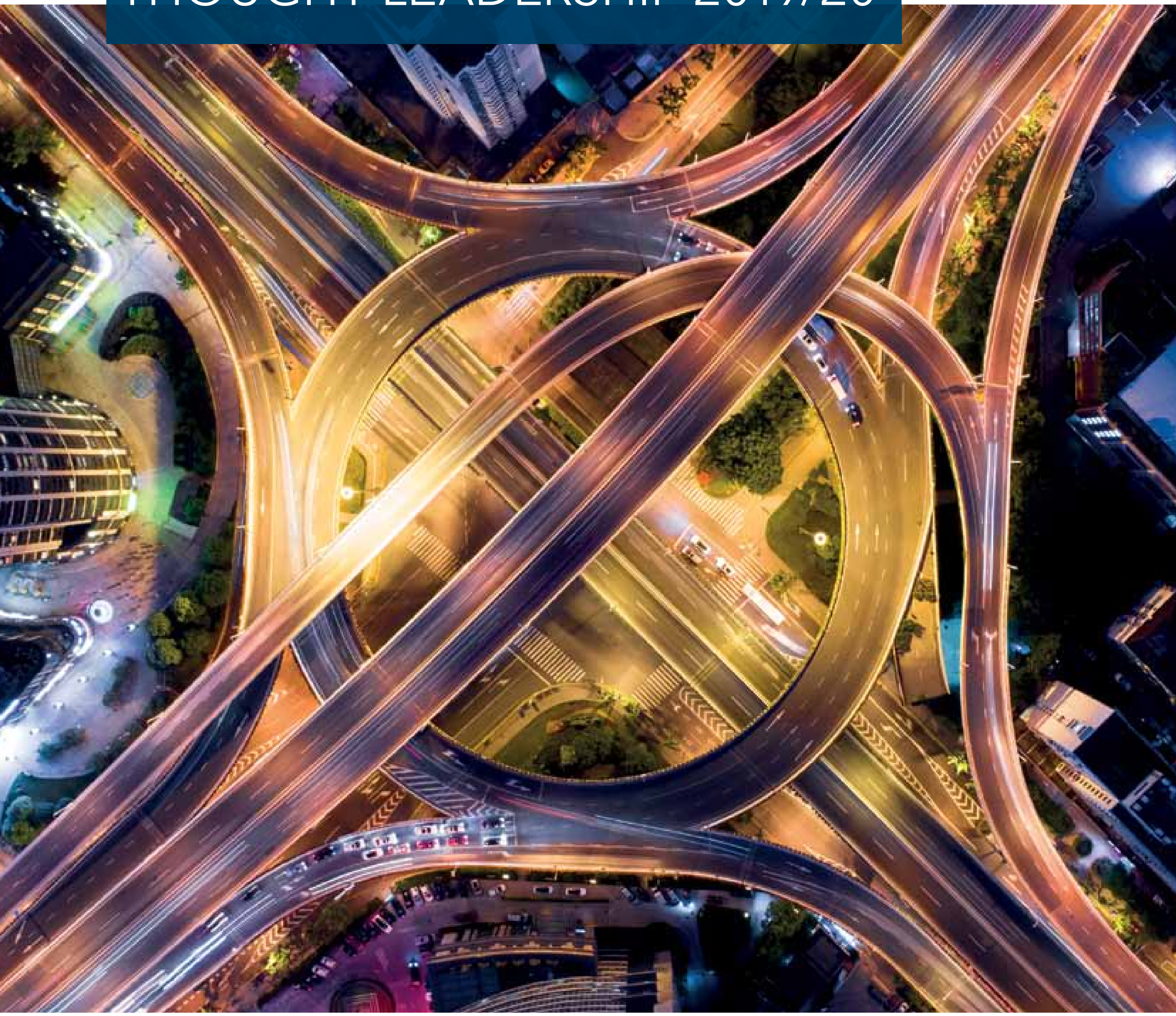
INFORMED INSURANCE: THOUGHT LEADERSHIP 2019/20



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WELCOME

Legalign Global's latest collection of thought leadership delivers "Informed Insurance" across the full spectrum of insurance risks and our global locations.

Wotton + Kearney is pleased to provide the latest perspectives on global insurance risk management. "Informed Insurance," spearheaded by DAC Beachcroft and shaped by all Legalign Global member firms, represents a notable evolution of the former "Insurance Market Conditions and Trends Report." In these pages you will find strategic insights into emerging market issues and practical implications for your organisation – today and well into the future.

A recent client survey highlighted a number of recurring C-suite concerns including technology, regulation and the impact of environment changes. All three are addressed in this report. While technological developments and cyber implications are common themes which run through all of our thinking, we open by taking a closer look at the drive for automation across land, sea and the air, followed by a shift of focus by regulators to conduct risk.

We also look at climate change and renewable energy and what insurers can do both in terms of investment and underwriting. Pooling our experience across various jurisdictions, we then turn our attention to developments in class actions around the world and the impact of the #MeToo movement.

One risk with all the technological developments is a loss of human contact. It is important we continue to develop our insights by collaborating with clients. I invite you to let us know your views and insights on these topics so we can help to maximise the opportunities they may bring to your business and claims strategies.

I hope you will visit the new "Informed Insurance" microsite (**https://insurance.dacbeachcroft.com**). I also hope this report will help to keep you well informed across a number of key global issues and look forward to continuing to provide strategic thinking alongside our global insurance law leaders to support your business.

David Kearney
Firm Chairman

Scan here for the microsite.

Legalign Global is a closely integrated alliance of the world's leading insurance law firms. The alliance was founded on the principle of offering clients uniform and unrivalled levels of legal excellence and service across all major commercial insurance lines. Each member firm has built a significant reputation for delivering high-quality legal services through decades of investment in the global insurance industry. Legalign Global offers the distinct advantage of independent advice from established lawyers in more than 60 offices worldwide throughout Europe, Latin America, Australasia, Asia Pacific and the United States. It is the largest team of specialists of its kind, understanding the risks and complexities of the global market, responding with world class service quality and efficiency.

BLD Bach Langheid Dallmayr, a German firm with close associations throughout Europe.
DAC Beachcroft, an international firm with coverage across the UK, Ireland, Spain, Latin America and Asia Pacific.
Wilson Elser, a US firm with offices across the United States and another in London.
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THE DRIVE FOR AUTOMATION

International moves towards automated vehicles pose a number of challenges, particularly on liability, data, cyber security and infrastructure.

The drive towards automated vehicles is accelerating and concentrating minds around the globe on the associated legal, regulatory, technical and physical challenges. The end goal is for safe, fully automated vehicles and mobility solutions that can drive anywhere without the need for a driver. It is the journey there that is the real challenge. As Matthew Avery, Director at Thatcham Research in the UK says: "There will be a mix of vehicles on our roads with different capabilities, some being driven manually, others automatically. It is vital that we make sure they can share the same road space and remain safe."

THE JOURNEY SO FAR

So how far towards automation have we come? The US-based Society of Automotive Engineers' Levels reflect the progress of automation, or rather the process of removing duties from the driver. Level 1 came in with the use of cruise control and lane-keep assist. Level 2, where computers take over multiple functions from the driver – and are intelligent enough to meld speed and steering systems together using multiple data sources – is where we are now in the UK.

Level 3 is conditional automation – where a driver must be on hand to respond to a request to intervene. In both Germany and France, Level 3 vehicles are now legal (since the amendment of the German Road Traffic Act in 2017 and adoption of the PACTE law in France) and can therefore be used on the road. The United Nations Economic Commission for Europe recently set up a working party that is expected to type approve Level 3 vehicles later this year, although the US and Australia do not have type approval, relying instead on self-certification. Audi calls its new A8 a Level 3 ready automated car – and it is being sold and used in Germany. However, its fully automated function, the traffic jam pilot (Staupilot) for speeds up to 60km/h, is not yet being activated due to unexpected problems in road construction.

The big step forward will be Level 4, where the driver will not really be needed in certain environments. It is anticipated that Level 4 vehicles will initially be used on motorways. This is where the likes of the Google Waymo and General Motors' Cruise fit in, although the Tesla has also been designed to be Level 4 ready and able to convert to automated driving via aftermarket software updates.

The great advantage of Level 5 vehicles is that they will be able to operate without conventional controls, which might see the end of steering wheels altogether. This is the stage that opens up mobility to non-drivers, including the young and the elderly. Whether the utopia of a Level 5 vehicle that can operate in all driving environments can be reached remains to be seen. It may be that they are instead restricted to low-speed, confined areas such as city centres and airports.

Testing of automated vehicles is also picking up pace globally. Peter Allchorne, Partner at DAC Beachcroft in Bristol and Head of the firm's Automated Vehicles Working Group, says: "In the UK, the next step is to enable testing on real roads without a human fallback safety driver either in the vehicle or remotely, as the Government pushes ahead to meet its set objective of a Level 4 automated vehicle being driven legally and safely in the UK by 2021."

GLOBAL APPROACH

Recent research shows that the development and use of new energy sources for transportation is a key catalyst to automation. Government support is a key influencer on prospective take up. "Scandinavia is right up there as the governments are very engaged and progressive in embracing electric vehicle readiness," says Allchorne. "In Norway, for example, 40% of new car sales are now electric vehicles as a result of favourable tax breaks, bus lane use and free parking incentives. In the UK, buying an electric vehicle is still expensive and the infrastructure patchy. Further UK Government support for charging infrastructure as set out in the Automated and Electric Vehicles Act 2018 is vital."

