation certificate describing six items of jewellery, which did not in fact exist. Asset valuations in particular require close scrutiny to assess whether the valuation is a fair one. If not then the valuation could be regarded as deceptive. Expert evidence may be required to support such allegations.

ACCOUNTS AND RECORDS

Accounts and business records should be checked. Falsification and suppression of accounts and other records are offences under the Theft Act 1968 where s.17 (1) provides:

> Where a person dishonestly, with a view to gain for himself or another or with intent to cause loss to another —
>
> (a) destroys, defaces, conceals or falsifies any account or any record or document made or required for any accounting purpose; or
>
> (b) in furnishing information for any purpose produces or makes use of any account, or any such record or document as aforesaid, which to his knowledge is or maybe misleading, false or deceptive in a material particular;
>
> he shall, on conviction on indictment, be liable to imprisonment for a term not exceeding seven years.

LIMITED COMPANIES

With regard to other aspects of company records and

accounts, it should be borne in mind that under s.221 of the Companies Act 1985 every company must keep accounting records sufficient to show and explain the company's transactions and disclose the company's financial position. If they fail to comply with the requirements, all officers of the company in default are guilty of an offence carrying two years' imprisonment unless they can show that they acted honestly and that in the circumstances the default was excusable.

Adjusters are often told that documentation is unavailable. Section 222 (4) of the Companies Act 1985 requires a private company to preserve its accounting records for three years. Failing to take reasonable steps to secure the company's compliance with this requirement renders any officer of the company guilty of an offence subject to two years' imprisonment. Mention of this may well help improve the memory of an officer of a corporate policyholder.

A further provision of the Companies Act which adjusters should bear in mind and be able to consider relates to the offence under s.450 (1) of the Companies Act 1985 relating to falsifying or suppressing company records.

Seven years' imprisonment is the sentence for an officer of the company if he:

a) destroys, mutilates or falsifies a document affecting or relating to the company's property or affairs,

b) makes a false entry in such a document, or

c) is privy to one of the acts in (a) or (b),b)

unless he proves that he had no intention to conceal the state of the company's affairs or to defeat the law.

There is some uncertainty as to whether the provisions of s.450 are of general application as they appear in part XIV of the Act which is primarily concerned with the inspection of company's books by the DTI. However, it may still be worth raising this in appropriate circumstances.

SOLE TRADER

The insured may not be a limited company but a sole trader. Unlike a company, an individual trader does not commit an offence by failing to keep proper accounts. However, if he subsequently becomes insolvent the failure to keep proper books becomes an offence under s. 158(1) of the Bankruptcy Act 1914, as amended.

This point is of interest as the policy often requires the policyholder to maintain proper books of accounts. In *Re Willis Ace exp Cambell* (1885)[38] it was said:

In my opinion, the not keeping of books is one of the greatest offences which can be committed by a trader… You may be almost certain that a trader who does not keep books will sooner or later become a bankrupt.

BOOKS OF ACCOUNT

In deciding the extent to which books of account should be maintained, the dictum of Lord Eshere in Re *Reed & Bowen* (1886)[39] is instructive:

> It is not enough that there should be books with entries in them which would require a prolonged examination by a skilled accountant in order to ascertain the result of them. That is not keeping proper books. The books should be properly kept and balanced from time to time, so that at any moment the real state of the trader's affairs may at once appear.

AWARENESS

The selection of criminal charges is a matter for the police and Crown Prosecution Service. However, an awareness of the possibility of informing the police of potential criminal charges adds strength to the factors to support an insurer's decision on how to process a claim. If irregularities with documentation or company management are discovered then the adjuster should seek specialist advice from a solicitor or accountant experienced in company law. The insurer's instructions should be obtained on the way in which any breaches of criminal law should be treated.

Indications received during this research suggest that while the police would appreciate the opportunity of acting on breaches of the criminal law discovered by adjusters, insurers are reluctant to act as the complainant. This is surprising considering the expressions of intent to assist the police encountered in the questionnaire responses discussed earlier.

Adjusters—crime detection

DUTY TO REPORT CRIME?

What is the position of the adjuster who discovers potential criminal offences or irregularities?

During the course of a claim an adjuster may become aware of information relating to the insured which involves an act which could possibly be regarded as criminal. The question then arises as to whether the loss adjuster has a duty to report that information to the police. CILA's honorary solicitor has considered the question and advised members as follows[40]:

> There is no legal obligation, at least in the circumstances of fraud, evasion and irregularities (Social Security fraud, Income Tax evasion, VAT irregularities, Customs Duty evasion or other and more serious criminal activities) upon the adjuster or his principals to report such facts to the relevant authority. *There is a legal obligation upon the adjuster to report such facts to his principals.*
>
> It is appropriate for the adjuster, having reported the facts to his principals, to leave it to them to consider whether they have a moral obligation to report the facts to the relevant authority. In judging that, insurers will no doubt have regard to the context in which they receive the information, the particular information and their commercial interests.

The effect of this advice is that while adjusters may seek to co-operate and assist the police and other authorities they do not regard themselves as having a

4

legal duty to do so or indeed as incurring a legal liability for failing to do so.

