Lunchtime Talk: Friday 19 April 1991
"THE WINDY SIDE OF THE LAW"
by Alan Bridgewater
Chief Executive, Norwich Union Group

Introduction

I have taken my inspiration from the immortal bard (Twelfth Night Act II Scene IV) and I hope to develop this theme by offering you some personal observations on the way in which the law both contributes to and, I believe, inhibits the successful development of the insurance industry. I stand before you not as a scholar or an expert practitioner in the intricacies of insurance law but as the chief executive of one of the largest insurance groups in the country. A group which has rooted in its history a long tradition of conducting its affairs in an ethical and law abiding fashion. In that situation and others, rather than being protected or sheltered I sense we are exposed to the windy blast! Yet, along with our colleagues in the industry, with whom we are more than happy to compete in the high street, we have had to grapple with and take on board an increasing level of regulation and control. I am sure that I am not alone amongst my fellow chief executives in expressing some concern over the ever escalating cost of compliance and perhaps the regulators would do well to remember, from time to time, that, as with all legal measures aimed at protecting the consumer, it is the consumer who ultimately bears the price either in higher premiums, lower investment returns or probably both.

The Financial Services Regime

I am of course referring here to the Financial Services Act 1986 and the plethora of regulatory organisations which have been established to control the different elements of the investment industry. Some of you may recall that the origins of the Act go back in part to the reports of Professor Jim Gower (recently appointed honorary Queens Counsel) in the mid 1980s, although if we look back in history, I understand that at the time of Edward I there was a statute which required brokers to be licensed by the Lord Mayor and Alderman of the City of London and as a condition of the licence they were required among other things to make an oath of good behaviour.

Well, we now have had the Financial Services Act in force for 3 years or, to be precise, as I know you lawyers like to be, we are 10 days away from the third anniversary of A day, the starting date for the authorisation of investment advisors. Whilst I do not wish to say too much about the impact of the Act on the securities industry, although my own group as a substantial investor is clearly not unaffected, I would like to

concentrate upon the impact of the financial services regime on life insurance companies. In a nutshell the new rules which have been imposed upon us by and through LAUTRO have altered irrevocably the distribution channels for life and pension products and put under threat the continued existence of the independent financial adviser upon whom many of the major life companies, especially the mutuals, have been dependent for a substantial proportion of their business.

I think that it is here that the life insurance industry both in the sense of life offices themselves and the independent intermediary network have been exposed to the windy side of the law. There are, I acknowledge, a number of positive features within the regime:-

1 I think that it is right that there should be arrangements to compensate investors who suffer through the collapse of an investment advisory firm. Life offices themselves have been subjected for many many years to the financial supervision of the DTI and when necessary policyholders have had their interests protected under the Policyholders Protection Act of 1975, but I have to ask myself why in 1991? (What is the proper meaning of "United Kingdom Policy" and what is the proper meaning of "Private Policy Act"?)

2 I think that it is right that we should aspire to develop and improve the training and competency of those engaged in selling and administering insurance business. As a past president of the Chartered Insurance Institute, I know only too well of the commitment which exists to raising the standards of the insurance profession. Current proposals for competence testing in the Financial Services field of activity are very relevant.

3 I think that it is right that the quality of information provided to prospective policyholders should be consistent as between one company and another to allow a proper comparison to be made.

4 I think that it is right that the policyholder should be able to change his mind during a cooling off period if he has been subject to high pressure salesmanship. Of course, life companies have been happy to provide cooling off for some time prior to the Financial Services Act.

Where I begin to part company with the FSA is over the question of polarisation and its consequences for the life company and the policyholder. I am sure you will all recall the basic principle that customers should know the status of the salesman with whom they are dealing whether that person is a tied agent or an independent broker.

The second principle is that the tied agent can only sell products of one company whereas the independent broker must search the entire market and choose the most suitable product for his client. Fine principles indeed but perhaps not entirely in the public interest. Some time ago the Office of Fair Trading recognised the difficulty of polarisation for financial conglomerates such as banks and building societies. The result has been a dual status situation where many of these institutions have parts of their business tied to an insurance company with other parts offering independent brokerage.

I have no doubt that many life offices including my own have been on a considerable learning curve in developing their distribution networks in the light of polarisation and other features embodied in the LAUTRO rules.

I look back to the busy days of late 1988/early 1989 when suddenly building societies and insurers began to tie. Life companies, formerly staunch supporters of the independent sector, began to break ranks and develop their tied agency networks to run alongside their independent intermediaries. Everyone was beginning to count up the actual and potential cost of compliance and, for the independent intermediary, how that was matched by what was on offer under the LAUTRO maximum commission agreement. The result has been many formerly independent intermediaries have felt it in their best interests to become tied to one particular company and companies themselves have not been slow to take these people on although, I have to say, most of us have now come to realise the practical difficulties in accepting full responsibility for appointed representatives under Section 44 of the Financial Services Act.

One development which I find particularly disturbing is the proposal that life offices will have to accept certain responsibilities for other activities of their appointed representatives for non investment and other financial business.

