2. INSURANCE INTERMEDIARIES
by Ray Hodgin, Senior Lecturer in Law, Birmingham University

As this is the first occasion that my topic has appeared in the update slot, I thought that I might start with the case of *Tickel v. Short.* This was decided by the Lord Chancellor in March 1750.

However, I calculate that if I do start with that case I will only reach the case of *Wing v. Harvey* in 1854 by the end of my 20 minutes.

I will start then by drawing two cases together on what may appear to be rather a low key point in terms of legal principle, but what is, however, I believe, an important reflection on how intermediaries carry on their day-to-day business.

In *Hadenfayre v. British National Ins & others* decided by the Commercial Court in 1984. ([1984] 2 Lloyd's Rep 393) the defendant insurers gave binding authority to write contingency insurance on their behalf to Burrows (Underwriting Managers) Ltd.

The plaintiffs were property developers in the North of England. They sold property valued at £275,000 and wanted to insure against the possible default in payment by the buyers.

They put the business in the hands of their brokers who in turn contacted Burrows who duly arranged cover on the facts presented to them.

The conditions of sale changed. The plaintiff informed their brokers who then 'phoned Burrows to notify the changes.

At least that is what they said they did because Burrows denied they ever received such a call.

A loss occurred and the claim was rejected.

The defence was non-disclosure in that the changed circumstances had not been notified. The plaintiffs argued that the call had indeed been made.

In the era of great technological advances, and of vast sums being spent on

modernising businesses, we come down to a situation of whether or not a 'phone call was made. I wonder just how often that problem arises?

Mr Justice Lloyd held that it was made and the insurers were liable to the insured.

It is clearly difficult for the court to come to a decision when the two sides offer totally conflicting evidence.

The judge was influenced by the fact that the plaintiff's brokers reported back to their clients that the change had been notified, *and* the brokers had written to their London office a week after the telephone call informing them of the change. "It was not quite contemporary. But it was as near contemporary as makes no difference." (Lloyd J.)

It was never alleged that the telephone call had ellicited more than either an "O.K.", or possibly "I will tell him".

Informality has often been heralded as one of the great hallmarks of the British insurance industry - so be it!

I now join *Hadenfayre* to *Vesta v. Butcher* [1988] 1 Lloyd's Rep 19.

This case has been mentioned in the previous two years' updates, under different headings, and as the appeal is ongoing I can only assume that it will reappear again next year in another update slot such is its popularity with everyone.

I am only concerned of course with the intermediaries' role and not with the conflict of laws point.

You will recall that the Norwegian insurers were told by their clients that the 24 hr watch clause on the fish farm was unacceptable to them.

The Norwegian insurers informed the London brokers by telephone and asked them to seek an alteration in the reinsurance wording.

This was not done. The Norwegian insurers paid out on a claim by their clients and sought to claim from the reinsurers and in the alternative against the London brokers for breach of duty in not attempting to carry out their instructions.

Both the Conmmercial Court and the Court of Appeal held that the reinsurers were liable.

Having held the reinsurers liable, the broker's breach of duty was not causative of any losses to the Norwegian insurers.

However if loss had been suffered by the Norwegians, then Mr Justice Hobhouse held the London brokers 25% to blame, and the Norwegian insurers 75%.

This apportionment I find difficult to understand.

The Court of Appeal rejected the broker's appeal against liability, and also rejected Vesta's appeal that the apportionment was wholly unreasonable.

While Lord Justice O'Connor was of the view that he did not think that there were sufficient grounds for interfering with the apportionment of fault, Lord Justice Neill preferred to say nothing as to the actual proportions fixed by the judge, with which he felt, the Court of Appeal could not in any event interfere.

Sir Roger Ormrod however said that the ratio 25:75 surprised him somewhat, but added that he did not think there was sufficient material to justify the Court of Appeal in interfering with the assessment.

Why 25:75 ratio? The Commercial Court had found that the telephone call was made,
that it was called for action,
that no action was taken.
Why?

