RFIB

Broker's Responsibility for Insurance Security

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Introduction

Under English Law a broker is "an agent acting for reward"

- Duty of such skill, care and diligence
- Servant of his principal, no matter how big the broker may be

Core duty of the Insurance or Reinsurance Broker is to:

- Place the risk
- Accept the client premium
- Issue a cover note
- Effects payment of the claim to the client

The Broker is NOT the source of the claims money

- Most disputes concern matters of interpretation of underwriting information supplied by or to the broker.
- Disputes also arise if the Insurer or Reinsurer is under financial pressure, sometimes becoming insolvent, and cannot pay the claims.
- Disagreements are often resolved by private arbitration or a public court case.

Disputes can often get very complex and to complicate further there are relatively few court cases involving Reinsurance brokers……..

Berriman & Ors v Rose Thomson Young (Underwriting) Ltd; 19th March 1996

One of the most prominent reinsurance cases was Berriman & Ors v Rose Thomson Young (Underwriting) Ltd case in the Commercial Court 19th March 1996.

This was a very complicated case in which the assured, who were Lloyd's names, were suing their own underwriting managers as well as the brokers - the judge's summing up ran to 81 pages.

Two legal points were emphasized by the judge in this case:

1. **Firstly – a broker has a duty to establish that the security put before a client is reasonably appropriate to the type of business written, for example excess of loss reinsurance or long tail liability or aviation etc .**

2. **Secondly – the client (the reinsured) is under an obligation to satisfy himself that the security offered by the broker is appropriate for the purpose for which he intends to use it.**

This was an important case in the market because the Lloyd's names – i.e. the investors or shareholders – were attempting to sue the underwriting manager due to a large number of losses, and difficulties in effecting recovery from reinsurance companies with doubtful security, which had been used by the broker.

Although doubtful security had been used, the judge did not find against the broker in this case, because it was in his view up to the professional underwriter to satisfy himself that the reinsurance security was suitable for his class of business. The broker in question operated a security committee and a security list, but would have sought the agreement of the underwriter to place the business with that security.

Bates & Ors v. Robert Barrow Ltd & Ors; 8th December 1994

In Bates & Ors v. Robert Barrow Ltd & Ors., a broker was accused of acting irresponsibly in placing stop loss reinsurances of Lloyd's underwriters with a Finnish company Kansa which the Lloyd's broker knew not to be legally registered to accept business in the UK.

Four underwriting agencies were involved in this case accused of neglect of a duty of care towards their names (investors)

The broker operated a binding authority of a reinsurer which he knew not to be licensed to write insurance or reinsurance business in the UK, and placed reinsurance of Lloyd's names with the company.

In the court judgment the judge pointed out that the broker ought to have taken legal advice, and did not, but nevertheless found that the broker was not liable to pay damages to the Reinsured's because he could not have imagined that the reinsurer Kansa would rely on the illegality of its own actions as a reason for refusing to pay out under the reinsurances.

The judge therefore found that the broker was not guilty of a breach of duty - this appears to be illogical, but the judge held that most brokers at the time would not have expected Kansa to rely on the illegality of its acceptance in declining claim settlements. He held the claim that the broker had breached his duty of care.

However, when considering the insurance market at the time the cover was placed (early 1980s) the judge did not think that a broker would have contemplated a reputable reinsurer relying on its own illegality to defeat a claim and therefore held that the loss was too remote for damages against the broker to be recoverable.

- **This shows that the Law does not always appear to follow logic**
- **In this case it was highlighted that by judgment in a precedent case, on which this case rested, the Court might be encouraging reinsurers to pay up under contracts that were legally void – which is a different legal question.**

Youell v Bland Welch &Co Ltd (No 2) Commercial Court 6th April 1990

This case involved reinsurance but with a very strange twist.

In this case the broker placed a reinsurance which expired before the primary insurance and the judge held that the reinsured had a duty to check the appropriateness of his reinsurance cover to the underlying risk and that the reinsured (underwriting manager) had failed in this duty, even though the broker was also negligent.

- **He therefore found the brokers only 80% to blame and liable.**

This case was not strictly about reinsurer security, but is interesting in illustrating the attitude of the courts towards the reinsured

- **The Courts tend to expect a high level of responsibility to be taken by companies buying reinsurance (or insurance) through brokers, and only find decisively against the brokers in cases where the broker was advising members of the public rather than fellow professionals or corporate entities.**

Osman v Moss (J.Ralph); 10th February 1970

This motor insurance case involved a broker who had recommended to a client an insurance company which was known to be in financial difficulties.

Here the judge had no hesitation in finding against the broker, because he had been negligent in his recommendation, and grossly negligent because instead of warning his client, he simply wrote to him recommending that he insure elsewhere.

Texas Homecare v Royal Bank of Canada Trust; 25th January 1996

This case shows how complicated insurance matters can become.

The broker in question had arranged the marketing of an extensive consumer insurance scheme via a major retailer with stores throughout the UK on the basis that the security for the scheme would be “AA status or equivalent”.

- **The security used was inferior and the insurance company went into liquidation.**

Texas Homecare Ltd v Royal Bank of Canada Trust Co (Jersey) and Ors; 25 January 1996

In this case the judge first of all ruled that the concept "AA status or equivalent" was not so vague as to have no legal meaning, and that no reasonable broker would have described an ISI rating of "A" as being equivalent to a Standard & Poors rating of AA.

- **The judge then found against the broker because the broker had knowledge that the quality of security was bound to place the other contracting parties at risk of financial loss in a large retail scheme of this nature.**

In fact this legal judgment was much more complicated than I have stated because there were more than one company involved in the marketing arrangement, with contractual arrangements which made reference to the "AA" rating, and therefore damages were awarded not only against the brokers.

Bell v Lothiansure Ltd
1st February 1991 – Scottish Law

This case involved the most unusual situation of a claim under a professional indemnity policy in which there was an exclusion of loss arising from "the insolvency of any insurance company".

The underlying cause of loss involved fraud, insofar as the insurer security offered (fraudulently) by the broker was already insolvent before the risk commenced.

The judge held that the proximate cause of insured's loss was the fraud, and not the insolvency.

It was therefore held that the professional indemnity policy had to respond to claims against the broker for negligence because the exclusion of insolvency as a proximate cause could not be invoked by the professional indemnity insurers.

- **The underlying conclusion of the court was the broker was held responsible for his negligent (fraudulent) actions.**

Arbitration

Many cases have not gone to Court, either because the dispute was settled out of court, or because the parties went to private arbitration. We know that there have been many arbitration cases involving brokers, but we think not many involving reinsurance security .

Since arbitration cases are private, the details are not available for publication.

However, we are aware of some cases involving very large sums – tens of millions of US Dollars – when awards were made against London brokers for negligence. However, we are not aware of any cases specifically involving the use of security by brokers.

One of the reasons for this is that in the UK, there are publicly funded arrangements for cases where a motor insurer becomes insolvent and clients face the danger of suffering financial loss.

Added to this, there have been very few high profile failures of insurers in the UK in the last 40 years, and only one in the last 20 years, so that very few cases against brokers for the use of security in retail insurance can have happened.

There have certainly been a number of failures of reinsurers, and no doubt there were questions surrounding the placement arrangements through brokers. However, here again it must be emphasised that in such cases, it is the practice of the market for Reinsureds and reinsurers to arrange for set off accounting between themselves, bypassing the brokers.

When it comes to reinsurance, we have seen that the English Courts have tended to demand a rather high standard from the ceding companies in their choice of security offered by the brokers, and have tended not to hold judgments wholly, or solely, against the brokers where there was some contributory negligence on the part of brokers.