In Germany, electric car sales have been subsidised by the state since 2016. However, according to Dr Martin Alexander, Partner at Legalign firm BLD in Cologne: "Only around 134 million Euros have allegedly been distributed by way of subsidy. This corresponds to around 100,000 requests."

According to Christophe Wucher-North, Partner at DAC Beachcroft in Paris, it is anticipated that 80-85% of new vehicles in France will have Level 2 or Level 3 automation by 2020.

In Australia, Paul Spezza, Partner at Legalign firm Wotton + Kearney in Brisbane, says that there has been no firm commitment offered by the Australian National Transport Commission to having Level 3 and 4 automated vehicles operating by a given date, largely because of ongoing differences in the legislative regimes across Australian states and territories, and concerns about the extent to which infrastructure will be available to support them.

In Japan, the authorities are also pushing hard, and want to have Level 4 automated taxis operational in Tokyo in time for the 2020 Summer Olympics. It also has a real need to embrace automation and new mobility solutions as it has one of the highest populations over 65.

So, automated vehicles are coming – but can the regulation, law and infrastructure needed keep pace and how will this play out globally? "There is a real danger", warns Allchorne, "that different countries will take different approaches, slowing progress."

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> DAC Beachcroft

LIABILITY

The first priority is liability: when will the human driver be expected to respond to avert an accident and when will liability switch to the vehicle itself?

Olya Melnitchouk, Senior Associate and product liability expert at DAC Beachcroft in London says: "A safe transition to automated driving requires clear definitions and warnings to help consumers understand their own and their vehicles' responsibilities."

It is an important issue. A preliminary report into a fatal accident involving a Tesla Model 3 in March 2019 in the US showed that the autopilot feature had been engaged ten seconds before the crash. The driver did not appear to have his hands on the steering wheel and neither he nor the autopilot took any evasive action. In May 2016, a driver of a Tesla Model S died when his vehicle failed to spot a lorry crossing its path. The driver was found to have used autopilot for 37 minutes yet during that time he only had his hands on the steering wheel for 25 seconds. This was despite the car giving him visual warnings as well as sounding a chime to alert him to the fact that his hands needed to be on the wheel.

In Germany, Alexander explains: "In Level 3 vehicles, the driver may turn away from the traffic situation if a highly or fully automated driving function controls the vehicle. However, the driver must remain sufficiently alert that they can immediately take over the vehicle control again." This is helpful but not clear. As Allchorne says: "Human response times are variable and the estimated average for full re-engagement is about 20 seconds."

On this point, the UK's Association of British Insurers insists: "Until a vehicle can handle emergency scenarios without driver intervention, they can only be considered to offer an advanced driver assistance system (ADAS). In these vehicles, drivers remain fully responsible for the car and must be ready to take back control at any moment."

This aside, the preferred short-term insurance solution around the world for advancing automation is well illustrated by the UK's Automated and Electric Vehicles Act 2018. It extends compulsory motor coverage to driverless vehicles – so that in an accident, the insurer pays out and can then pursue the supply chain using existing common law and product liability laws should the driver not be at fault. Insurers would be able to limit their liability, for example, if the automated driving system (ADS) was tampered with by the insured, or if updates to the ADS were not installed or updated by the insured. The 2018 Act will not, however, apply until relevant vehicles are on the road.

The European Union has reviewed the scope of the Motor Insurance Directive and the Product Liability Directive and no changes were considered necessary for automated vehicles. Automated vehicles will be required to have third-party liability insurance in line with the Directive. The insurer can take legal action against a manufacturer under the Product Liability Directive if there is a malfunction or defect in the ADS. It is also possible that claims could be brought for negligence or breach of contract.

One issue that remains uncertain is whether a product, as defined in the Product Liability Directive, would include an over-the-air update which is purely software and not incorporated within a physical medium. The European Commission has established an Expert Group on liability and new technologies to consider such questions and develop principles which can serve as guidelines for possible adaptations of applicable laws at EU and national level relating to technologies such as automated cars.

DATA

Whatever the legal framework countries adopt, one thing is sure: insurers, manufacturers and the authorities will need to have an agreed minimum post-collision data set sharing arrangement in place – with appropriate contractual provisions on data protection – with those who process any personal data. This is not as simple as it may sound and it still needs to be clearly established what data sets will need to be shared between the parties in the event of an accident.

The General Data Protection Regulation (GDPR), which came into force on 25 May 2018, has enhanced an individual's data privacy rights. Any processing and sharing of personal data which is collected by automated vehicles will need to comply with the various obligations set out in the GDPR. Failure to do so could result in significant fines (of up to 4% of annual global turnover or 20 million Euros, whichever is the higher) or enforcement action such as orders to stop processing personal data.

In Germany, comments Alexander, the 2017 Road Traffic Act (Straßenverkehrsgesetz) stipulates certain data must be recorded anonymously if a highly-automated driving function takes over control of a vehicle and that authorities and third parties can apply for access to it in the event of an accident. Insurer Allianz has proposed the data must be handled by an independent trustee from whom the manufacturer and insurer can request information in future.

The French data protection authority (CNIL) has also issued a package of compliance guidelines for personal data from connected vehicles but according to Wucher-North, the CNIL is yet to address in more detail the future needs of data sharing.

According to Spezza, the Australian National Transport Commission is following the German approach on the issues of privacy and cyber security. He says that the collection, use and disclosure of personal information by entities involved in the roll out of ADS will likely be governed by the Commonwealth Privacy Act rather than the legislative regimes dealing with privacy in the states and territories. Spezza notes: "On a broader level, there are still some doubts as to whether the existing legislation adequately deals with the risks of government access to automated vehicle data."

In the UK, the legal issues are being looked at by the Law Commission. Crucially, it excludes data, cyber security and infrastructure from its remit. It has, however, mooted some relevant questions that it believes need to be addressed:

- Should there be a road accident investigation branch to consider high-profile road accidents (including those involving driving automation)? An advantage of this is that it could develop high levels of technical expertise and pool data over many individual incidents, however, this would involve potential data sharing implications that would need to be considered.
- Are there any potential problems in retaining data for long periods of time to deal with possible claims under the Automated and Electric Vehicles Act 2018?
- Should developers disclose their ethics policies?

But there are wider issues, flags Shehana Cameron-Perera, a data protection and cyber specialist at DAC Beachcroft in London: "Another significant data issue relates to the broader use and ownership of the much richer data set that will be collected by the vehicles on an ongoing basis. Beyond the value to insurers for pricing and underwriting, this data is also of real commercial value to any marketing-orientated organisation." As Allchorne adds: "If drivers see real benefits from sharing their data, such as receiving timely discounts and savings via the in-car infotainment screen, then they may be happy to share their data."

CYBER SECURITY

"The move to interconnected cars that talk to each other in real time under Level 4 and the potentially large amounts of data that may be collected by automated vehicles also up the stakes in terms of increased vulnerability to hacking and cyber-attacks. Ultimately, as technology advances, more useful data will be collected, which will consequently become more attractive to hackers or could result in threats from terrorist or criminal activity," advises Cameron-Perera.

The European Commission consulted on the issue of data and cyber security at the end of 2018, but at the time of writing the results have not been published. The expected approach is one of security by design, transparency over use of personal data, board-level accountability and requirements to keep abreast of the whole supply chain to stop any weak links. That final point is critical as security is only as good as the weakest link when transferring data. A requirement for software patches and updates to be rolled out by vehicle manufacturers – and infrastructure providers – in a timely manner is also likely to be included, learning from problems experienced recently in the airline industry.

INFRASTRUCTURE

Infrastructure is another internationally and regionally variable factor – and one susceptible to power surges, outages, hacking, everyday wear and tear and lack of maintenance.

"The sheer scale of Australia against what is a relatively small population, the majority of which is concentrated in the south-east corner of the country, will present challenges from an infrastructure and technology perspective," says Spezza. "Australia has approximately 900,000 kilometres of roads – over half of which are unsealed and unmarked. The inconsistencies among urban, regional and country roads and how they interface with digital infrastructure, such as mapping and communications, will necessarily require considered and co-ordinated management by the Federal Government."

One issue is that dynamic electronic signs and LED signs do not necessarily have the same level of functionality as that seen in Europe. "Australia's geographic coverage of cellular communication is also relatively low when compared with other developed countries, particularly outside urban areas. We have seen examples of motor vehicle manufacturers withholding particular safety applications in vehicles because of limitations in our infrastructure network," adds Spezza.

The lack of basic white lines and patchy 4G network coverage is an issue in the UK – especially as the Government plans to work with the existing infrastructure to meet its 2021 target.

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> Wotton + Kearney

Network coverage across the rest of Europe is generally better than in the UK, and the motorway networks also have longer stretches of road than the UK, making vehicle platooning – which can reduce stop-start traffic, lowering emissions and costs – more achievable.

