BASIS OF CONTRACT CLAUSE: BALANCE BETWEEN LAW AND ETHICS

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Abstract

Section 151 of Insurance Act 1996 is enacted among others to resolve the issue of information obtained by agent while filling in proposal form on behalf of the insured. This issue is of great consequence since failure of the proposer to disclose material fact in the proposal form would enable the insurer to avoid the policy all together. However, the current trend or practices of insurer in inserting the basis of contract clause at the end of proposal forms has made the application of Section 151 with regard to insured duty of disclosure obsolete. This clause converts all the answers in the proposal form into warranties. All questions poses in the proposal form automatically become material facts even though some may in actual fact be immaterial. The effect of such clause is twofold. On one hand it helps to eliminate the necessity of considering whether such information is material or not, and whether there is disclosure of that material facts. On the other hand, the clause also seems to remove the responsibility of the insurer or agent to make sure that all material information had been obtained and recorded properly. By virtue of this clause, even if the proposer (insured) provides correct information but the insurer or agent mistakenly, negligently or purposely writes something else in the proposal form, the insurer is entitled to avoid the policy on the ground of non disclosure of material facts. This article explores the co-relations between law, ethics and practice in the insurance industry since the doctrine of ubberimae fidei set a contract of insurance apart from other types of commercial contracts. Thus, although it is a profit motivated industry, the insurer should not have a carte-blanche authority to include unfair terms which may result in the insured being denied compensation.

Introduction

Insurance has become an integral part of our modern way of life. The recent development in economy made insurance contract one of the most common types of contract available. Insurance industry in Malaysia is regulated by the Insurance Act 1996, Bank Negara Malaysia and to some extend the General Insurer Association Malaysia (PIAM) as well as the Life Insurance Association of Malaysia (LIAM) to ensure, among others, ethical practices and protection of policy holder's interest. However, despite being the one of the most regulated commercial industries, there are still areas in insurance especially with regard to the insurance contract where the industry's practices which may seem less desirable form the ethical perspective.

Unlike the conventional contract where the terms in the contract are agreed facts put into writing, insurance contract and proposal forms are usually a pre-prepared documents prepared by the insurer. The insurer basically set out all the terms in the documents and these terms are usually fixed and cannot be amended. It falls onto the insured to read the documents including the fine prints to understand the terms set out. In certain situations, the prints are so technical and small that it makes it very difficult for insured to read, let alone comprehend what was written. In consequence, insured sometimes did not understand what they are committing to. Thus allowing the insurer to use this 'ignorance' as a ground to cancel the contract or avoid liability. This paper sought to explore the practice of the insurance companies in inserting the basis of contract clause in their proposal form and to consider whether such practice is ethical, just and favorable to the insured. The effect of the clause is so significant that it is one of the most commonly used grounds for insurer to rescind the policy or avoid liability. This paper stand on the premise that the practice of inserting the clause need to be re-considered to ensure that the law and industry's practices balance the interest of both insurer and insured, reflect the needs of modern insurance industry and allow insurer as well as insured to know their rights.

Basis of Contract Clause

Basis of contract clause is a declaration usually found in every proposal form or insurance policy stating to the effect that the insured warrant the truth of the answers in the proposal form or the policy and that answers will be the basis of the whole contract (Mahmood, 1992). The declaration that the proposer had to sign contained the elements, namely, first that the answers to the insurer's questions were made the basis of the contract between the assured and the insurer, and secondly, that any untrue statement should render the insurance policy null and void. A typical basis of contract clause reads as follows:

> 1. I/we declare that the particulars in this proposal are true and correct and agree that they shall be the basis of the contract to be made between me/us and the Company
>
> 2. I warrant that the above statements made by me or on my behalf are true and complete and I agree that this proposal shall be the basis of the contract between me and the company (Singh,1994)

The effect of basis of contract clause is twofold. First, it creates a warranty on the correctness of information in the proposal form. By signing the declaration, insured converts all answers in the proposal form into warranties. Warranties are express terms in the contract which must be strictly and literally complied with by the party upon whom such term is imposed (Mahmood, 1992). Contrary to other types of contract, breach of warranties in insurance contract would enable the insurer to repudiate the policy. If a statement which the insured 'warranted' proved to be incorrect, the insurer is discharged from all liability under the policy and is entitled to reject all claims from the date of the breach. As such, if the

insured warranted the truthfulness of statement in the proposal form by signing the declaration, the whole proposal form became a warranty. Thus, any misstatement or omission in the proposal form will render it as breach of warranty entitling the insurer to repudiate the claim. This is regardless of materiality (Abdullah, 2004) or whether the statement induces the insurer to enter into the contract. Viscount Cave in its judgment in *Hambrough* v *Mutual Life Insurance Co of New York (1895) 72 L.T. p. 141* held that

> "upon the whole, it appears to me that both on principle and authority that the meaning and effect of the basis clause taken by itself, it that any breach of its promissory clauses, shall avoid the policy and that be the contract of the parties, it is fully established...that the question of materiality has not to be considered".