> Because the broker forgot.
> The broker should himself or through another employee have promptly contacted the lead underwriter and communicated to Vesta the underwriter's reaction. Something acceptable to both sides would have been worked out.

These are the findings of the judge; why then only 25% liability against the brokers?

He accepted their argument that Vesta were guilty of negligence in not following up on their original request to have the cover changed.

He therefore acepted that they displayed, in his words, "a high degree of blame-worthiness."

He went on to say that the brokers should have made and kept a note of the telephone call. Its importance was admitted. Their failure was as much a continuing one as Vesta's - although LESS grave.

Conclusion In both Hadenfayre and Vesta we have examples of poor communications leading to financial losses.

It is interesting to note that the Financial Services Act 1986, and especially the FIMBRA Rulebook are weighed down with minutiae of office practice. The great chorus of protest presently mounted by all parts of the industry against the Act, might just reflect that in Hadenfayre and Vesta the industry could not even cope with telephone instructions in an efficient way.

Unfortunately, there is very little in the Rulebook that would cure the simple problems posed in Hadenfayre and Vesta.

6. I would like to turn to a different topic, that of Umbrella Agreements at Lloyd's. The working of such an agreement is illustrated by the decision in *Johns v. Kelly* [1986] 1 Lloyd's Rep 468.

Hoover PLC wanted to offer extended warranty cover on their products. They contacted insurance consultants who in turn suggested that Multi Guarantee set up and manage the scheme. Multi Guarantee instructed non-Lloyd's brokers to place the risk. Their decision was to place the business at Lloyd's, and in order to do so they negotiated an umbrella agreement with Lloyd's brokers. The non-Lloyd's brokers were to pay as commission, to the Lloyd's brokers, 5% of the premium income due to the underwriters. The other details of the agreement called for the non-Lloyd's broker's principal to be employed by the Lloyd's brokers, but the former were to reimburse his salary to the latter. The non-Lloyd's brokers were also to pay any increase in the Lloyd's broker's professional indemnity premium caused by employing the principal of the non-Lloyd's broker. The non-Lloyd's broker was also bound to indemnify the Lloyd's broker for all liabilities in tort that might arise due to the clients of the non-Lloyd's broker suing the Lloyd's broker.

The principal placed business at Lloyd's using the Lloyd's broker's slips. Hoover PLC were the named insured and the maximum total cover was £1/2m.

Both points were contrary to Hoover's instructions. They wanted the individual customers to be the named insured and they wanted no ceiling on cover.

Many claims arose under the extended warranties. At that point the errors in cover were detected, the action was compromised, and £1m was paid to Hoover. The Lloyd's brokers contributed £20,000 to this sum and then sought to reclaim this from their professional indemnity insurers. These insurers defended the claim, arguing (a)

the claim was not within the policy wording, and (b) there had been serious misrepresentations by the Lloyd's brokers in not disclosing that the non-Lloyd's broker was an associate company of the Lloyd's broker and (c) that there was a non-disclosure in not divulging the existence of the umbrella arrangement.

The Commercial Court (Bingham J.) *held* (a) the non-Lloyd's broker was not an associate company of the Lloyd's broker; (b) the Lloyd's brokers were negligent regarding Hoover's requirements in not exercising control over the non-Lloyd's broker's principal and that the negligence was covered by their professional indemnity policy; (c) the relationship between the brokers did not mean that the principal of the non-Lloyd's broker was an employee of the Lloyd's broker, but it was merely a matter of form to satisfy the Committee of Lloyd's; (d) the existence of an umbrella agreement was clearly a matter that would influence the judgement of a prudent insurer and the Lloyd's broker should have disclosed this fact. Thus, (e) the professional indemnity insurers were entitled to avoid liability because of the breach of the failure in (d) above.

7. An investigation into the use of umbrella agreements was set in motion at Lloyd's. This found that at least 125 such agreements were in existence at the time of the enquiry. The outcome is the Lloyd's Byelaw No. 6 of 1988 - Umbrella Arrangements, that came into effect on 1 August 1988.