The US, which is ripe for vehicle platooning, should, in theory, be streets ahead in terms of early adoption. However, while the Federal Government is responsible for regulating the safety performance of vehicles, Frank Manchisi, Partner at Legalign firm Wilson Elser in New York, says states and local governments regulate the licensing of drivers, establish the rules of the road and formulate policy on tort liability and insurance. In seeking a solution, Manchisi says, the National Highway Traffic Safety Administration (NHTSA) is pushing for uniformity and urging states and localities to work to remove barriers such as unnecessary and incompatible regulations to automated vehicle technologies and to support interoperability.

Australia has a similar issue, says Spezza, with an estimated 716 pieces of federal, state and territory legislation requiring amendment. "In November 2018, Australian state and territory transport ministers agreed to remove barriers to automated vehicles in Australia with the development of a purpose-built national law," says Spezza. He further notes that those ministers endorsed the safety assurance approach of automated vehicles including mandatory self-certification by the company bringing the technology to market and a clear set of performance-based safety criteria against which companies must provide evidence.

THE IMPACT ON INSURANCE

Safety has been the main driver in the push for automated vehicles – and it is easy to see why. According to the World Health Organisation, around 1.35 million people die on the roads each year and 95% of all road traffic accidents are caused by human error. Advances in ADAS are already helping to reduce the amount, and cost, of personal injury and it has been estimated that automation could reduce insurance premiums by 75%, especially if liability is shifted from drivers to manufacturers and technology companies.

However, as Allchorne explains: "The cost of physical repairs is also set to rocket as innocuous bumps and scrapes cost thousands to repair, with complex and intelligent headlights and bumpers. Perhaps, ironically, this will drive insurance underwriters to focus more on the vehicle itself, rather than the driver, much sooner than the switch to full automation would entail."

CONSUMER COLLABORATION

A further consideration for manufacturers is consumer acceptance and education. While public confidence varies in different jurisdictions, there remains both distrust and a lack of understanding generally. For example, the labelling of Tesla's current Level 2 driver assistance system as 'Autopilot' is not helpful as it implies the vehicle is capable of driving itself when it is not, Allchorne warns.

In the final analysis, the pace of change will be dependent on industry collaboration with consumers. As Allchorne advises: "If automated vehicles are to achieve mass market penetration, industry stakeholders must keep consumers at the forefront of their minds as they bring to market increasingly sophisticated new vehicle technologies."

WHAT IS HAPPENING AT SEA?

The testing of automated crewless craft is underway on a limited scale, but is increasing says Toby Vallance, Partner at DAC Beachcroft in London. One example is Finferries' Falco, developed with Rolls Royce, which navigated a distance of 1.5 miles in Finland under full autonomous control, with the return journey conducted under remote control. It is notable that unlike with automated road vehicles, remote controlled ships (with or without crew) will form part of Maritime Autonomous Surface Ship development. And in Norway, testing of the Yara Birkeland, an automated fully electric zero-emission container vessel operated by fertiliser company Yara, is aiming to be in full operation by 2020.

These developments have helped to focus the mind of the regulator, the International Maritime Organisation (IMO), says Vallance, and its maritime safety committee is looking at how crewless vessels could work in practice. The IMO is also reviewing the Safety of Life at Sea regulations, which currently require crews on board; and the existing collision regulations.

As the reliance on technology increases, the IMO is also looking at liability and cyber issues, such as an automated engine management system being hacked and shut down. GPS-spoofing is also on the increase, including recent incidents involving the South Korean fishing fleet and the US Navy.

Investment is being driven by economics and the cost savings from removal of crew quarters, crew pay and overall efficiency. "We will see more vessels being tested on a coastal basis and, over the next five years, remote control shoreside vessel management and improved regulation," says Vallance. "However, we are looking at 2030 and beyond before we see regular deployment of fully automated ocean-going vessels due to the conservative nature of the maritime sector and the entrenched seafaring lifestyle."

THE RISE OF DRONES

"Drones continue to make inroads in both the leisure and commercial spheres, with a major uptick in the latter," says Stephen Turner, Legal Director at DAC Beachcroft in London, "especially in construction, offshore energy, agriculture, and insurance underwriting and claims."

Growth in urban environments is limited with the issues of congestion, safety and interference perfectly illustrated by incidents around London Gatwick and Dubai International airports. While improved geo-fencing helps, it can only do so much as individual drone owners also need to upgrade their software and adapted or hacked drones can – and will – circumvent any security.

The established aviation sector provides the obvious framework for regulation and standards, and the EU is working with the international aviation regulator. The direction of travel is clear; the Civil Aviation Authority in the UK will, for example, introduce increased certification and training requirements for drone operators in November 2019, while new EU-wide rules on the use of drones have been published and will be in force from 2020.

"The onus will be placed on manufacturers to build in cyber and data security features. However, emphasis is also shifting towards the operator," summarises Turner, "with the need for pilots to be registered, certified and trained."

Privacy issues are also on regulators' minds, as many drones have cameras fitted – raising concerns over how data and information collected are shared. In the UK, guidance from the Information Commissioner's Office relies on the existing pre-GDPR CCTV code of practice for commercial users. However, in Spain, the Government plans to create guides for manufacturers on processing data and the protection of communications, says Pilar Rodriguez Lopez, Partner at DAC Beachcroft in Madrid. Training centres will also be created for operators and measures put in place for the control and inspection of operations.

Contributors:

Dr Martin Alexander
BLD, Cologne
martin.alexander@bld.de

Peter Allchorne
DAC Beachcroft, Bristol
pallchorne@dacbeachcroft.com

Shehana Cameron-Perera
DAC Beachcroft, London
scameron-perera@dacbeachcroft.com

Wendy Hopkins
DAC Beachcroft, London
whopkins@dacbeachcroft.com

Olya Melnitchouk
DAC Beachcroft, London
omelnitchouk@dacbeachcroft.com

Stephen Turner
DAC Beachcroft, London
sturner@dacbeachcroft.com

Toby Vallance
DAC Beachcroft, London
tvallance@dacbeachcroft.com

Christophe Wucher-North
DAC Beachcroft, Paris
cwuchernorth@dacbeachcroft.com

Pilar Rodriguez Lopez
DAC Beachcroft, Madrid
prodriguez@dacbeachcroft.com

Frank Manchisi
Wilson Elser, New York
francis.manchisi@wilsonelser.com

Paul Spezza
Wotton + Kearney, Brisbane
paul.spezza@wottonkearney.com.au

REGULATORS SHIFT THEIR FOCUS TO CONDUCT RISK

Increasing government intervention and regulation of conduct risk are forcing insurers from all jurisdictions to change the products they sell and who they sell them to.

Global and national regulators are still smarting from the battering they took in the wake of the financial crisis a decade ago. Many were accused of being asleep on the job, of having relaxed regulations too much and not spotting the looming problems across the world's financial markets. Their response has been to review, revise, strengthen and extend regulation across all sectors. This includes the insurance industry, despite its many protestations that its severely depressed investment returns make it one of the victims of the financial crisis, not a cause of it.

The main focus in the immediate aftermath of the crisis was prudential regulation, mirroring the tougher rules for banks. Solvency II and IFRS17 are both consequences of that phase of regulatory review.

That focus is now shifting. Regulators are not sitting back. Conduct risk is moving centre stage, bringing pressure on the financial services sector to do more to protect vulnerable customers (see box: EIOPA raises its conduct risk game). This relentless pace of regulatory change is clear evidence of the determination of governments and regulators not to be caught out again.

"Some of it is still a backlash from the financial crisis and the 'light touch' approach to regulation, urged by politicians, that preceded it. That wasn't necessarily the direct cause of the financial crisis, but it created a regulatory environment in which it could happen," says Mathew Rutter, Partner at DAC Beachcroft in London.

"As a consequence, governments and politicians want to appear to be the champion of the consumer and this is driving the regulatory agenda."

CONDUCT RISK IN THE UK

As that agenda develops, there is an expanding range of regulatory requirements in different jurisdictions focused on demonstrating customer value and eliminating poor advice, so-called 'conduct risk'. The specific actions may differ, but they are all essentially pulling in the same direction and influencing each other. There is an emerging international consensus on what conduct risk means and how consumer detriment manifests itself. Insurers need to plan to manage the impact of the regulatory changes flowing from this, as it is changing the way insurance products are designed and sold.

The UK has been one of the leaders in developing a new regulatory regime for conduct risk, partially driven by two decades of mis-selling scandals around personal pensions, endowment mortgages and payment protection insurance. As a result, the Financial Conduct Authority (FCA) is now far more proactive, says Rutter.

"It has moved from reacting to abuses and just preventing detriment, to trying to ensure that markets work better, focusing on improving outcomes for consumers rather than just preventing harm."

This is evident in the debates around dual pricing (where new customers are charged lower premiums than existing customers), add-ons and overall product transparency.

Some of these issues are not as simple as regulators and consumer champions make them out to be, says Rutter:

"With dual pricing everyone focuses on those who lose out, but there are others – those who shop around – who benefit from it. It would be hard for the industry to agree collectively to move to single pricing without being at risk of breaking competition law. Single pricing will also leave firms vulnerable to those who want to buy market share.

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> DAC Beachcroft

"If you also attack add-ons and marginal benefits in products, you run the danger of ending up with bland, vanilla products with no differentiation and everyone charging the same price. What does that mean for consumer choice?

"I think the FCA understands these dangers, but it is under a lot of political pressure to do something about things like dual pricing."