DISCLOSURE OF INFORMATION

The institute's honorary solicitor states that where an adjuster receives an approach from a competent authority requesting information the adjuster should:

> Report the fact of that approach to his Principals. Seek their confirmation that they agree to him disclosing information to the authority and, I would not expect that there would normally be any difficulty in obtaining this. However, if difficulty arises the position is that it is an offence under Section 4(i) of the Criminal Law Act 1967 where a person has committed an arrestable offence for any other person, knowing or believing him to be guilty of the offence or of some other arrestable offence, without lawful authority or reasonable excuse to do any act with intent to impede his apprehension or prosecution. It follows that *an adjuster must, if asked by a competent authority about a specific matter and informed that the information is sought for the purpose of consideration of criminal proceedings, supply relevant information in his possession.* That does not include privileged documents. I should add that up to the point when he makes a witness statement *there is some risk that the adjuster could render himself vulnerable to defamation proceedings by the Insured;* care is therefore necessary.[41]

Loss adjusters have been advised to inform their principals of any information suggesting that the policyholder may have committed a criminal offence. Considering that CILA suggests that the adjuster is paid from the fund of all policyholders' premiums then it is perhaps the policyholders (or indeed shareholders) who should be regarded as the eventual principal.

Insurers' reluctance to prosecute

How should the discovery of a crime be dealt with by the insurer?

MORAL DUTY?

Pro bono publico – For the public good.

Having been advised by the adjuster, the question then arises as to whether or not the insurer has a duty to report the alleged criminal acts or offences. This is a question that requires further consideration and research. (Rec. IV.11)

If a particular insurer is seen as taking a strong position by pressing the police to prosecute fraudulent claimants it may be that potential fraudulent claimants will select softer targets to insure with or control their desire to exaggerate grossly the claim following a genuine loss.

Comparison with the deterrence effects produced in the retail sales sector by prosecuting shoplifters may identify whether a beneficial result would be achieved. Insurers should perhaps research whether an increased demand for the prosecution of fraudulent claimants would produce a quantifiable deterrent effect against fraud. (Rec. IV. 12)

The enactment of immunity laws in America has helped to avoid legal complications arising from insurers and adjusters working with the police and other authorities. (Rec. IV.8)

Michael Clarke[42] and T.E. Heward[43] have both noted insurers' reluctance to pursue a criminal charge once the claim has been successfully repudiated and no payment has to be made. The opportunity of producing a deterrent effect by pursuing selected cases of fraud through the criminal courts appears to have been outweighed by the concerns relating to cost, adverse publicity, and public opinion. It is worth considering whether the insurance company's shareholders might express concern over the insurers' apparent reluctance to seek to deter fraudsters from pursuing such claims again at a future stage.

PUBLICITY CAMPAIGN

It is suggested that individual insurers or the ABI should consider organising a publicity campaign to increase public awareness of:

— the personal and financial suffering brought about as a result of arson;
— the potential life imprisonment sentence for the crime of arson;
— the other potential sentences for criminal offences arising from fraud in general;
— details of successful prosecutions. (Rec. IV. 13)

8. CONCLUSIONS

This paper contains constructive criticisms, questions, suggestions and recommendations, which could lead to a more integrated approach to arson investigation, and a reduction in the cost of fraudulent claims especially those arising from arson.

It is of considerable concern that the insurance industry and the government have not achieved more success in addressing the immensely expensive and socially unacceptable problem of arson.

The approaches to fraud detection and arson investigation are fragmented and could be significantly improved. Increased co-operation between the insurance industry and public services would benefit both. Insurers, however, seem to regard this cooperation as a panacea, which it is not. It is within the resources of the insurance industry alone to increase the success rate of identifying fraudulent arson claims, and decrease the cost of such claims.

9. RECOMMENDATIONS

It should be recognised that the space constraints of this work prevent a full and detailed rehearsal of arguments for and against each individual recommendation. The aim is to promote, and provoke discussion about the subject.

There are almost 60 recommendations contained in this work grouped into the broad categories of:

I Underwriting

II Detection

III Statistics

IV Resolution

The six key recommendations from the author's point of view are:

- Establishment of a central 'anti-fraud' register (1.2)
- Training and examination for loss adjusters in fraud and fire investigation (11.2)
- Production of a statement of practice for commercial underwriting and claims investigation (11.5)
- Creation of an active investigation department within the Arson Prevention Bureau (11.19) to:
- Analysis of all losses over £50,000 during past two years (111.2)
- Rewording of the fraud condition to avoid claims exaggerated beyond reasonable negotiating level (IV.3)

I. Underwriting

I.1 Research to be conducted to assess the extent to which, if at all, direct insurers are influenced in their decision-making processes (underwriting and claims) by the presence and extent of reinsurance.

I.2 Access to information relating to past claimants and suspected or proven fraudsters would assist insurers at the underwriting and claims stages. It is suggested that a central anti-fraud register be established by insurers, not just restricted to fire claims, containing details of:

a) policyholders and shareholders, directors, and managers of policyholders who have been involved with an insurance claim of a significant size arising under a commercial insurance policy;

b) the amounts claimed and paid;

c) if the claim was repudiated then the amount of claim and reasons for the repudiation;

d) the insurer and adjuster concerned. (Rec. 11.1)

1.3 ABI and BIIBA to agree procedure where no proposal form available. One possibility could be that the broker must record information on a standard internal fact find form which should be sent to the insurer possibly even signed by the proposer.