Some of you will be familiar with the provisions of LAUTRO Consultative Bulletin No 5 issued in March 1991 which follow on from one of the SIB Core Rules. The Regulatory environment has, in effect, created polarisation. The Regulatory environment has created the "halo" effect of perhaps leading the public to believe that an Appointed Representative has the backing of his host insurance company for *all* business matters rather than just those for which he is tied.

Yet the life insurance companies will now have to accept the responsibility for making sure that their Appointed and Company Representatives are properly authorised or are exempt for any other investment business they carry on.

We will not be in breach of the proposed Rule if we have "... taken reasonable steps to comply". The penalty for failing to comply will involve a liability to investors.

This is, of course, perfectly reasonable in respect of our own investment business. But, the Regulators *must* lay down specific steps which they would regard as reasonable for the insurance company to take in respect of the business which is not their own.

If I am giving you the impression of carping at those who have been given responsibility to regulate the industry please let me assure you that I entirely support the principles behind the legislation and I realise that they have at times a difficult job to do in reconciling the views of Government, consumer protection bodies and industry practitioners.

However, it is perhaps worth noting that in the general insurance sector we have been able to avoid to a greater extent legislation aimed at controlling the marketing of our products. Lloyds itself has a strong tradition of self regulation. The global credibility of the London Market depends upon this. In addition we have the code of conduct which was put together last year under the auspices of the ABI. I think this demonstrates what can be done within the industry itself without the need for Government or statutory intervention.

By way of summary at this point I think it is worth adopting the motto used, I believe, by the Royal Yachting Association which is equally concerned at keeping its members away from the windy side of legislation. Their watchword is "education not legislation". Our industry has a commitment to self regulation. The process began and will continue on sound ethical principles of fair trading, healthy competition and financial stability, but I do not believe that the key lies in over regulation, in extensive rule books and over elaborate and expensive control systems. I believe the answer in the longer term depends upon education, training and recognised qualifications.

When launching the new SIB core rules in January this year Sir David Walker expressed his hope that "some of the earlier antipathy between the regulators and the regulated will disappear". We can only hope that when these principles find their way into the revised rule books of the self regulatory organisations we will begin to see the industry settle down to a period of consolidation in the regulatory sense so that we can properly address the challenges of 1992 and beyond. We have perhaps spent too much time concentrating upon the weaknesses and not maximising the strengths of what is after all one of the strongest if not the strongest sector of the UK economy.

Courts and Legal Services Act 1990

I want to say a little bit about European opportunities in a moment but before doing so I have a few thoughts which I wish to share with you staying with my windy theme about the way in which the legal process can on occasions work against the interests of insurers. I realise that law and litigation is a complex process and many of you, if not all of you, here today are specialists in this field. However, I think we have to bear in mind that insurance companies are amongst the largest buyers of legal services in the country and thereby significant customers of the legal system.

I confess that I do not know too much about the detailed provisions of the Courts and Legal Services Act 1990 but it seems to me that in the same way as the Financial Services Act has caused the life insurance industry to view its operations the legal profession itself has now been subjected to statutory intervention aimed at eliminating monopolistic practices within the legal profession, creating a more competitive market and improving professional standards amongst all those who aspire to provide legal services.

Section 17 of the Act sets out the general objects of the development of legal services in England and Wales, in particular the development of advocacy, litigation, conveyancing and probate services by making provision for new or better ways of providing such services and a wider choice of persons providing them, while maintaining the proper and efficient administration of justice. Dealing first with advocacy and litigation I think that the ending of the barristers' monopoly rights of audience in the higher courts should be regarded as a positive step. It will create what in the financial services industry we have called a level playing field so that those with appropriate skills in the conduct of litigation whether they be barristers or solicitors or indeed members of other professional bodies can represent their clients in the higher courts. What is more I understand that in theory and I hope in practice all such individuals will be eligible for appointments at all levels of the judiciary.

I think we will all be watching these developments with interest and from the perspective of the insurer I think we could end up by getting better value for money by not having to pay solicitors and barristers fees although in a wider and more social context I would be disappointed if those smaller solicitors firms in the provinces lost the opportunity to sue the services of the independent bar.

As to conveyancing and probate services as an interested observer it seems to me that this has caused and will continue to cause greater rumblings amongst the rank and file of the solicitors profession than any other aspect of the new Act.

I think we should remember the long-standing interest of life companies and indeed general insurers in the residential housing market. It is in our interests to promote an efficient and cost effective house transfer procedure and there is no greater spur to efficiency than the force of competition.

I recall the relative euphoria amongst a number of building societies and banks about 18 months ago when they saw the prospect of being able to add on conveyancing services. I expect that some are now thinking again in the light of the recession in the housing market but I think the time will eventually come when there will be even greater institutional control over the provision of conveyancing services and also I suspect probate services. Even though we want the solicitors profession to survive and we all value the need for independent advice I think we will see a number of financial institutions actively managing networks of independent legal practices to whom the client is referred for certain particular services which will have to be provided for a price and to a standard specified by the institution.