IMPACT ON EUROPE

Across Europe, the industry is coming to terms with this new proactivity among regulators, with the European Insurance and Occupational Pensions Authority (EIOPA) setting a firm lead. In February 2019, it published a framework for assessing conduct risk throughout product lifecycles, making clear this was a priority as it follows up what it sees as the success in driving through the implementation of the Insurance Distribution Directive (IDD) (see box: Vulnerable customers – the new regulatory horizon).

National markets certainly feel the IDD has been the catalyst for tough action by regulators. "The IDD has increased the attention paid to conduct risk. Regulation started slowly with the compliance and risk management procedures under Solvency II, but now we have a lot of changes, especially to commissions and processes in firms," says Dr Alexander Beyer, Partner at Legalign firm BLD in Cologne.

The German Federal Financial Supervisory Authority – BaFin – has clamped down on commission sharing by insurers and intermediaries, including commission overrides and using vouchers as an incentive to buy policies.

"This has had a significant impact on intermediaries as they are no longer allowed to receive additional commission based on how many contracts from an insurer they have in their portfolio or accept any form of bonus commission," says Beyer.

Rebating commission to a policyholder has also been outlawed as part of the implementation of the IDD. This has already been challenged in the courts in Germany where they have said that only an insurer can reduce the premium, not an intermediary.

Beyer says the market anticipated many of the new requirements the IDD would impose, creating voluntary codes so that the impact of the changes has not been overly dramatic for many insurers, outside of the commission debate.

In Spain, the situation is slightly different, advises Marisol Lana, an Associate at DAC Beachcroft in Madrid: "The IDD should have been transposed into national law in July 2018 and applied from October 2018, but this has still not happened. The project has been paralysed by the call for parliamentary elections and it is not expected to be ready until 2020.

"However, even without waiting for the legislation, Spanish insurers are taking steps well beyond the proposed regulation, focusing on transparency and putting the customer at the heart of their actions. The change of paradigm towards conduct risk is already very noticeable through the websites of the vast majority of Spanish insurers. The Spanish insurance regulator is also focused on promoting and improving the information provided by and transparency of the insurance market, encouraging insurers to simplify the language of their products and tailoring it to the target profile of customers for each product."

FINANCIAL REFORM IN AUSTRALIA

Some of the biggest upheavals in financial services regulation have been in Australia, where a series of financial scandals led to the creation of a 'Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry'. This has created an ambitious and wide-ranging reform of financial services regulation, says Cain Jackson, Partner at Legalign firm Wotton + Kearney in Melbourne:

"We have had a period of ten years of dramatic reforms around financial services. This has tended to track corporate collapses and financial catastrophes, but now with the Royal Commission the Government is looking at non-financial risks, including conduct risk."

This change is going to hit the insurance industry hard, says Nick Lux, a fellow Partner at Wotton + Kearney in Melbourne:

"The focus in the past has been on compensation and remediation. The Royal Commission has been very critical of the regulator for stopping there and not going on to punish and deter."

This is having a major impact on insurers' costs, with many now looking at extensive self-insurance of the costs of investigations and prosecutions.

According to Jackson, some of the criticism heaped on insurers has been unfair but is not going to go away as the media and politicians have the industry in their sights.

"Insurance has been caught in the backwash of the bad behaviour of the banks," says Jackson, although the Australian insurance sector has had its own scandals to contend with, especially with add-ons, a parallel with the UK. "Car dealerships were selling add-ons as part of a loan and taking up to 70% in commissions. This affected about seven insurers but was one of the key case studies used to claim that the insurance industry was failing customers. The perception is that there is now a need for reform across the board rather than targeting problem areas."

A NEW APPROACH IN THE US

The pressure for tougher regulation of the behaviour of firms has also been a feature of the changing regulatory landscape in the United States.

A lot of insurance regulation there is at state level, but the tone and emphasis is set by the Securities and Exchange Commission (SEC) and it has been far more proactive in pursuing bad conduct by firms since the turn of the century, says Jim Thurston, Partner at Legalign firm Wilson Elser in Chicago.

Forced into action by scandals at Enron, the collapse of firms when the dot-com bubble burst and the behaviour of serial fraudsters like Bernie Madoff, the SEC and Department of Justice became tougher. "For the first time the US Government pursued the directors and officers for serious jail time. That was really unusual before the financial meltdown in the early 2000s," says Thurston.

"The Government in the United States wants to be seen as one of the leaders and not to be lagging behind as it sometimes has been in the past."

This new emphasis on weeding out and punishing bad behaviour has not changed since Donald Trump was elected President. "When he came to office many saw him as an ally of business and thought he would be friendlier. However, the SEC and Department of Justice enforcement actions against individuals and entities do not show much change."

In 2015-16 there were 784 actions. This dropped slightly to 754 in 2016-17 but jumped by almost 9% to 821 in 2017-18. "These enforcement procedures are used as a barometer of how seriously the US Government is regulating the financial services sector."

With new regulatory regimes coming on stream around the world, insurers and intermediaries are going to have to place conduct risk at the heart of their compliance regimes.

EIOPA RAISES ITS CONDUCT RISK GAME

The pan-European regulator published a new framework for conduct risk at the end of February 2019. It says its aim is to clarify the drivers of conduct risk and their role in the emergence of consumer detriment.

It highlights the issues faced by consumers and the types of conduct risks EIOPA and the national competent authorities should focus on. It sets a common starting point for more practical supervision of particular products, services or market segments, for instance, through 'deep dive' thematic work or for future policy development, some of which has already been seen in the UK with the investigations into add-ons and the wholesale insurance markets.

The framework focuses on conduct risk throughout all stages of product lifecycles, that is to say from the point before a contract enters into force through to the point when all obligations under the contract have been satisfied.

The risks identified by EIOPA cover the following areas:

- Business model and management risks – risks arising from how undertakings structure, drive and manage their business and from relationships with other entities in the value-chain.
- Manufacturing risks – risks arising from how products are manufactured by insurance undertakings prior to being marketed and how they are targeted to customers.
- Delivery risks – risks arising from how products are brought to the market and from the interaction between customers and insurance undertakings or intermediaries at the point of sale.
- Product management risks – risks arising after the sale of the insurance product relating to how products are managed and how insurance undertakings or intermediaries interact with and service customers until all obligations under the contract have ceased.

Many of these risks will not be new to firms, with issues such as product bundling, conflicts of interest and product reviews already covered by rules under the IDD. However, the framework provides important signposts for firms wanting to understand how the conduct priorities of EU supervisors and others might develop.

VULNERABLE CUSTOMERS – THE NEW REGULATORY HORIZON

The emergence of regulatory concern around vulnerable customers creates some tricky issues for insurers, starting with definition, says Mathew Rutter, Partner at DAC Beachcroft in London.

"How do you define vulnerability? How do you ensure consistency?" he asks.

"There are dangers of pigeonholing people if you take too simplistic an approach. For instance, you cannot assume that everyone over 80 is vulnerable and needs special consideration. It will not always be so much about the definition as how you apply it, as people may not define themselves as vulnerable."

According to Rutter, defining vulnerability and identifying those who fall within the definitions will require firms to share data and this will raise all sorts of data protection issues that will have to be addressed by the regulators.

There is also a danger that some people may look to define someone as vulnerable in retrospect and argue they were sold cover they did not need or that was inappropriate. "If you regulate after the fact, firms will need higher margins to cover potential compensation."

Contributors:

Dr Alexander Beyer
BLD, Cologne
alexander.beyer@bld.de

Mathew Rutter
DAC Beachcroft, London
mrutter@dacbeachcroft.com

Marisol Lana
DAC Beachcroft, Madrid
mlana@dacbeachcroft.com

Jim Thurston
Wilson Elser, Chicago
james.thurston@wilsonelser.com

Cain Jackson
Wotton + Kearney, Melbourne
cain.jackson@wottonkearney.com.au

Nick Lux
Wotton + Kearney, Melbourne
nick.lux@wottonkearney.com.au

FROM FOSSIL FUELS TO RENEWABLES: THE CHALLENGE OF CLIMATE CHANGE

When the history of the early 21st century is written by future generations, it will be our response to the huge threats from man-made climate change that will define our age.

While artificial intelligence and Brexit may transform commerce and society, it is climate change that will irrevocably alter the world. Facing up to the impact of climate change, especially carbon emissions from fossil fuels, is now top of the agenda for many supra-national bodies such as the United Nations, the European Union and the World Bank. Climate change activists are no longer on the fringes but are listened to by these organisations, whether that be campaign groups such as Unfriend Coal or the Swedish teenager Greta Thunberg.

The insurance industry has now been dragged centre stage in responding to the challenge of climate change. This goes far beyond the need to meet claims from the natural catastrophes now attributed to climate change, although this is a major issue for regulators (see box: Regulators vigilant on climate change impacts). The huge losses of recent years have hit global insurers and the Lloyd's market very hard and demand a re-assessment of risks, increases in premiums and investment in claims handling capabilities. That is a traditional role and response for the insurance industry.

However, the climate change debate and the agenda around sustainable finance takes the industry into uncharted territory. It is pushing insurers to respond to a political agenda by shunning fossil fuels as underwriters and investors. It also brings a new range of risks to the table as the renewable energy sector expands rapidly.