1.4 The continuing development of placing of business by means of an electronic slip demands an early reappraisal of the traditional proposal procedure. This will increase the responsibility of the broker for accuracy and comprehensive transmission of all material facts. Policyholders should be clearly advised that a broker is a policyholder's agent and that all information provided to insurers should be seen and verified and approved by the policyholder.

1.5 In view of the decreasing use of a proposal form it is recommended that early consideration be given to amending the way in which an underwriter obtains material facts from the proposer. Increased openness in terms of defining the information required as material would give more certainty to both parties. Insurers may possibly have to accept the burden of confirming to the insured in writing the information which has been provided as part of the proposal and the extent to which it is regarded as material by the underwriter.

1.6 Greater emphasis, involvement and publicity to be given to the Loss Prevention Council with regard

a) post-loss investigations to produce anti-arson risk-hardening guidelines;

b) development of ways to minimise damage from a fire caused by arson;

1.7 A minimum level of appropriate fire extinguishing appliances should be compulsory.

1.8 Certain categories of policyholder in particular classes of business and located in specified geographical locations should be required to produce quarterly reports detailing key factors relating to the performance of the business.

1.9 In view of the high proportion of fire losses that occur overnight, consideration should be given to increasing the level, extent and effectiveness of overnight protection of property by security guards and videotaped CCTV.

I.10 Reinsurers should conduct underwriting and claims audits on a more frequent basis than seems to exist at present.

I.11 Insurers should consider the extent to which their shareholders, policyholders and reinsurers should be provided with information on how each company deals with the risk of fraudulent claims in general, and fraudulent arson in particular.

I.12 Insurers should consider providing risk management advice to policyholders in areas such as contingency planning, physical protections, personnel procedures.

I.13 It is recommended that insurers should research and form an opinion on the disclosure responsibility of

a bank in terms of utmost good faith.

I.14 Insurers should assess the status of a bank in terms of whether co-insured or interest noted only. Which would they prefer? Should additional premium be charged?

I.15 A capability rating to be assessed on a continuous basis for insurance companies, Lloyd's underwriters and reinsurance companies for:

a) claims management;

b) underwriting.

I.16 Questions on a proposal form should seek information relating to all individuals not just directors who could be regarded as *alter* egos of the proposer.

II. Detection

II.1 A central anti-fraud register of suspect claimants to be developed on computer subject to strict controls and immunity from Data Protection considerations. (Rec. 1.2)

II.2 A training programme should be developed for loss adjusters to provide comprehensive training and preparation for new examinations in the areas of:

a) fraud investigation;

b) fire investigation.

II.3 Every qualified member of CILA should be issued with a photograph identity card.

II.4 It is suggested that the UK network of fire liaison panels represents an ideal forum for the various agencies to:
— encourage involvement of loss adjusters;
— focus on arson prevention and detection;
— review and consider proposals to improve interagency relationships.

It is recommended that:

a) a CILA fire liaison committee to be established;

b) CILA to lobby for at least one qualified CILA representative to be a member of each and every fire liaison panel in the UK.

II.5 A statement of practice to be prepared summarising the usual steps involved in commercial underwriting and claim investigation. This statement to be submitted to, approved and adopted by ABI and Lloyd's.

II.6 In appropriate underwriting and claim situations, individuals of the insured company should be asked to produce a current police print-out showing the information held in the police computer regarding criminal record.

II.7 CILA to establish or sponsor a study to produce software to support recording and analysis of information gained during investigation process.

II.8 There has been little research into the extent of fraud in general and fraudulent arson in particular. A research study at industry level would enable insurers to assess the true extent of what is in effect theft.

II.9 Insurers, should consider the extent to which their shareholders, policyholders and reinsurers, should be provided with information on how each company deals with the risk of fraudulent claims in general, and fraudulent arson in particular.

II.10 Members of CILA and other interested parties, e.g., ABI and Lloyd's, to be consulted on whether the loss adjuster should be a watchdog or a bloodhound,

II.11 Consultation with forensic science profession to define more clearly the roles and responsibilities of the adjuster and forensic scientist.

II.12 Research to be conducted to assess the priority and resources allocated by the Crown Prosecution Service to the prosecution of arson.

II.13 Research to establish the viability of a centrally operated (regional or national) Fire Mark rapid notification system.

II.14 The existing fire investigation teams and units that operate independently throughout the UK should be encouraged to co-operate with loss adjusters and private forensic scientists.

II.15 A procedure should be established enabling cooperation between loss adjusters, police and fire brigade.
I.16 A feasibility study should be conducted to ascertain whether financial assistance from insurers to the fire brigade and police would produce cost- effective benefits to insurers, closer co-operation, and advantages to the brigade and police.

II.17 CILA to explore opening a dialogue with the Association of Chief Police Officers to assess whether a procedure can be agreed to achieve closer co-operation between the police and loss adjusters.