Secondly, basis of contract clause also creates contractual obligation for the insured. An insurance policy will incorporate the terms in the proposal form into the policy. As such, the performance of duty to ensure that all statement made in the proposal form correct became contractual. Non-compliance with the warranty in the proposal form which had been incorporated into contract would make the policy voidable at the option of the insurer. The inclusion of basis of contract clause and incorporation of proposal form into the policy integrate insured's answer into the contract although they are not set out in the policy. In order to create contractual obligation, the basis of contract clause must be incorporated into the policy. It is insufficient for it to appear in the proposal alone (Community Law Reform Program, 1983). Incorporation of proposal forms into policy usually read as:

> In consideration of You having applied to Us to insure Your Vehicle by a proposal and declaration which shall be the basis of this contract and having paid to Us the premium stated in the Policy Schedule in accordance with the laws of Malaysia, We will insure You against loss, damage or liability as described in this Policy occurring during the Period of Insurance subject to the terms, conditions, endorsements, clauses or warranties forming part of this policy. (Kumia Insurance, nda)

Once a statement has been made the basis of the contract, the question whether the statement was material to the risk undertaken is no longer an issue (Poh, 1992). They would automatically become material facts even though they may be in actual fact immaterial (Abdullah, 2004). The decision in *MacKay* v *London General Insurance Co Ltd (1935) 51 LIL Rep 201* stated that "since insured had warranted the truth of his statements, he could not recover under the policy for their accuracy was the basis of the contract". The principle is still applicable almost 60 years later where in *Dawsons* v *Bonnin (1922) 2 AC 413* the insured declared that the insured vehicle was garaged at 'No 46 Cardogan Street, Glasgow'. In fact, it was usually parked at a farm at the outskirt of the town. The proposal form contained a basis of contact clause and the policy stated 'the

proposal shall be the basis of the contract and be held as incorporated therein'. The vehicle was destroyed in a fire. It was held that although the misstatement was immaterial to case, it create a warranty. Thus, the insured could not recover. Similarly, the High Court in Malaysia in *Aetna Universal Insurance Sdn Bhd* v *Fan Foo May Wan* [2001] 1 MLJ 227 decided that there was a non-disclosure of fact in the proposal form by the insured. As there was basis of contract clause, the inaccurate answer amounted to breach of warranty. The contract of insurance was void and insurer was not liable to pay.

Duty of Disclosure

The significance of basis of clause contract stems from the duty of each contracting parties in insurance contract to disclose facts material to the contract. The principle of *uberrimae fidei* which is inherent in all insurance contracts set insurance contract apart from other kind of contract (Abdullah, 2004). Literally, *ubarrimae fidei* is defined as utmost good faith; hence, the most basic element in insurance contract is the requirement of all contracting parties to disclose all fact material to the risk to each other. Since certain facts regarding the risk to be insured are exclusively known only to one party, it is the duty of that party to disclose the fact to the other party so that the decision whether to accept the risk or the coverage would be given after having taken into account all relevant facts. The party in the dark will depend on the good faith of the party having the knowledge to impart such knowledge to him (Mahmood, 1992).

The duty of disclosure started in marine insurance where it was the common practice of the merchants to pass around a 'slip of paper' containing a brief description of the vessel and goods sought to insure to potential underwriter. The 'slip' will become the sole reference for the underwriter to decide whether to provide coverage and the premium to impose. As such, a symbiotic relationship where the insured depend on the underwriter to provide coverage and the underwriter trust the insured to provide full and accurate information regarding the risk sought to be insured. In the words of Lord Mansfield in *Carter* v *Boehm 97 ER 1162.*

> Insurance is a contract upon speculation. The special facts upon which the contingent chance is to be computed, lies most commonly in the knowledge of the insured only; the underwriter trust to his representation, and proceeds upon confidence that he does not keep back any circumstances in his knowledge, to mislead the underwriter into a belief that the circumstance does not exist, and to induce him to estimate the risqué as if it does not exist. The policy would equally be void against the underwriter is he conceal as if he insured a ship on her voyage which he privately knew to be arrived and an action would lie to recover the premium.