THE ROLE OF THE INSURANCE INDUSTRY

Top of the hit list for the campaigners is coal. The pressure group Unfriend Coal has the ear of the United Nations and the European Union. It is uncompromising in its belief in the central role of the insurance industry in driving towards its target of zero coal consumption by 2050, a modest ambition compared to some other climate change campaigners' demands.

"Insurance companies are in a unique position to accelerate the transition to a low-carbon economy. As risk managers they play a silent but essential role in deciding which types of project can be built and operated in a modern society. Without their insurance, almost no new coal mines and power plants can be built, and most existing projects will have to be phased out.

"With assets of approximately US$31 trillion, insurers are also the second largest group of institutional investors after pension funds.

Reports commissioned by Ceres (a sustainability non-profit organisation) and Unfriend Coal have found that the largest US and European insurers have invested close to US$600 billion in fossil fuels," says Unfriend Coal.

The campaign also points to the industry having a vested interest in ending coal-fired energy production:

"Insurance companies cover a large part of the increasing damages caused by ever more serious hurricanes, wildfires, floods and droughts. They have access to the world's best climate science and have warned about climate risks since the 1970s. Continuing to prop up the coal sector is incompatible with their fundamental mission to protect us from catastrophic risk."

"Their view is that if a coal-fired power station cannot get insurance then it can't operate," says Toby Vallance, Partner at DAC Beachcroft in London.

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>
> Toby Vallance
> DAC Beachcroft

Several large insurance groups have responded to the pressure to limit and eventually withdraw from underwriting the extraction of coal and coal-based energy production, including AXA, Zurich, Allianz, Generali, QBE and most recently Chubb. At the end of 2018, 19 major insurance groups had also announced they would stop investing in coal.

This raises several interesting challenges for the insurance industry, and is not without its controversy and risks.

DIVESTMENT

The divestment argument has divided opinion with the leading research body, the Geneva Association, urging caution, according to its Director of Extreme Events & Climate Risk, Maryam Golnaraghi:

"A rising number of Chief Investment Officers are looking into opportunities for investing in green and climate-neutral assets, but they caution against divesting too suddenly from fossils fuels. This is because the biggest financial force in developing renewable energy is the fossil fuel companies as that is their exit strategy from carbon. Divesting too quickly could essentially be choking funding for investing in green technology."

This concern was also raised at a recent European Commission conference on the progress towards sustainable finance when Hiro Mizuno, the head of Japan's public sector pension scheme, the US$1.4 trillion Government Pension Investment Fund, said that: "Divestment means that we transfer ownership from the responsible investor to the less responsible investor; that's why we have a policy of no divestment."

Similar concerns surround the withdrawal of underwriting capacity, says Carl Pernicone, Attorney at Law at Legalign firm Wilson Elser in New York: "Fossil fuels will still be needed as a back-up even after renewable capacity increases. What do you do when the sun doesn't shine and the wind doesn't blow? You can reduce reliance on it but can you get rid of it altogether?"

While it is unlikely we will be able to get rid of fossil fuels in the near to mid-term, growth in the likes of tidal energy and energy storage technologies may in time enable renewable energy to replace fossil fuels.

WHAT COVER WILL BE AVAILABLE

What does the withdrawal of major insurers from underwriting coal mean for those businesses still needing cover?

"They will probably have to pay more for it, especially in Europe," says Duncan Strachan, Partner at DAC Beachcroft in London. "It is a different picture in North America. The fossil fuel industry in North America is huge, as it is in China and with oil and other natural resources in Latin America. There is little prospect in the current political climate, for instance, that the Venezuelans are not going to insure the oil industry."

"I don't think you can totally move away," says Pernicone. "They will have to insure somewhere. They may have to self-insure or form captives. If they clean up their act perhaps some of the insurance groups will come back."

According to Hamish Roberts, Chief Executive Officer of the Power Division at JLT Specialty, writing in a US publication, brokers are not experiencing any problems finding capacity for fossil fuel risks: "As a broker we are still able to arrange company programmes for our clients despite this public and noticeable withdrawal of capacity. Yes, more insurers and reinsurers are stopping or limiting their insurance support for coal, but an ingenious broker will always be able to devise risk-transfer solutions."

POTENTIAL CLAIMS

Remaining active as an underwriter of fossil fuel-dependent businesses will not be without its risks, says Strachan.

"The operators are going to face increasing claims for environmental damage. Traditional types of cover will not extend to that type of liability. There is a big gap for the insurance industry to offer cover for the sort of awards we are likely to see," he adds, citing a recent award of US$10million in Ecuador for damage to the local community by an oil refinery.

Elsewhere in Latin America, governments are making significant moves to hold firms responsible for pollution, says Liliana Calvo Rojas, a Director at DAC Beachcroft in Mexico.

"In 2012, Mexico passed the Climate Change General Law in order to promote education, research, development and mitigation of climate change.

"We now have a Federal Protection Authority for environmental purposes, which carries out inspection and surveillance actions for the entities required to provide reports due to the emission of gases. In the case of an imminent risk, they could be subject to a sanction in accordance with environmental laws, with the directors being exposed to administrative sanctions and lawsuits."

In Peru there is legislation in place that requires liability policies to respond to claims for environmental damage.

One case from Peru has found its way into the European courts. A Peruvian farmer has taken a German firm to court to recover the cost of protecting his home town from damage caused by a melting glacier. The farmer is arguing that carbon dioxide emitted by factories owned by RWE had been a major contributor to global warming and the consequent melting of the glacier. The case was originally rejected by the lower court in Germany but has been ruled admissible. This will be watched very carefully across Latin America, says Calvo Rojas, and could provoke many more claims.

Governments across Europe have passed or are in the process of passing similar laws, with France leading the way in requiring firms to report on their carbon emissions. It is not hard to see the regulatory and reporting burden on energy producers increasing significantly in the next few years.

"In theory, there should be capacity to cope with this but that cannot be guaranteed. If these actions become commonplace, say if there is an action from a large urban area and courts around the world follow that, then there might be doubt over the capacity available," warns Vallance.

RENEWABLE ENERGY - NEW RISKS

As they move away from fossil fuel risks, insurers are expected to be supportive of the rapidly developing renewable energy sector, such as onshore and offshore wind farms and solar energy installations. This also presents challenges, says Bastian Finkel, Partner at Legalign firm BLD in Germany:

"If insurers change from covering old energy types to newer energy types, they have a whole new range of risks on their books. They will then have risks of which they do not have much experience."

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>
> Bastian Finkel
> BLD

This is not just about the physical risks but also about the increased connectivity and inter-dependence of different producers and firms in the production and distribution supply chain says Finkel's colleague, Partner Christina Eckes: "Insurers will also have to look at how the technology moves together with blockchain and data risk. These issues about how they communicate are very new."

In her view, this is a political issue as well: "The discussion is all about the new infrastructure and insurers are putting risks on their books that they might not be able to assess in a way they could in the past."

For Denise Eastlake, Senior Associate at DAC Beachcroft in London, rapid development of the technology inevitably poses a challenge for insurers, however, there is already capability in the market:

"There are certainly lots of new entrants to the market and the technology is constantly evolving. However, the first UK wind turbine came online in 1991 so there is already some considerable expertise in the market. Insurers can also draw on their knowledge from underwriting and handling claims in other areas of the energy sector and dealing generally with engineering risks.

"The impact is not only in relation to the insureds that construct and operate renewable energy plants, but extends to all those engaged to service, monitor and repair these plants. You may have a relatively small engineering firm facing large business interruption claims where defective works have caused an interruption of supply."

One response to this problem has been to put broader policies in place at the project planning stage, says Eastlake: "Project policies are getting wider and wider as the banks and investors insist on these risks being addressed."

The risks to which some renewable energy installations are exposed are not well understood, says Vallance: "Many of them have a vulnerability to extreme weather events, perhaps related to climate change."

This is another issue that needs to be addressed early in a project, says Eastlake: "It is hard to say whether the design, materials and build are right as windspeeds, for instance, are often unknown. It is essential that engineers and underwriters delve into these risks. Smart underwriting comes into its own and pays off in the long-term."

"In Australia, we have seen rapid investment in renewable infrastructure," says Adam Chylek, Head of Property and Energy at Legalign firm Wotton + Kearney in Sydney. "Many of the issues that we are seeing arise from the perceived imbalance between the almost unfettered appetite to develop the assets, against the high risks – associated with weather, defects in design and workmanship – which lead to significant claims. Many component assets are designed or manufactured offshore, and regularly have a critical operational impact; when they fail there is a chance of a significant total loss.

"We are also seeing contractors being asked to agree to unworkable warranties in areas around foundations, ground stability and operational life, which often far exceed ordinary contractual terms and the capacity of responsive insurance policies."

It is important to understand what can go wrong with renewable energy installations, says Ryan Williams, Attorney at Law at Legalign firm Wilson Elser in Denver:

"We need to look at what renewable energy has in common with other energy production industries as well as trying to imagine what is different about the renewable energy businesses. We have had to consider what end-users might expect and what the potential claims might be. With renewables it is more about the economic impact of something going wrong than the environmental impact."

The insurance industry, reluctantly or willingly, is a key player as the world embarks on its journey from fossil fuels to renewables and is going to have to respond to many new challenges along the way.