II.18 Further research into:

a) reasons for unsuccessful criminal prosecutions, including those where CPS declined to proceed to prosecution;

b) successful prosecutions to assess key pointers to future success and assess whether the insurance industry had been of any assistance to the police.

II.19 Consideration should be given to expand the present role of the Arson Prevention Bureau. A proactive role is recommended with the Bureau operating an Active

Investigation Department. The Bureau should be provided with authority to involve and coordinate the activities of the fire brigade, police, loss adjusters and forensic scientists involved on any particular fire.

II.20 It is recommended that urgent consideration be given to a period of experimental co-operation in connection with losses that exceed £50,000. This cooperation to involve not only future losses but also research into such losses that have occurred during the past 24 months. (Rec. 111.2)

II.21 Insurers to consider the suggestion for a two- tier forensic science reporting procedure.

III. Statistics

III.1 Consideration should be given to integrating the relevant statistical information currently maintained separately by agencies such as Home Office, police, Association of British Insurers and Fire Protection Association as well as individual insurers and reinsurers.

III.2 It is suggested that an analysis of fire losses especially those over £50,000 that have occurred during the past two years should enable:

a) the extent of arson and fraudulent arson to be identified;

b) the accuracy of cause identification by fire brigade and loss adjusters to be verified. (Rec. 11.20)

III.3 Early consideration should be given to disclosing the cost of fire claims by consequential loss insurers. The true total cost to insurers of fire claims could then be identified, as could the amounts attributable to arson and possibly fraudulent arson.

III.4 Further investigation to establish the extent of consequential losses to the economy by fire, arson especially.
III.5 Policy condition that at insurer's request the police should be notified in event of deliberate fire. This should:

a) improve arson statistics;

b) oblige police involvement, to a fraudulent insured's disadvantage.

III.6 A significant responsibility for compiling fire statistics rests with loss adjusters and insurance companies. The present system of collecting information should be reviewed and improved to ensure accurate capture of information. In particular it is suggested that random analysis should be undertaken of cases that are:

a) malicious;

b) deliberate or doubtful;

c) attributed to other causes (e.g., smoking materials) which could in fact be deliberate but have not been so identified.

III.7 Early research required to:

i) determine the real extent of the crime of arson;

ii) study fraudulent arson within a general study of commercial crime.

IV Resolution

IV.1 Further research is required to assess the effectiveness of organisations operating overseas and the extent to which the UK could follow and benefit from their experience.

IV.2 For certain insureds in specific classes of business and certain geographical locations it should be compulsory for a complete set of duplicate business records to be stored safely at an alternative premises.

IV.3 The fraud condition within the policy to be expanded to make it clear that grossly exaggerated claims will be regarded by the insurer as a fraud, which will deprive the claimant of cover. 'Grossly exaggerated' will need to be defined by insurers.

JV.4 The fraud condition to be amended to reflect the trend to interpret theft as 'dishonest' rather than 'fraudulent'.

IV.5 Reverse burden of proof when loss found to be caused by arson. In appropriate cases it is suggested that a reverse burden clause be inserted in the policy to the effect that fires caused by arson would not be covered unless the insured can prove that the fire was not caused by the insured.

IV.6 Amend arbitration clause to require arbitration on policy liability as well as quantum.

IV.7 Insurers, possibly through the ABI, to seek a dialogue and support from the consumer lobby on ways to protect the funds of genuine policyholders from fraud.

IV.8 A study should be undertaken to establish the extent to which insurers require legal protection— immunity—as a result of:

—information exchanged during an investigation;
—possible defamation arising from repudiation.

IV.9 Additional General Condition to be added to policy providing for a contractual limitation of one year from the date of loss unless the claim is subject to litigation or arbitration.

IV. 10 Insurers to consider developing guidelines for the use of a reward in arson cases either by individual insurers or through a centrally controlled and funded agency.

IV. 11 Insurers to research whether they have a duty to report to the police any alleged criminal acts by the insured.

IV.12 Insurers to research whether an increased demand for the prosecution of fraudulent claimants would produce a quantifiable deterrent effect against fraud.

IV. 13 Consideration should be given to the organisation of a publicity campaign to increase public awareness of:

a) the personal and financial suffering brought about as a result of arson;

b) the potential life imprisonment sentence for the crime of arson;

c) the other potential sentences for criminal offences arising from fraud in general;

d) details of successful prosecutions.

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20. Munich Re (1988), p21
21. *S & M Carpets (London) Ltd* v. *Cornhill Insurance Co. Ltd* (1982) 1 Lloyd's Rep 423 (CA)
22. Supra, 15
23. *Exchange Theatre Ltd* v. *Iron Trades Mutual Insurance Co. Ltd & others* (1983) 1 Lloyd's Rep 674
24. Sherlock Holmes, *The Reigate squires,* Strand June 1893
25. *Carter* v. *Boehm* (1766) 3 Burr 1905; 97 ER 1162
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27. *Woolcott* v. *Sun Alliance & London Insurance Co. Ltd* [1978] 1 Lloyd's Rep 629
28. Duiwich, R.H. (1984)
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APPENDIX A

Specimen questionnaire to UK insurers

Reference No.