The duty of disclosure applies both to the insured and insurer. The duty that is placed on the contracting parties is not the duties to disclose all information, but only those which will have bearing on the risk to be undertaken or policy to be

bought (Poh, 1992). Insured have the responsibility to divulge to the insurer all fact material to the risk. Materiality of a fact depends on whether the disclosure of said fact would either influence the insurer whether to accept the risk or how much premium to be imposed. If the information is known to the insured to be relevant to the contract or that the information would influence the insurer with regard to acceptance and determination of premium, the information is said to be material and need to be disclosed. The Insurance Act 1996 incorporates the duty of disclosure under Section 150. The section reads:

> (1) Before a contract of insurance is entered into, a proposer shall disclose to the licensed insurer a matter that—
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> *(a)* he knows to be relevant to the decision of the licensed insurer on whether to accept the risk or not and the rates and terms to be applied; or
> *(b)* a reasonable person in the circumstances could be expected to know to be relevant.
>
> (2) The duty of disclosure does not require the disclosure of a matter that—
>
> *(a)* diminishes the risk to the licensed insurer;
> *(b)* is of common knowledge;
> *(c)* the licensed insurer knows or in the ordinary course of his business ought to know; or
> *(d)* in respect of which the licensed insurer has waived any requirement for disclosure.

Failure to satisfy this duty would enable the contract to be made void at the option of the party whom the disclosure should be made to. Thus entitling him to avoid liability or recover the premium.

Proposal form and the duty of disclosure

Proposal form is a document in where insurer would pose questions and insured to write down information relating to the subject matter to be insured. It has been the practice of insurer to require insured to fill in proposal form since is the most common and easiest method for insurer to obtain material information from the insured. It is however, not the only means in which material fact can be disclosed. The duty of disclosure is in no way been satisfied merely by filling in the proposal form since 'duty of disclosure exist independently of any proposal form'[1]. As long as there are still information material to the risk still not disclosed, the insured is still duty bound to disclose them (Singh, 1994). The proposer is not relieved of his duty merely by correctly answering the question therein[2]. There is

[1] *Asia Assurance Co Ltd v Tat Hong Plant Leasing Pte Ltd (1192) 1 CLJ 330* per Rajendran J; *Roselodge Ltd v Castle (1966) 2 Llyod's Rep*
[2] *United Malayan Insurance Co Ltd v Lee Yoon Heng (1964) MLJ 453*

presumption that matters dealt with in the proposal form is material, but there is no corresponding presumption that the matters not so dealt with are not material[3].

It has always been the practice among insurance agent to render their assistance to insured to fill in the proposal form on the insured behalf. Proposal form can be technical and lengthy. For those who are illiterate, unfamiliar with technical terms or just cannot be bothered to personally fill in the proposal form, the agent became their amanuensis. As such, the agent is considered as performing the task of filling in the proposal form for the insured, thus, assuming the capacity as agent to the insured instead of the insurer (Hussain, (1996). The case of *Newsholme Brothers* v *Road Transport and General Insurance Co (1929) 2 KB 356* laid down the principle that an agent filling in the proposal form for the insured is acting beyond his authority as agent to the insurer. The agent will be considered as agent to the insured, and any information obtained by him while filling in the proposal form cannot be imputed to the insurer. In short, any disclosure made to the agent while agent fill in the proposal form cannot be considered as disclosure to the insurer even though the well accepted principle in agency relationship states that act done by agent is act done by principal[4].

The issue of status of disclosure made while agent fill in proposal form for the insured was first tackled by the court in *Bawden* v *London, Edinburgh and Glasgow Assurance Co.* (1892) 2 QB 534. The Court of Appeal held that the insurer was liable under the policy even though the insured, a one-eyed man had signed a declaration saying that he has no physical infirmity which can render him peculiarly liable to accident. The ground being that the agent had knowledge of insured physical disability even before he assisted the insured to fill in the proposal form, making his knowledge the knowledge of the insurer.