REGULATORS VIGILANT ON CLIMATE CHANGE IMPACTS

The Bank of England has led the way among global regulators in warning of the risks climate change poses to the insurance industry. Through the Prudential Regulation Authority (PRA) it has released a series of supervisory statements urging insurers to identify and manage financial risks relating to climate change, the most recent being in April 2019.

The PRA expects insurers to have plans for how best to approach climate change within their current policies, especially meeting massive claims from the growing number of severe natural catastrophes. It wants the industry to look at how it can address the risks posed by this issue.

It has also warned that insurance companies could face a significant downgrade on their investments in fossil fuel companies if governmental pressure accelerates the move away from fossil fuels.

Contributors:

Christina Eckes
BLD, Cologne
christina.eckes@bld.de

Bastian Finkel
BLD, Cologne
bastian.finkel@bld.de

Denise Eastlake
DAC Beachcroft, London
deastlake@dacbeachcroft.com

Simon Jones
DAC Beachcroft, London
sdjones@dacbeachcroft.com

Duncan Strachan
DAC Beachcroft, London
dstrachan@dacbeachcroft.com

Toby Vallance
DAC Beachcroft, London
tvallance@dacbeachcroft.com

Liliana Calvo Rojas
DAC Beachcroft, Mexico
lcalvo@dacbeachcroft.com

Ryan Williams
Wilson Elser, Denver
ryan.williams@wilsonelser.com

Carl Pernicone
Wilson Elser, New York
carl.pernicone@wilsonelser.com

Adam Chylek
Wotton + Kearney, Sydney
adam.chylek@wottonkearney.com.au

THE #METOO MOVEMENT: CHANGING THE WORKPLACE FOREVER

Movements such as #MeToo and #TimesUp have meant harassment claims have extended beyond employment practices liability into D&O liability insurance and both governments and employers are considering significant changes.

When American actress Alyssa Milano encouraged survivors of sexual harassment to post #MeToo as their status back in October 2017, few could have predicted the impact this single tweet would have. Although the phrase had been around since 2006, the power of social media meant it quickly went viral, with far-reaching repercussions.

Just a week after that initial tweet, #MeToo had been tweeted more than 1.7 million times by people in 85 countries. On Facebook, 4.7 million users around the world had posted in excess of 12 million posts, comments and reactions.

EXTRAORDINARY REACTION

Raising the profile of sexual harassment and giving a voice to many who had not previously felt able to speak has shaken the world. "It's been extraordinary," says Ricki Roer, Regional Managing Partner at Legalign firm Wilson Elser in New York and founding Chair of its National Employment & Labor litigation practice. "Claims of sexual harassment have increased dramatically since 2017. We haven't seen anything on this scale since allegations of sexual harassment were brought against Clarence Thomas in 1991."

This uptick is shown in figures from the US Equal Employment Opportunity Commission. At the end of the fiscal year ending 30 September 2018, it recovered almost US$70 million from employers for survivors of sexual harassment, up from US$47.5 million the previous year.

It's a similar picture in other countries too. In Australia, where sexual harassment cases can be brought at a federal or state level, the numbers are up in nearly every jurisdiction. In the year to September 2018, New South Wales saw the largest increase, with claims up by 39%, while claims in the federal arena rose by 19%.

In December 2018, a Bauer Media poll reported that 82% of New Zealand women have experienced either sexual violence or sexual harassment. These numbers do not appear to be reflected in claim volumes, but New Zealand only started collecting data on sexual harassment in the workplace in July 2018. A recent investigation suggests that sexual harassment complaints in the public sector have doubled between 2015 and 2018 and with the current environment more supportive of disclosure, it is expected that claim numbers will rise.

Ireland has also seen an increase in cases, with the 200 gender-related statutory claims it saw in 2016 rising steadily to 350 in 2017 and 318 in 2018. David Kennedy, Senior Associate at DAC Beachcroft in Dublin, says that while there was a spike in claims around the time of the #MeToo tweet, he believes other factors are affecting the figures. "There have been some high-profile cases in Ireland," he explains. "As it has become so newsworthy, it may be that employers are more prepared to settle than they were before."

The same is being seen in the UK. The introduction of tribunal fees in 2013 caused more than an 80% decline in claims but, following their abolition in 2017, the 2018 employment tribunal statistics showed that at certain points the number of sex discrimination claims was reaching the levels seen pre-2013. Louise Bloomfield, Partner at DAC Beachcroft in Leeds and Head of its Employment Practices Liability team, also notes that there has been a 56% increase in UK pregnancy discrimination claims, commenting that: "Employees appear to be much more confident in challenging what is seen as unacceptable behaviour in the workplace."

Even where #MeToo has had less of an effect, societies are finding themselves grappling with the same issues. Germany is a good example of this, as Bastian Finkel, Partner at Legalign firm BLD, explains: "The #MeToo movement isn't as big in Germany, but equal treatment has been a hot political, social and moral issue for the last few years. The 'No Means No' campaign has been running here for around five years."

UNDER PRESSURE

Regardless of which drivers are at play, expectations are that the number of claims will continue to rise according to Raisa Conchin, Partner at Legalign firm Wotton + Kearney in Brisbane. "These types of claims are still severely under-reported," she says, pointing to research released by the Australian Human Rights Commission in September 2018. This suggests that, although 71% of Australians have been sexually harassed at some point in their lives, just 17% of those who experienced sexual harassment at work in the last five years made a formal report or complaint.

Neither is the pressure likely to come off. As well as empowering more people to launch claims, the #MeToo movement has also resulted in the creation of organisations such as Time's Up in the US and NOW in Australia.

Sharing the goal of stamping out sexual harassment in the workplace, they also raise money to help individuals access legal support and counselling. For instance, within just two months, Time's Up had raised more than US$21 million and attracted nearly 800 lawyers prepared to offer their services on a voluntary basis.

Money is flowing from other sources as well. In New Zealand, the crowdfunding platform Give a Little, raised more than NZ$55,000 to defend a defamation claim by the country's Conservative Party founder Colin Craig against his former press secretary Rachel MacGregor. In a separate claim, Mr Craig was found to have sexually harassed Ms McGregor on multiple occasions. His defamation claim appears to have no prospect of success, but it may indicate a worrying trend of wealthy perpetrators using defamation actions to discourage or further persecute harassment victims.

Public focus has also expanded to include other groups that have suffered discrimination. In the US, the #UsToo movement was created to seek equality for individuals who had suffered racial discrimination. In Germany, football star Mesut Özil sparked the launch of the #MeTwo campaign (based on his having both a German and a Turkish identity) when he resigned from the national team citing racism and disrespect.

In this climate, Roer says that employers need to be aware about all aspects of the work environment. "It's not just a sexual harassment issue," she says. "Disparate treatment undermines the workplace. Social media can allow these issues to go viral, potentially undermining recruitment as well as increasing litigation exposure."

> *"It's not just a sexual harassment issue… Social media can allow these issues to go viral, potentially undermining recruitment as well as increasing litigation exposure."*
>
> Ricki Roer
> Wilson Elser

GOVERNMENT ACTION

Given the scale of the outcry, many governments have been forced to develop responses to the issue of sexual harassment. While some of this is still at the information gathering stage, others are already a long way down the path to introducing more robust legislation to protect individuals in the workplace.

This is the case in the US. Laws have been passed in states such as California and New York requiring employers to implement anti-harassment training and the Bringing an End to Harassment by Enhancing Accountability and Rejecting Discrimination in the Workplace Act (more commonly referred to as the BE HEARD in the Workplace Act) is set to overhaul harassment laws at a federal level. Roer says it will replace legislation that has been in place since 1964. "It will extend rights to a much broader class of people and make it easier to bring a case," she explains.

Significant change is also expected in Australia, where #MeToo has triggered the Human Rights Commission to launch the National Inquiry into Sexual Harassment in Australian Workplaces, led by Sex Discrimination Commissioner Kate Jenkins. "It's a world first," says Conchin. "The Commissioner is travelling around the country gathering information with a view to making legislative changes. It sends out a strong statement: the Australian Government wants to be seen as a world-leader in this space."

Anticipated changes include the potential extension of health and safety legislation to include a specific duty to protect from sexual harassment. By making it a regulatory issue, it would take some of the pressure off employees who don't want to go to court and would also mean both quasi-criminal fines for businesses and potentially jail sentences for officers who fail to protect their employees.

The UK also has some potentially significant changes on the horizon. In December 2018, the UK Government announced that it will be introducing a statutory Code of Practice on sexual harassment, which will be developed by the Equality and Human Rights Commission, and that it will also consult on a new legal duty on employers to prevent sexual harassment in the workplace. It is also likely that the Government will seek to increase the time limits for employees to bring sexual harassment claims in the UK employment tribunals. "Given the complexity of some sexual harassment issues and the impact upon all of those involved, quite often internal investigations and processes have not concluded before the legal time limit to bring a claim has expired," explains Bloomfield.

CHANGING ATTITUDES

While some countries' politicians are grappling with new legislation to combat sexual harassment in the workplace, others are finding that it feeds into a broader discussion on equality. The aim of the Irish Government's National Strategy for Women and Girls 2017-2020 is to create a better society for all by promoting action on women's equality.