The Legal Process

As I have already mentioned I hope that the Courts and Legal Services Act will lead to a better legal service and improvements in the legal process. Access to the Courts is supposed to be a constitutional right but I fear that the legal process for civil disputes at least could become the preserve of the rich who can afford to pay (including insurance companies of course) and the legally aided poor who cannot afford to pay. I appreciate that many of us are now looking with increasing interest at the potential for the legal expenses insurance market which will seek to help those of us, who would otherwise have to fund our own litigation, with access to legal advice. That apart I think we would all agree that delays in getting cases to Court can be intolerable, frustrating and indeed lead to real hardship. Even when we get to Court the outcome can seem to depend upon what the Judge had for breakfast or perhaps a party, although right in law, could be made to feel uncomfortable as a result of the Judge's remarks. I am referring here to the windy side of the Court of Appeal in the case of *Foster v. Turnball* (reported in The Times May 22 1990). In this case my company sought successfully to avoid liability for a claim because of inadequacies in the procedural steps taken by the plaintiff's solicitors. However, we were criticised by Lord Justice Leggatt for playing the game, that is to say not acting in accordance with an acknowledged code of good behaviour by cynically taking advantage of such procedural rules as might prove of benefit to us. I must say that at the time we took and still do take exception to these obiter remarks, designed, I think, to shame us into paying a claim which due to delays on the part of the plaintiff's solicitors was out of time. Of course we can bear such remarks upon our broad shoulders but it is a pity that

His Lordship's remarks, at least as reported, did not dwell a little more upon the performance of the plaintiff's own solicitors.

Let me give you another interesting example of where I think the legal process has let us down. I will for obvious reasons avoid names but what I can tell you about is my annoyance at hearing that in a contractual dispute which is of major importance to us the plaintiffs obtained judgement against Norwich Union by default. This in fact was a mistake on the part of the Court office which has now been put right. However, the fact that such a judgement was issued to the Plaintiff by mistake was and continued to be a source of frustration and annoyance to me. I am told that this can be quite a frequent occurrence and perhaps indicates that the judicial system is overworked and underresourced. Maybe it tells us that we should begin to look very positively for alternative procedures.

I have long since held the view that there should be some legal process by which an innocent Plaintiff, caught in a dispute between two or more Defendants and who is bound to succeed in full, should be compensated before that dispute is resolved.

The Lord Chancellor's Department could well take this matter on board as I do not consider the Insurance market as a whole would be prepared to freely reach an agreement on this basis. At the end of the day it could well result in a saving to all parties.

Alternative Dispute Resolution

And alternatives there certainly are. I know that some of you here today are very much involved in the developments of alternative dispute resolution. I can see that there is considerable scope for this for insurers particularly in the personal injuries field. What we all want to see, I think, is a much more effective process of settling liability and quantum in getting the claims paid without the tortuous and time consuming processes of full blown litigation. There are so many situations where disputes can be resolved not in the traditional adversarial manner but through a consensual approach especially where the parties want to continue future business relations.

I accept that ADR is not the solution to all legal difficulties. Especially those where one party seeks some coercive solution as for example in the case of squatters which, in my company, we seem to have to deal with with increasing frequency in a number of our office and shop properties. It amazes me that the Court process seems to be so slow and overworked that those of us with legitimate rights to occupation and control of our property cannot quickly obtain eviction orders against those who are trading from them quite illegally and, in effect, at our expense.

European Developments

I said earlier that I would return to say something about the European scene. We certainly have the increasing prospect in years to come of a good deal of cross border selling of life and general insurance products as well as subsidiary operations throughout the Community. I know that the harmonisation process has begun not only in the insurance industry but also within the legal profession. I am sure that BILA through its association with AIDA will continue to contribute to the comparative study of insurance laws in different countries within the Community and that this work will be of great value as we pit our wits against our European competitors.

Role of Insurance Lawyers and Conclusion

As I now come towards the end of my address I would like to close by emphasising my personal views of the reports of lawyers within the insurance industry. I think it was Charles Dickens in *Bleak House* who said that "the business of the law is to increase the business of the law". I am sure that there are still many members of the public who are not a million miles away from that sentiment. Certainly in the insurance context I believe that the job of the lawyer is to provide his insurance client with expert advice in all the diverse fields in which insurance companies now operate. The advice he gives must be not only correct in law but realistic in the context of the commercial environment in which insurers have to operate. Insurance is essentially about assessing and taking calculated risks. Any insurer who proceeds without the benefit of expert legal advice deserves no sympathy if things so wrong. My belief is that in offering his particular skills and professional objectivity to the business manager the lawyer can make and be seen to make a significant contribution to the success of his client's business leaving, of course, the client to ultimately make the business decision with, I am sure, the benefit of the lawyer's analysis of the legal risks involved in one course of action or another.

In offering you this pot pourri of thoughts about the windy side of the law I hope that I have been able to provoke you to think through a number of points from the non legal practitioners point of view.