The same argument was forwarded by the insured in *Newsholme*. The insurer repudiated a claim on the ground of non disclosure of material fact. The insured argued that although the proposal form was filled in by the agent, the true facts had been disclosed to the agent. When the dispute was referred to arbitrator, the arbitrator found that the agent had full disclosure of the fact and this knowledge can be imputed to the insurer. As such, the insurer was liable under the policy. The Court of Appeal however decided that the insurer can avoid liability on three grounds. The first being that, agent while filling proposal form had acted beyond his capacity as agent to the insurer since there is nothing to show that agent have authority to fill in proposal form on behalf of the insured. Since agent had acted in excess of his authority, any information obtained by him while doing so cannot be considered as information obtained by the insurer. Secondly, the proposer (insured) had signed the proposal form which contained basis of contract clause and declaration that all information given in the form was accurate. Thus, making any incorrect or insufficient information in the proposal form, the reason for the insurer to avoid the contract. Thirdly, parole evidence rule prohibit the admission of oral evidence to contradict the term in a written contract.

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[3] *March Cabaret Club & Casino Ltd* v *London Insurance Ltd (1975) 1 Llyod's Rep 169 p 176*

[4] S 182 Contract Act 1950. Notice given or obtained by an agent in the course of principal business bind the principal.

The judge distinguished *Newsholme* and *Bawden* saying that knowledge obtained by the agent in Newsholme was obtained while he was writing down the proposal form. The knowledge obtained by agent in Bawden however was obtained even before he assisted the insured to fill in the proposal form. As such, the agent in Bawden was still acting in his capacity as agent of the insurer when he came to know the insured disability. Thus whatever knowledge obtained by the agent can be imputed to the insurer.

Malaysian courts have also followed the principle in *Newsholme.* In *Mazzarol* v *United Oriental Assurance Sdn Bhd (Kuantan) (1983) 1 MLJ 328*, the Federal court upheld the High Court decision that there was a disclosure made to the agent. The agent assisted the insured to fill in proposal form. While doing so, insured informed the agent about the fact that the vessel was grounded. This however was not reflected in the proposal form. Federal Court distinguished the stages where agent negotiate the contract and assist insured in filling in proposal form. It was held that the agent must have acted in his capacity as agent when he received the information. Even though the agent filled in proposal form for the insured, he was acting within his capacity as agent to the insurer when he when to see the insured with the proposal form, inspect the vessel and tendering the form to his branch office.

The effect of *Newsholme* is even though the material facts was already disclosed to the agent, as long as the disclosure was done while agent filling in proposal form, that disclosure will not be considered as fulfillment of insured's duty of disclosure. This slight departure from the agency principle is of no great importance if the agent had accurately filled in the proposal form according to the information given by the insured. However, should the agent mistakenly, negligently or purposely write something else in the proposal form , omitted to write information disclosed by the insured and the proposal form contained basis of contract clause, the accurate disclosure made by the insured to the agent will not be considered as disclosure to the insurer. Thus, allowing the insurer to rescind the contract and avoid liability altogether on the ground of non-disclosure material facts.

Section 151 of Insurance Act 1996 is enacted among others to resolve the issue of information obtained by agent while filling in proposal form on behalf of the insured The words in section 151 was first seen in section 44A Insurance Amendment Act 1979 Act A465 of 197. The section reads:

> (1) A person who is authorized by a licensed insurer to be its insurance agent and who solicits or negotiates a contract of insurance in that capacity shall be deemed, for the purpose of the formation of the contract of insurance, to be the agent of the licensed insurer and the knowledge of that insurance agent shall be deemed to be the knowledge of the licensed insurer.

For the purpose of formation of contract, any information made known to the agent while in capacity as an agent will be deemed to be information made known

to the insurer. The knowledge of the agent will be imputed to the insurer. By virtue of this section, the problem created by applying *Newsholme* is resolved. Insurer cannot rescind the contract or avoid liability on the ground of non-disclosure merely because the information was disclosed to the agent while agent filling in proposal form.

Basis of Contract Clause: the Concerns

Despite the solution provided by section 151 of the Insurance Act 1996 with regard disclosure of material fact, the practice of inserting the basis of contract clause in proposal form created another problem concerning duty of disclosure. In cases where insured had disclosed the material facts to the agent and agent did not write it down in the proposal form (either intentional or unintentional) and the proposal form contain basis of contract clause, the insurer will still be able to avoid liability on the ground of non-disclosure. In *United Malayan Insurance Co Ltd* v *Lee Yoon Heng(1964) MLJ 457*, the court rejected insured argument that there was disclosure of material facts; agent knew the fact that the insured vehicle was to be used for commercial purpose when he was assisting insured to fill in the proposal form. In allowing the insurer's application to declare a policy as void on the ground of non-disclosure of facts Gill J emphasis the fact that insured had signed at the foot of the proposal form, a declaration that the particulars therein are true and would be the basis of the contract. When insured signed a proposal form that contain basis of contract clause, he would have been taken as to have read and agreed to its content.[5]