For Kennedy, it is part of a broader shift in attitudes in Ireland. To illustrate this, he points to changes including the overturning of the abortion ban, the introduction of statutory paternity leave and the Gender Pay Gap Bill. "Ireland is at the forefront in protecting employees from discrimination, with powerful statutory remedies in place," he says. "But #MeToo has definitely provided an impetus for further change."

In some countries, the movement is even forcing change to the language. This is the case in Germany, where gender is an integral part of the language. Unsurprisingly, given the current focus on equality, this bias towards masculine genders is causing plenty of consternation. "It has triggered a huge political debate around whether the German language represents today's world," explains Christina Eckes, Partner at Legalign firm BLD. "It has made everyone stop and think about how you phrase sentences. Do we want our language to be in line with our position on diversity?"

WORKPLACE SHIFT

Employers are also finding themselves making changes to protect their employees from sexual harassment and discrimination in the workplace.

For some – such as the US states of California and New York – the requirement to take a more proactive approach to protecting employees has been mandated, with laws passed requiring employers to provide anti-harassment training and awareness. Others say it is more of a cultural shift. "We are seeing enhanced workplace policies and more training being put in place," says Kennedy. "The focus on sexual harassment means that more people will come forward, but these changes should help to reduce risk by improving working conditions. We have come a long way from the culture of silence in the workplace."

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>
> David Kennedy
> DAC Beachcroft

There is also considerable pressure on employers to make changes. As an example, after demands from employees and unions for better protection from sexual harassment, the American Hotel and Lodging Association, which includes major hotel chains including Hilton Worldwide and Marriott International, agreed to install safety devices such as panic buttons by 2020.

The thorny issue of non-disclosure and confidentiality clauses is also being explored in some countries. In particular, as part of her National Inquiry into Sexual Harassment in Australian Workplaces, the Commissioner has called on employers to voluntarily waive confidentiality clauses to encourage more submissions. As a result, 13 major employers have agreed to this on a limited basis. Conchin says this is meaningful. "It's a reflection of the support this issue has in Australia," she says. "That this is happening on a voluntary basis means that employers recognise the importance of the inquiry, potentially even against their own interests."

INSURANCE RESPONSE

Putting robust policies in place to prevent sexual harassment and other forms of discrimination is a positive step, but the rise in both awareness and the number of claims means that #MeToo is a significant insurance industry issue.

Employment practices liability policies offer cover for sexual harassment and discrimination claims brought against the organisation. Both Bloomfield and Kennedy have seen more litigation in this area in the UK and Ireland, with quantum rising. "More allegations of mental health injuries are being made in this area," says Kennedy. "Where an employee claims they have suffered psychological harm such as depression or post-traumatic stress disorder, it can be a difficult case to defend. Courts will often accept the medical evidence, even where a medico-legal doctor has only spent a short time assessing the claimant." As a result, while awards in Ireland have typically been around two years' salary, some recent cases have been as much as four.

Bloomfield notes that in the UK, damages and also settlement expectations are increasing, alongside an increase to injury to feelings awards up to a maximum of £44,000 and employment tribunals also being able to award up to £20,000 as aggravated damages.

The impact of these types of claim means that, in some countries, they've moved beyond employment practices liability and on to shareholders' claims, triggering directors' and officers' insurance. This is particularly the case where the board has failed to act on sexual harassment allegations or is shown to have turned a blind eye.

Other insurance policies are also being affected. Following a review into sexual harassment at New Zealand law firm Russell McVeagh, and evidence that nearly one third of female lawyers in New Zealand have experienced harassment, the New Zealand Law Society increased its attention on the issue. Its Standards Committee recently imposed a professional disciplinary fine of NZ$12,500 on a law firm partner for inappropriate behaviour at work social functions. This was significant, because the Standards Committee found he was providing regulated services at the time, which creates new exposures for professional indemnity insurers.

More positively, the increased focus on sexual harassment also appears to be driving take-up of insurance. Conchin explains: "We are seeing more employers taking out employment practices liability cover on a standalone basis or as a bolt-on to management liability cover. Where an organisation has an insurance broker, it's rapidly becoming the norm to have this cover."

Conchin is also heartened by the actions of insurers in this space. Many provide educational material to brokers and employers to help them ensure the right procedures such as training and policies are in place to prevent sexual harassment in the workplace. "Five years ago, this wasn't really on the agenda, but we now have insurers getting behind a campaign to raise awareness and lower risk," she adds. "It's very positive."

Contributors:

Christina Eckes
BLD, Cologne
christina.eckes@bld.de

Bastian Finkel
BLD, Cologne
bastian.finkel@bld.de

David Kennedy
DAC Beachcroft, Dublin
dkennedy@dacbeachcroft.com

Louise Bloomfield
DAC Beachcroft, Leeds
lbloomfield@dacbeachcroft.com

Ricki Roer
Wilson Elser, New York
ricki.roer@wilsonelser.com

Raisa Conchin
Wotton + Kearney, Brisbane
raisa.conchin@wottonkearney.com.au

Rebecca Scott
Wotton + Kearney, Auckland
rebecca.scott@wottonkearney.com

A TOUCH OF CLASS

Class actions have been a feature of the US legal system for years, designed, at least in theory, to help groups of individuals seek redress against major (and minor) corporations and organisations. There are now signs across the globe that this approach is gaining more traction, particularly in Europe.

A class action, class suit, or representative action – where one of the parties is a group of people who are represented collectively by a member of that group – originated in the US before spreading to Australia. Now pressure is building in Europe in the wake of cross-border scandals from VW's Dieselgate through to Petrobras, a bribery and corruption securities class action, which was one of the largest of all time.

THE US AND AUSTRALIA LEAD THE WAY

The US and Australian legal systems are structured for class actions to flourish as the use of contingency agreements shield plaintiffs from having to cover costs if a case should fail. In addition, plaintiff law firms and litigation funders can reap rich financial rewards of up to 35-45% of the damages awarded – particularly in shareholder related cases.

"We are seeing unprecedented activity in the Australian market in the class action environment," says Andrew Moore, Partner at Legalign firm Wotton + Kearney in Sydney. "This volatile environment is having a major impact on insurers' appetite when it comes to D&O insurance and premiums have been on the rise for some time."

There are, however, some signs in the US that the business community – boosted by the Trump administration's pro-business stance combined with changes to members of the Supreme Court – will increasingly look to avoid class actions. "The Supreme Court is showing a growing acceptance of agreements that waive class arbitration," says David Ross, Partner at Legalign firm Wilson Elser in Washington. "This is increasingly being utilised by the business community across all classes, including the consumer and employment area, to avoid class actions altogether. If someone sues you and tries to bring a potential class action, you can divert the case to arbitration and force the case to be administered on an individual basis instead of having to face a class action in either a court or arbitration."

In addition, the fees that law firms can earn are being trimmed, notes Paul S White, Partner at Wilson Elser in Los Angeles, as the courts – and the Department of Justice – are increasingly scrutinising settlements to find a way to ensure the class members themselves get a fair share of the damages.

These developments aside, the appetite for class actions shows no respite. New moves include attempts to obtain class certification around the #MeToo movement, although these have been hampered by the need for the injuries claimed to be unique to the individuals. There has also been increased activity over company websites for being inaccessible to the visually impaired and claims related to concussion in sport at the collegiate (and youth and professional) level.

In the securities areas, says Jim Thurston, Partner at Wilson Elser in Chicago, there has also been a major increase in the number of actions being filed. And filed, as opposed to being trialled, is the key word here as the cases underline the power of media pressure on large corporates. "Since 1995 there have been over 5,200 actions filed of which fewer than two dozen have actually gone all the way to trial," says Thurston. "In other words, you don't need a successful trial to get a settlement, and often, as soon as a claim is made, a company's insurer may be willing to open settlement discussions."

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> Jim Thurston
> Wilson Elser

Similarly in Australia, Patrick Boardman, Partner at Wotton + Kearney in Sydney, reports: "Securities class actions continue to be seen as 'good business' by plaintiff law firms and litigation funders alike. While the number of class actions is still small (compared to the US), those numbers are increasing, as is the number of competing class actions that require judicial determination on which is to proceed. Plaintiff-friendly laws (which have been the subject of the recent judicial commission's recommended amendment, but that are unlikely to be followed in the current political and business climate) are the 'bedrock' of the claims and have meant that to date all claims have been settled, with the average settlement increasing from $40m to $50m." With a D&O premium pool of approximately $300 million it does not take many class actions to cause market losses.

The market is changing, with brokers reporting a median increase in primary premiums of 89-122% and some insurers are either reducing capacity or pulling out of the market altogether. Boardman also notes: "The recent Banking Royal Commission has provided material for a variety of consumer class actions against financial institutions including responsible lending, add-on insurances and superannuation."

Fuelled by a desire to find new sources of income around the world, this experience is now driving powerful plaintiff law firms to make inroads in Europe.

THE MOVE TO EUROPE

Bastian Finkel, Partner at Legalign law firm BLD in Cologne, comments that there has been a sea-change in political mood: "There is a political desire to embrace some form of class action in Germany, in large part in the wake of the Volkswagen emissions scandal. German consumers feel mistreated – they have seen class actions and enormous payments to consumers in the US following class actions taken against a German company – whereas they have had nothing."