The main effects are:-

(a) An umbrella agreement between a Lloyd's Broker and non-Lloyd's Broker must be registered at Lloyd's before any business is transacted with an underwriter.
When an agreement is registered it is valid for 3 yrs, but extensions will be possible.

(b) (i) The non-Lloyd's broker must be enrolled or registered under the Insurance Brokers (Registration) Act 1977.

(ii) He must intend to apply for registration as a Lloyd's Broker within the 3 yr period of the umbrella arrangement and he must appear capable of meeting the various requirements of such registration.

(iii) Lloyd's Brokers must give an undertaking to Council adequately to supervise the conduct of the non-Lloyd's Broker.

(iv) There will be no registration of two concurrent umbrella arrangements with same non-Lloyd's Broker.

(v) The non-Lloyd's Broker must not be a managing agent or associated with a managing agent.

(c) Every umbrella agreement must be submitted to Council annually by the Lloyd's Broker.

(d) The Lloyd's Broker must be directly responsible to the underwriter for the payment of premiums unless different arrangements exist between the Lloyd's Broker and the underwriter.

(e) If the non-Lloyd's Broker fails to discharge his obligations to his client then the Lloyd's Broker must take over the responsibility of servicing the business.

(f) The non-Lloyd's Broker acting under the authority of a registered umbrella agreement must not represent that he is a Lloyd's Broker.

(g) Slips must clearly indicate that business is being conducted under an umbrella arrangement.

(h) The Council may dictate the conditions and requirements of the PI cover that the non-Lloyd's Broker must have if they are parties to umbrella agreements. Both Lloyd's and non-Lloyd's brokers must disclose to their PI insurers the existence of the umbrella agreement.

(i) The Lloyd's Broker must see that the amount of net brokerage derived from its umbrella agreements does not exceed 25% of all its net brokerage for the year.

8. Finally, I would like very briefly to look to the other side of the world.

In 1984 Australia passed two major Acts, the Insurance Contract Act and the Insurance (Agents and Brokers) Act 1984. (Admittedly the latter Act was partly based on our IB(R) Act 1977).
But This year s.12 of the Insurance (Agents/Brokers) Act came into force.

This section states that, apart from a general insurance broker and a life insurance broker, (special categories created by the 1984 Act) every insurance intermediary shall be deemed to be the agent of the Insurer and *not* of the insured.

It will be recalled that the Law Reform Committee made similar suggestions for changes in our law in 1957. Nothing happened.

The Law Commission Report 1980 reinforced the 1957 recommendations - nothing has happened.

In a few lines of legislation Australia has removed the effects of those blots on insurance intermediary law made by the Court of Appeal in 1929 with *Newsholme v. Road Transport and General Insurance.*

My worry is that while I believe there is little chance in this country of legislative reform in general insurance law, what chances may have existed will have been well and truly scuppered by the nightmares caused by the Financial Services Act 1986 and the lingering after-effect that it will have for general insurance.

3. REINSURANCE LAW
by Stephen Ruttle, Barrister

1. There have been a number of recent decisions of considerable importance to the reinsurance market. I shall concentrate on two of these cases:

(a) *Boden v. Hussey* (1988) 1 Ll. R. 84 (Adrian Hamilton Q.C.): (1988) 1 Ll. R. 423 (Court of Appeal); This was the *Air India* reinsurance case which in essence concerned the definition of "loss" in a standard excess of loss reinsurance wording.

(b) *Home & Overseas Insurance Co. Limited v. Mentor Insurnace Co. (UK) Limited* Financial Times, 10th August 1988, Hirst J.

There are two important matters discussed in this decision.

(i) Whether on a standard excess of loss reinsurance wording payment by the reassured is a condition precedent of the reassured's right to recover against the reinsurer.

(ii) The effect of the "honourable engagement" provision in a standard Arbitration clause in a Reinsurance Treaty wording.