QUESTIONNAIRE FOR COMPLETION BY GENERAL MANAGERS/MANAGING DIRECTORS IN INSURANCE/REINSURANCE COMPANIES IN UK

1. To what extent should policyholders, and shareholders expect their insurance company to investigate and defend claims arising from fire damage where the fire is thought to have been started by the insured?

2. At what level in the management of your company is a decision made to fully commit your company to securing experts and information to defend such a potential fraudulent claim?

3. At what stage would you instruct:

   (i) Independent Loss Adjuster

   (ii) Forensic Investigator to establish cause and origin

   (iii) Legal Adviser, Solicitor/Attorney

   (iv) Forensic Accountant

4. Should the insurance company be prepared to fund and conduct all the enquiries necessary to defend successfully a claim arising from fraudulent arson?

   If yes, why?

   If no, why?

5. Would you be willing to support the police force in their efforts to obtain a criminal prosecution of the insured?

   If no, why?

   If yes, how?

6. Are you able to categorise your fire claims statistic into:

   (a) Fire caused deliberately—persons unknown?

   (b) A sub-group of (a) where fraud is suspected by the Insured?

   Could you please set out the categories which you currently use for describing the suspected cause of fire claims.

7. Are you able to advise accurately or approximately the amount and percentage of fire claims under:

   (a) Fire caused deliberately - persons unknown?

   (b) A sub-group of (a) where fraud is suspected by the Insured?

8. During the investigation of a substantial claim thought to result fire set by the Insured do you:

   (a) co-ordinate all enquiries through a member of the claims department acting as co-ordinator?

   (b) expect the appointed Loss Adjuster to co-ordinate all enquiries?

   (c) instruct a solicitor to act as co-ordinator?

9. Would you consider offering a reward for ‘information leading to conviction of person(s) responsible for setting the fire’?

10. Have you during the past three years successfully defended a fire claim thought to result from a fire set by the Insured? If yes:

    (a) are you able to confirm the number of such claims and the total payments thereby avoided?

    (b) would you be willing to share tactical legal information (on a strictly private and confidential basis) with:

    (i) other insurers

    (ii) the arson bureau

    (iii) this researcher?

APPENDIX B

Specimen questionnaire to reinsurers

QUESTIONNAIRE TO REINSURANCE COMPANIES

1. To what extent should each of the following groups expect you to satisfy yourselves that direct clients are dealing with claims correctly?

   a) our shareholders

   b) your direct clients

   c) your own reinsurers

2. How do you satisfy yourselves that claims for payment from direct clients are in respect of valid claims rather than, for example, claims paid:

   a) *ex gratia*

   b) without prejudice

   c) paid with no regard to policy terms

   d) where suspicion of fraud and/or arson by policy holder existed but direct insurer decided not to pursue investigations and settled claim.

   e) on reinstatement values even though the policyholder had not reinstated at time of payment.

3. With regard to arson and fraudulent claims has your company:

	Please circle answer
a) conducted research	Y/N
b) run or participated in training course	Y/N
c) prepared external seminars (e.g., for direct clients)	Y/N
d) presented guidelines/contractual instructions to direct clients	Y/N

   If Yes please provide brief details.

   (It would be greatly appreciated if copies of any materials, agreement wordings etc. could be provided, all of which will be treated in strict confidence.)

4. Would you expect to be notified by a direct client of its intention to contest a claim through the courts?

   If yes, for what reason: Please tick

   a) term of reinsurance agreement ☐

   (please provide if possible a copy of wording)

   b) general courtesy ☐

   c) because claim exceeded a certain value ☐

   Please indicate value

   d) other, please specify ☐

5. Please provide the following information relating to commercial fire claims:

INFORMATION	1989 (£)	1990 (£)
a) total nett claims paid		
b) where fire caused by deliberate means		
c) where fire thought to have been started/arranged by direct policy holder		
d) where claim settled by direct insurer on without prejudice or ex gratia basis.		

6. Would you be willing to contribute to costs incurred by direct client in investigating and legally defending a fire claim thought to arise from arson by the policy holder when the actual cost of that claim in total would impact your reinsurance account?

7a) In your opinion is there a tendency for a direct insurer to pay a suspect fire claim (because the reinsurer will then pickup a percentage of the payment) rather than conduct a detailed investigation (the cost of which might not exceed the direct insurers nett retention if successful)?

7.b) Do you have any method of identifying whether a direct insurer has paid rather than investigated?

If yes, please explain.

8. Do you maintain records separating fire damage into categories of cause?

If yes please list the cause categories

If no please explain why you do not maintain such an analysis.

9. When entering a reinsurance agreement do you assess the capability of a direct insurer's claims department?

If yes, please briefly explain criteria for assessment.

If no please explain why you do not maintain such an analysis.

10. Do you provide direct clients with training and guidelines on the approach to claim investigation?

11. Do you reserve the right to review/audit claims dealt with by direct clients?

	Please circle answer
a) in total	Y/N
b) in particular classes of business, e.g., fire	Y/N
c) in respect of individual losses	Y/N

(Copies of any applicable wordings would be appreciated)

12. .Do you request statistics from direct clients in order to assess their effectiveness in a) identifying or b) defending/reducing claims arising through fraud?

If yes, please advise basis upon which information requested.