Compensatory collective redress is available in 19 member states, but in over half of them it is limited to specific sectors, mainly consumer claims. At the same time, nine countries do not provide the option to collectively claim compensation in mass harm situations. Only six member states have a proper alternative dispute mechanism focused on mass harm situations: Belgium, France, Italy, the Netherlands, Spain and the UK.

Germany has now introduced a sort-of class action regime, says Finkel, though this is only available for use by specific consumer not-for-profit agencies. "This is well short of the US or Australian system," he adds.

There is, however, a European Commission (EC) proposal that goes a step further, says Finkel. The Representative Action Directive is a part of the New Deal for Consumers, launched in April 2018 by the EC, which aims to ensure stronger consumer protection in the EU and follows in the wake of cross-border scandals.

It would allow group action against trader violations with a broad public impact in domestic and cross-border cases in different consumer areas such as data protection, financial services, travel and tourism, energy, telecommunications, environment and health. Crucially, however, under the draft rules representative action could only be brought by eligible entities, such as consumer organisations and certain independent bodies designated by member states. These should be non-profit and have no financial agreements with law firms.

"If the draft is passed as it is now," says Finkel, "we will have opened the door to a class action related to consumer protection – including data breach lawsuits."

> *"If the [EC proposal] is passed… we will have opened the door to a class action related to consumer protection – including data breach lawsuits."*
>
> Bastian Finkel
> BLD

Julie-Anne Binchy, Senior Associate at DAC Beachcroft in Dublin, adds that the Directive would, however, still face some hurdles in Ireland, "particularly in relation to third-party litigation funding, which is expressly permitted by the Directive, but which remains broadly unlawful in Ireland."

Recent decisions of the Irish Supreme Court upheld Ireland's position, "however," says Binchy, "these cases also highlighted the need for consideration to be given to potential legislative reform where the prohibition on third-party litigation funding arrangements may impede access to justice by a party that cannot otherwise afford costly litigation to protect or secure its rights. Practitioners in Ireland will be following developments in this area with interest."

The English legal system, although it recognises group litigation in restricted factual situations, has not traditionally permitted US-style class actions. It is, however, seeing increasing pressure to embrace more collective redress in the consumer area. The Consumer Rights Act 2015 introduced an opt-out collective redress regime for competition claims. This permits a claimant representative to bring an action on behalf of a group of individuals where this follows-on from an 'infringement decision' or 'an alleged infringement' of anti-competitive behaviour prohibited by the Competition Act 1998 or EU law.

The opt-out nature means that claimants are included in the group unless they expressly opt-out. However, claims can only proceed if they are certified as suitable by the Competition Appeal Tribunal (CAT) and, crucially, the person representing the class is a suitable representative. If these stringent eligibility criteria are met, a Collective Proceedings Order is issued and the class action may continue.

This has been used in the Mastercard case pursued by former Chief Ombudsman Walter Merricks, who alleges that for 16 years, 46 million people paid higher prices in shops than they should have because of high card fees and that they should all be awarded a share of £14 billion. The CAT threw out a representative claim but now the Court of Appeal has ordered it to look again.

A MATTER OF DATA

If there is one cross-border issue that illustrates the challenges facing society internationally, it is data privacy. Even the US, with its advanced class action regime, is struggling with this issue – as so-called injured parties are not actually injured in any way. Or are they? The US courts are split, especially in the data breach area. As the US Congress is not taking the lead on the issue, nothing will really change until the Supreme Court looks at it – and that, as Thurston comments, "could be some time away, as the court is usually at least five years behind any new trend."

This international move to recognise and enshrine an individual's data privacy rights – such as the European Union's General Data Protection Regulation (GDPR) – has been universally accompanied by a failure to establish any form of affordable process for redress. In the case of the EU, while the national regulatory bodies such as the Information Commissioner's Office in the UK can issue fines against firms, it has no say over individual compensation.

As Hans Allnutt, Partner at DAC Beachcroft in London, says: "In this context it is fair to say that class actions could serve a need – enabling individuals to have access to justice."

That said, the GDPR has opened the door for collective redress – but only if it is via a not-for-profit body such as human rights organisations and privacy watchdogs. No surprise then when campaigner Max Schrems launched the first challenge on day one of the GDPR last year, aimed at Google and Facebook's 'forced consent' via his hastily created not-for-profit NOYB.

Two other English cases also underline how data privacy could drive more class action style activity. Following supermarket chain WM Morrison being found liable for the actions of a former employee who stole staff pay data and published it on the internet, a group litigation order is being pursued, led by ten claimants – representing 5,500 of the total 100,000 staff affected – who were selected to articulate the different types of claims, damage and circumstance. However, Morrison has now been granted permission by the Supreme Court to appeal the judgment and, crucially, the critical issue of quantum of damages for distress has not yet been addressed.

According to Allnutt, the claim by Richard Lloyd against Google also failed when the High Court refused to allow a representative action – the court reinforcing the need to demonstrate damage resulting from data privacy breaches and not rely solely on a violation of a legal right in order to claim compensation.

However, perhaps more significantly, the case attracted noticeable litigation funding, says Allnutt, with the backers prepared to put up £15.5 million for costs and to buy insurance in case of loss of £12 million. The case did not progress, but it certainly shows the appetite.

This point is underlined by his colleague, Partner Graham Ludlam, who cites an increasing investment by US law firms and litigation funders in England and Wales – and Europe. They are not able to practice in England and Wales but are organising or providing funding themselves, along with their knowledge of how to force corporates to settle.

Sticking with Europe, the Netherlands is also proving to be a natural home for cross-border busting collective-redress claims, with the Petrobras case a major example. In 2018, it accepted jurisdiction over the international securities class action lawsuit against Petrobras Brasileiro – despite the offences taking place in a foreign jurisdiction.

In April 2019, its Government passed a new law declaring that representative entities, for example the Dutch claim foundation in Petrobras, will no longer be prohibited from claiming financial damages on behalf of their constituents. This will undoubtedly increase the attractiveness of the Dutch collective redress system in cross-border disputes. As Duncan Strachan, Partner at DAC Beachcroft in London, comments: "Only the Netherlands is anywhere close to the US system – although there is nowhere with a comprehensive opt-out system in Europe and no jurisdiction that recognises punitive damages in its own law to the extent available in the US."

In the final analysis, despite a noticeable shift in public and political opinion moving towards acceptance of the value of class actions – particularly in the wake of international corporate scandals and new data privacy rights – the legal, judicial and funding systems across Europe, and much of the world, continue to work against any major change. But with US plaintiff firms looking to grow outside their country, litigation funders eyeing potential returns, and international cross-border corporate scandals, attempts to force the issue will no doubt continue to increase.

Contributors:

Bastian Finkel
BLD, Cologne
bastian.finkel@bld.de

Julie-Anne Binchy
DAC Beachcroft, Dublin
jabinchy@dacbeachcroft.com

Hans Allnutt
DAC Beachcroft, London
hallnutt@dacbeachcroft.com

Graham Ludlam
DAC Beachcroft, London
gludlam@dacbeachcroft.com

Duncan Strachan
DAC Beachcroft, London
dstrachan@dacbeachcroft.com

Jim Thurston
Wilson Elser, Chicago
james.thurston@wilsonelser.com

Paul S White
Wilson Elser, Los Angeles
paul.white@wilsonelser.com

David Ross
Wilson Elser, Washington
david.ross@wilsonelser.com

Andrew Moore
Wotton + Kearney, Sydney
andrew.moore@wottonkearney.com.au

Patrick Boardman
Wotton + Kearney, Sydney
patrick.boardman@wottonkearney.com.au

KEY CONTACTS

David Kearney
Firm Chairman (Sydney)
T: +61 2 8273 9916
david.kearney@wottonkearney.com.au

Nick Lux
Partner (Melbourne)
T: +61 3 9604 7902
nick.lux@wottonkearney.com.au

Antony Holden
Managing Partner, New Zealand (Wellington)
T: +64 4 260 4286
antony.holden@wottonkearney.com

Andrew Moore
Partner (Sydney)
T: +61 2 8273 9943
andrew.moore@wottonkearney.com.au

Patrick Boardman
Partner (Sydney)
T: +61 2 8273 9941
patrick.boardman@wottonkearney.com.au

Rebecca Scott
Partner (Auckland)
T: + 64 9 377 1871
rebecca.scott@wottonkearney.com

Adam Chylek
Partner (Sydney)
T: +61 2 8273 9940
adam.chylek@wottonkearney.com.au

Charles Simon
Partner (Sydney)
T: +61 2 8273 9911
charles.simon@wottonkearney.com.au

Raisa Conchin
Partner (Brisbane)
T: +61 7 3236 8702
raisa.conchin@wottonkearney.com.au

Paul Spezza
Partner (Brisbane)
T: +61 7 3236 8701
paul.spezza@wottonkearney.com.au

Cain Jackson
Partner (Melbourne)
T: +61 3 9604 7901
cain.jackson@wottonkearney.com.au

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Microsite **Brochure**

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Delivering fresh thinking and strategic insight on hot topics, our global thought leadership will stimulate discussion and debate.

Jan '20

Predictions

Our international experts will look ahead at the opportunities and challenges the insurance market may face in the coming year.

May '20

Developments

Our guide will keep you abreast of key legislative, judicial and other developments, essential reading for managing risk and business planning.

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