It is humbly submitted that although the insertion of basis of contract clause in insurance contract is valid, it is however objectionable from ethical point of view. The insertion of such clause creates an imbalance between the two contracting parties. The insurer has total control over the wordings in the proposal form and policy since both of these documents are standard documents prepared by the insurer. The insured have no say in the proposal or policy wordings. It clearly goes against the very basic definition of contract; that is the documentation and manifestation of meetings of minds of the contracting parties. As such, when only one party has the control over the wordings the clause, there is no meeting of minds. There is also no equal bargaining power given to the insured. Although insured have the option whether to buy the policy or not, this option became superfluous since all proposal form contain this clause. At the end of the day, insured still have to accept the clause and bear the consequences.

Secondly, if the insured does not understand what the effect of the declaration in the basis of contract clause which he signed, he will be trapped by what he signed. In an Australian case of *Bazouni* v. *Sun Alliance Insurance Limited 17 March 1981, Supreme Court of New South Wales,* a fire damaged a shop. The owner was a middle-aged Lebanese lady who had lived in Australia for twelve years at the time of the hearing. In 1973 she bought a shop with an adjacent dwelling in a Sydney suburb. In 1977 a burglary occurred at the premises and the insurer paid

[5] *National Insurance Co v Joseph* (1973) 2 MLJ 195

under the relevant policy a sum of $500. In the same year that insurer decided to discontinue the insurance and advised the owner accordingly. The owner was unable at any time, including the time of the hearing, to speak or read English to any extent. After withdrawal of the insurance in 1977 the owner and her daughter went to the office of another insurance company and completed a proposal for fire insurance. At the foot of the proposal form was a form of declaration in the following terms: "No insurer has declined to insure me, refused renewal or cancelled any policy of insurance" The owner signed and made the declaration in the proposal which became the basis of this contract. The owner did not make any disclosure to the new insurer at any stage of the withdrawal of cover by the previous insurer. A fire occurred on the premises almost two years later. The owner made a claim upon but rejected on the ground of non-disclosure. In the Supreme Court Mr. Justice Yeldham held that there had been a breach on the part of the owner of her common law duty to disclose material facts. Although the court's decision was that breach of the common law duty was sufficient to determine the matter, the judge also said that even if section 18(1) could be invoked he "would not be prepared to hold that the insurer was not prejudiced by the relevant non-disclosure". As well as the common law duty of disclosure, this case presented a question arising from the incorporation into the insurance contract of the provisions of the proposal,

At the same time there is also possibility of it being abused. Basis clause is a powerful weapon in the hands of the insurer and this privilege may often be abused when an insurer seeks to rely on statements which are immaterial to the risk insured to avoid liability under the policy (Poh, 1992). The materiality of fact which is the foundation of duty of disclosure no longer needs to be considered in order to cancel the contract. It does seems like the insurer is allowed to create a loop hole in the contract in which on they can utilize in order to cancel the policy. Swift J lamented:

> If he had stated the truth in its full detail, this insurance company would have jumped at receiving his premium. They would never have dreamed of rejecting his application, but after they have given him the policy and after the accident have happened and the liability is incurred, they seize upon these inaccuracies in the proposal form in order to repudiate their liability. I am extremely sorry for the plaintiff in this case. I think he has been very badly treated, shockingly badly treated. They have taken his premium. They have not been in the least bit misled by the answers which he has made. They would never have refused to take his money; they would never have refused him his policy if they have known everything which they know now. But they have seized upon this opportunity in order to turn him down and leave him without any indemnity for the liability which he has incurred. But I cannot help the position. Sorry as I am for him there is nothing that I can do to help him. The law is quite plain.