13. Do you require direct insurers to:

a) obtain detailed placing information

b) use proposal forms

c) survey risks

If yes please provide as much information as possible including the sanctions adopted if requirements not complied with.

APPENDIX C

Specimen questionnaire to banks

QUESTIONNAIRE TO UK BANKS AND FINANCIAL INSTITUTIONS RELATING TO INSURANCE OF COMMERCIAL ORGANISATIONS

1. Do you require your customers to insure their property if such property is the subject of security in respect of overdraft?
   If yes, could you please supply a copy of the wording, condition or agreement setting out your requirement to the customer.
   If no, on what basis are you able to protect your interest as a named party?

2. Do you require sight of a policy showing your interest as a named party?
   a) At inception of the loan/overdraft Y/N
   b) At renewal of loan/overdraft Y/N

3. Do you have a specific wording relating to your interest in the insurance policy?
   If yes, could you please supply a copy of the wording.

4. Do you have an approved list of insurance companies?
   If yes, please advise basis upon which list is compiled.

5. If a fire occurs at your customer's business involving damage to property over which you have a charge do you:
   a) send a bank official Y/N
   b) instruct a specialist to represent you? Y/N
   If yes, please advise whether specialist would be:
   i) forensic scientist
   ii) public loss assessor
   iii) accountant
   iv) solicitor

6. To what extent would you become involved in the actual calculation of the loss payment under the policy?

7. Would you expect the insurance monies to be paid direct to you if the amount payable was equal to or less than the amount of your charge over the insured property?

Thank you for completing this questionnaire. The information will be treated in strict confidence.

APPENDIX D

ABI Statement of Practice – private insurance

ASSOCIATION OF BRITISH INSURERS
STATEMENT OF GENERAL INSURANCE PRACTICE

The following Statement of normal insurance practice applies to general insurances of policyholders resident in the UK and insured in their private capacity only.

1. PROPOSAL FORMS

(a) The declaration at the foot of the proposal form should be restricted to completion according to the proposer's knowledge and belief.

(b) Neither the proposal form nor the policy shall contain any provision converting the statements as to past or present fact in the proposal form into warranties. But insurers may require specific warranties about matters which are material to the risk.

(c) If not included in the declaration, prominently displayed on the proposal form should be a statement:

(i) drawing the attention of the proposer to the consequences of the failure to disclose all material facts, explained as those facts an insurer would regard as likely to influence the acceptance and assessment of the proposer

(ii) warning that if the proposer is in any doubt about facts considered material, he should disclose them

(d) Those matters which insurers have found generally to be material will be the subject of clear questions in proposal forms.

(e) So far as is practicable, insurers will avoid asking questions which would require expert knowledge beyond that which the proposer could reasonably be expected to possess or obtain of which would require a value judgement on the part of the proposer.

(f) Unless the prospectus or the proposal form contains full details of the standard cover offered, and whether or not it contains an outline of that cover, the proposal form shall include a prominent statement that a specimen copy of the policy form is available on request.

(g) Proposal forms shall contain a prominent warning that the proposer should keep a record (including copies of letters) of all information supplied to the insurer for the purpose of entering into the contract.

(h) The proposal form shall contain a prominent statement that a copy of the completed form:-

(i) is automatically provided for retention at the time of completion: or

(ii) will be supplied as part of the insurer's normal practice: or

(iii) will be supplied on request within a period of three months after its completion.

(iv) An insurer shall not raise an issue under the proposal form, unless the policyholder is provided with a copy of the completed form.

2. CLAIMS

(a) Under the conditions regarding notification of a claim, the policyholder shall not be asked to do more than report a claim and subsequent developments as soon as reasonably possible except in the case of legal processes and claims which a third party requires the policyholder to notify within a fixed time where immediate advice may be required.

(b) An insurer will not repudiate liability to indemnify a policyholder:

(i) on grounds of non-disclosure of a material fact which a policyholder could not reasonably be expected to have disclosed;

(ii) on grounds of misrepresentation unless it is a deliberate or negligent misrepresentation of a material fact;

(iii) on grounds of a breach of warranty or condition where the circumstances of the loss are unconnected with the breach unless fraud is involved.

c) Liability under the policy having been established and the amount payable by the insurer agreed, payment will be made without avoidable delay.

3. RENEWALS

(a) Renewal notices shall contain a warning about the duty of disclosure including the necessity to advise changes affecting the policy which have occurred since the policy inception or last renewal date, whichever was the later.

(b) Renewal notices shall contain a warning that the proposer should keep a record (including copies of letters) of all information supplied to the insurer for the purposes of renewal of the contract.

4. COMMENCEMENT

Any changes to insurance documents will be made as and when they need to be reprinted, but he Statement will apply in the meantime.

5. POLICY DOCUMENTS

Insurers will continue to develop clearer and more explicit proposal forms and policy documents whilst bearing in mind the legal nature of insurance contracts.

6. DISPUTES

The provisions of the Statement shall be taken into account in arbitration and any other referral procedures which may apply I the event of disputes between policyholders and insurers relating to matters dealt with in the Statement.

7. EEC

This Statement will need reconsideration when the Draft EEC Directive on Insurance Contract Law is adopted and implemented in the United Kingdom.