Recommendations

Hasson, (1971) wrote 'no meaningful reform in insurance law can be achieve without complete overhaul of the law which has develop around the 'basis of contract' clause in insurance litigation.' (Singh,1994). The easiest way to ensure that the insured's interest is protected is by abolishing the whole clause from insurance policy. By applying this method, there will be no issue of abuse of basis of contract clause to avoid liability. Insurer will have to go back to the basic principle of duty of disclosure that is, insurer is allowed to cancel a policy or avoid liability only when there is non disclosure of material fact. To succeed in this ground, insurer will have to prove that the fact not disclosed is material to the risk and that the insured had failed to disclose them. Failure to disclose fact or incorrect statement in the proposal form will not entitle the insurer to avoid liability or cancel the policy if the information not disclosed or incorrect is immaterial to the contract. In cases involving incorrect statement or information in the proposal form, the statement or information should be treated as a representation. As mere representation, it will not enable the insurer to rescind the policy or deny liability merely on the basis or incorrect statement or information. As long as there is no fraudulent intention, the incorrect statement can only be used as a ground to rescind contract or avoid liability if the statement or information is material.

It is also possible for us to enact a section which can minimize the harsh effect of basis of contract clause. The Insurance Act 1996 is not alien to the issue of controlling the outcome of inaccurate or false statement in proposal form. Section 147 reads:

> A licensed life insurer shall not dispute the validity of a life policy after the expiry of two years from the date on which it was effected on the ground that a statement made or omitted to be made in the proposal for the insurance or in the report of a doctor, referee or other person, or in a document leading to the issue of the life policy, was inaccurate or false or misleading unless the licensed life insurer show that the statement was on a material matter or suppressed a material fact and that it was fraudulently made or omitted to be made by the policy owner.

The section give a 'cooling of period' in which insurer can rescind a contract or avoid liability on the ground of non disclosure of material fact by merely showing that the information given in proposal forms or reports are misleading or false. Beyond this period, the incorrectness of the information is no longer material and cannot be use as a ground to cancel a policy or deny liability. Insurer need to show that the incorrect facts are made fraudulently by the insured in order to enable the insurer to use it as a ground to rescind the policy. Although the information given in the proposal form is incorrect, they became warranty only within the stipulated period. After the period ended, the information ceased to be a warranty and insurer would need to fraudulent intention. Nevertheless the extension of this section onto other types of insurance could be difficult since the

period of coverage is usually one year. The 'cooling off period' would be very short and would not allow sufficient time for insurer to rescind the contract. Due to this, it is prudent to take a look at a provision in Australia where the application of the section clearly intended to modify the Common Law with regard to insurance contracts other then life insurance (Law Reform Committee of New South Wales, 1983). Section 25 of Instrument Act 1958 (Victoria) reads;

> No contract of insurance (other then a contract of life insurance) shall be avoided by reason only of any incorrect statement made by the proponent in any proposal or other document on the faith of which such contract was entered into revived or renewed by the insurer unless the statement so made was fraudulently untrue or material in relation to the risk of the insurer under the contract.

This section limits the effect of basis of contract clause. The clause will only be applicable if the incorrect statement was made with fraudulent intention. If the incorrect statement was made honestly, by mistake or negligent act of the agent, the insurer will not be entitled to rescind the policy. While not denying the insure their right to ensure that the insured gave correct statement in the proposal form, it also made it a point that only statement made with fraudulent intention will give rise to right to cancel policy (Law Reform Commission of Western Australia,).

It is also submitted that if insurer insist on retaining the basis of contract clause as part of the proposal form, they should also take an active role in ensuring that the material information are disclosed. It is unfair to penalize the insured when they did not know whether a fact is material and need to be disclosed. This is due to the fact that the insurer is in better position to know whether the information given in the proposal form sufficient enough to influence them in determining whether to accept the risk and how much premium to be imposed. If the information is insufficient or doubtful, insurer should have an obligation to ask question relevant to the facts in order to extract the required information out of the available information voluntarily given by the insured in the proposal form (Turpin, 2006). By doing this, insurer not only be able to extract material information from the insured, the also will be able to educate or warn the insured on the need for material fact to be disclosed. After all enquiries completed and insured signed the declaration in the basis of contract clause, the information given proven to be false or insufficient, insurer will be have the right to rescind the policy or avoid liability.

Conclusion

It is worthy to note that many writers and legal scholars had commented on the unethical effect of basis of contract clause. Not only it is undesirable from the view point of the insured, it also objectionable from the view of law of contract. This is clearly the case of practice does not always makes perfect. In order to make the practices insurance company 'perfect', the insertion of basis of contract clause need to be reconsidered. The Law Reform Committee in Australia had already made several proposals to reform this practice solely on the basis of its

unjust effect to the insured. In Malaysia however, such move is yet to be seen. It is hoped that the insurance industry will take cognizance of ethical issue of the clause and try to find a balance between law, practice and ethics.

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