January 1986

APPENDIX E

ABI and banks agreement regarding notification of interest on mortgaged properties

Association of British Insurers /banks agreement regarding notification of interest on mortgaged properties (or properties in Scotland over which a heritable security has been granted)

1. THE 'UNDERTAKING'

The insurance companies listed in appendix A, undertake in respect of any policy in which any of the banks/organisations listed in appendix B has notified an interest, using the prescribed in appendix C, that they will instead of endorsing the policy with the bank's/organisation's interest

(a) advise the bank/organisation if the policy is not renewed as soon as practicable after such non-renewal has come to their knowledge;

(b) advise the bank/organisation if the cover in which the bank/organisation is interested is reduced or if any risk previously covered is restricted or cancelled;

(c) pending the receipt of prompt instructions from the bank/organisation keep its interest in the policy in force up to the full sum insured and for the same risks as were covered when the bank's/organisation's interest was notified (subject to the insurance not having been replaced elsewhere with the consent of the bank/organisation).

In the event that the bank/organisation instructions under paragraph (c) are to continue the insurance, or part of it, the bank/organisation undertakes to pay the premium upon demand.

2. LIMITATIONS

(a) This Agreement is restricted to insurances on the structure/fabric of:

(i) mortgaged properties in England, Wales, Northern Ireland, the Isle of Man, the Channel Islands, and

(ii) properties in Scotland over which a Heritable Security has been granted.

(b) The Agreement des not apply to:

(i) policies of marine, aviation, motor vehicle or life insurance

(ii) insurances of privately occupied properties including houses, flats and maisonettes where the sum insured is £200,000 or less.

Explanatory notes to limitation (b) (ii)

The threshold figure is taken from the policy not the bank/organisation advance. Where a doubt arises as to whether the property is a private dwelling house, enquiries should be made and relevant information passed to the insurers when notification is being given. For example, where a residential property has been purchased for investment purposes the bank/organisation may wish to notify its interest to the insurer.

Where a farmhouse or other building is regarded as being a private dwelling house a bank/organisation will only be required to notify its interest to an insurer where the sum insured exceeds the threshold. In the case of such a property not being regarded as a private dwelling house, a bank/organisation should notify its interest to an insurer irrespective of the sum insured.

3. OPERATING PROCEDURES

(a) Banks/organisations should notify their interest and interest on the advice form shown in Appendix C.

(b) Appendices A and B will be kept up-to-date regularly by an exchange of letters between the secretariat of ABI with various other parties to the agreement.

(c) In the event of an insurance company which is a party to the agreement withdrawing there from

or ceasing to transact business, it will under the terms of the Agreement, notify individual bank branches/organisations branches from whom they hold notices of interest where that insurance cover has been terminated.

4. 'BLOCK' POLICIES – BUILDING SOCIETY ARRANGEMENTS

Full protection within the terms of the Agreement is enjoyed by a bank/organisation which has notified an interest in a property to a building society operating a block policy with insurers listed in Appendix A. Thus, an insurer has no reason to expect to have such enquiries addressed to him regardless of the sum insured.

5. 'PRIVATE DWELLING HOUSES' OUTSIDE THE AGREEMENT

Under the contingency insurance arrangements available in the market, but which do not form an integral part of the Agreement, insurance protection can be made available where the sum insured on private dwelling houses does not exceed the threshold. In such cases the bank/organisation has to be satisfied that a policy or insurance on the private dwelling, adequate to cater for the bank/organisation's interest has been effected by the mortgagor on the buildings on the security of which the mortgage is granted. In the event of the insured (the bank/organisation under the contingency cover) learning that a mortgagor's original policy is cancelled, reduced, or not renewed, the insured shall arrange insurance separately:

It follows, therefore, that this contingency insurance will, subject to its terms and conditions, indemnify the bank/organisation in the event of a claim arising from an insured peril in respect of such properties where the original policy is found for some reason not to be sufficient to protect the bank's/organisation's interest and so long as the bank/organisation took the initial step, inter alia, reasonably to satisfy itself that adequate insurance arrangements had been made by the mortgagor.

Thus, the most a house insurer can be expected to provide in respect of an insurance below the Agreement threshold is confirmation that insurance arrangements were extant when the security was taken.

Reference: G/227/500

September, 1991

APPENDIX F

Arson-for-profit indicators

Insurance Crime Prevention Institute, USA

Fire Scene Indicators of Arson-for-Profit

FRAUD INDICATORS ASSOCIATED WITH THE FIRE SCENE

❑ Building is in deteriorating condition and/or located in a deteriorating neighbourhood.

❑ Fire scene investigation suggests that property/contents were heavily over-insured.

❑ Fire scene investigation reveals absence of remains non-combustible items of scheduled property covered by floaters, e.g. coin or gun collections, special jewellery, etc. (While in some fire losses, stamp collections, furs and other combustible items may be totally consumed, there will often be some identifiable remains to confirm the loss).

❑ Fire scene investigation reveals absence of remains of expensive items used to justify an increase over normal 50% contents coverage, e.g. antiques, piano, expensive stereo/video equipment etc.

❑ Quality of furnishings is incompatible with residence, neighbourhood, occupation and/o income of the insured (insured may have removed expensive items in anticipation of the fire and replaced them with inferior quality goods).

❑ Fire scene investigation reveals absence of items of sentimental value, e.g. family Bible, paintings, family pictures, trophies, awards, degrees, licences etc.

Fire scene investigation reveals absence of remains of items normally found in a home or business. Insureds have been known to remove all sorts of items from homes/businesses prior to planned fires. The following is a sample listing of such items, most of which will be identifiable at fire scenes except in total burns.

Kitchen items

❑ major appliances (washer, dryer, refrigerator, etc.)

❑ minor appliances (coffee maker, blender, etc.)

❑ normal food supply in refrigerator, cabinets, pantry

❑ pots and pans

Living room items

❑ TV and video equipment

❑ stereo equipment

❑ record and tape collections

❑ organ and piano (check with neighbours regarding recent removal)

❑ chairs, sofa, etc. (springs will remain)

Bedroom items

❑ gun(s)

❑ jewellery

❑ clothing

❑ toys

Basement/garage items

❑ Office equipment, e.g. typewriters, adding machines, etc.

❑ Normal inventory (raw materials, finished products)

❑ Display cases

❑ Catalogues

❑ Plumbing and electrical fixture

❑ Office furniture

❑ Business records (which are normally housed in metal filing cabinets and should survive most fires)

❑

Indicators of Arson-for-Profit or Fire Related Fraud

While arson-for-profit is unquestionably the most vicious and costly economic assault on the Property Insurance Industry, claims personnel should also be on the outlook for fraud which occurs when an insured decides to take criminal advantage of an accidental fire or an arson committed without his knowledge or intent. While most of the indicators below suggest arson-for-profit, others relate to fraud alone, regardless or whether an insured started or arranged for the fire.

MANNER OF THE INSURED

- Insured is overtly pushy for a quick settlement.
- Insured is unusually knowledgeable with regard to insurance terminology and the claims settlement process.
- Insured handles all business in-person thus avoiding the use of the mail.
- Insured is willing to accept an inordinately small settlement rather than document all claimed losses.
- Insured contacts agent to verify coverage or extent of coverage just prior to loss date.
- Suspiciously coincidental absence of insured and/or family on overnight or short vacation at the time of the fire.
- Suspiciously coincidental absence of family pet at time of fire.

INDICATORS ASSOCIATED WITH THE LOSS INCIDENT

- Fire occurs at night, especially after 11.00 PM.
- Commercial fire occurs on holiday, weekend, or when business is closed.
- Fire Department reports fire cause is incendiary, suspicious or unknown.
- Fire occurs just after coverage takes effect, just before coverage is about to cease or just after coverage has been increased, e.g. the recent addition of business interruption coverage, floaters, riders, etc.
- Commercial contents losses which primarily involve seasonal inventory or equipment and which occur at the end of the selling season, e.g. ski inventory destroyed in spring, or farm machinery in the fall.
- Losses include a large amount of cash.
- Fire site is unoccupied at the time of the loss.
- Fire alarm and/or sprinkler system failed to work at the time of loss.
- Losses are incompatible with Insured's residence, occupation and/or income.

INDICATORS ASSOCIATED WITH THE CLAIMS PROCESS

- Loss inventory indicates unusually high number of recent purchases, e.g. all major appliances, purchased within the preceding year, etc.
- Insured cannot recall place and/or date of purchase for newer items of significant value.
- Insured indicates distress over prospect of an examination under oath.
- Insured cannot provide bank or credit card records for recent purchases of significant value.

GENERAL INDICATORS OF FIRE FRAUD

- Building and/or contents were up for sale at the time of the loss.
- Insured had a loss at the same site within the preceding year. The initial loss, though small, may have been a failed attempt to liquidate contents.
- Building and/or business is recently purchased.
- Commercial losses include old and unsaleable inventory, fixtures and/or chemicals/materials outlawed by a government agency.
- Insured or insured business is experiencing financial difficulties, e.g. bankruptcy, foreclosures, presence of new competitor etc.
- Fire site is claimed by multiple mortgages or chattel mortgagees.

APPENDIX G

Arson loss report form for submission to Fire Loss Bureau

Fire Loss Bureau
140 Aldersgate Street, London EC1A 4HX Telephone: 071-606 3757

Confidential arson loss report form

(To be completed by the Loss Adjuster (or insurer when an adjuster is not appointed) and sent to the Fire Loss Bureau at the above address)

Date of Loss and Time:

……

Classification of Loss by Type:

Tick box

Domestic ☐

Commecial/Industrial …….. (by trade)

Location:

(By outer postcode only e.g. SM7 or RH6) ……

Estimated Loss:

Material Damage

£

Business Interruption

£

Cause of Loss:

Tick Box

1. Fire caused or thought to be caused by vandals/intruders etc. (i.e. malicious) ☐
2. Fire known to be of deliberate origin and where there are suspicious circumstances, other than those included in 1. above ☐
3. Other suspicious fires which are the subject of further enquiry (i.e. unexplained cause/ doubtful circumstances), not included in 1. or 2. above ☐

(Further explanation/comment may be given where helpful)