THE INSURANCE BROKER: INTERMEDIARY OR ADVISER?

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The purpose of my address today is to persuade you that the insurance broking business is undergoing certain developmental changes which have profound implications for the manner in which the business is managed and in particular for its exposure to liability.

I would like to begin by describing myself to you what I will call the old model of the insurance broker. This is the person who is the agent of the client and who may recognise that. He is the person who arranges the policy with the underwriter and receives his remuneration from a percentage of the underwriter's income, thereby giving him a neat conflict of interest with respect to his duties to the client. This is also the person who, if he understands the nature of the duty to disclose material facts, will not have thought to impart any of this information to the client at the outset. This is also the person who, although capable of talking all day, writes nothing down. This somewhat unkind and unfair description is in essence familiar from litigation affecting brokers.

From the primeval swamp of the highly cut-throat and competitive UK retail market there has emerged what I will call the modern model of insurance broker. This is the broker who, under pressure of showing added value and competing hard against his peers, has had to become much more thoughtful about the client's needs and requirements. This is a broker who has become adept at analysis and at the review of existing coverage. For this broker, the client has at long last taken control of his remuneration. The modern broker is paid either by way of a fee or by way of some proportion of the total commission. Either way it is a negotiation with the client. The modern broker also has the advantage of being able to write and now maintains respectable files which assist him in his moments of difficulty.

It appears to me that even the modern model is now under further pressure to change from three principal sources: the first is interesting; the second is depressing; and the third is positive, at least from the insurance broker's point of view. The interesting development is the phenomenal success of direct selling. Whilst confined at the moment to sectors of the mass market, nobody here today will need persuading that this is a vigorous area for growth, and will soon find its way into many other classes of insurance. This poses a threat not only to competitor insurance companies, but also to the broker whose traditional role of distribution agent is cut out altogether by this method.

The depressing pressure has been the failure of the product itself. The doctrine of utmost good faith has been abused by a number of insurers in order to avoid claims under policies. What is worse, a number of companies in the London market have become insolvent in the last three or four years, and we may see more of that. Either way, the customer's confidence in the reliability of the product has been diluted. Clients can no longer rely on having laid off particular risks by parting with premium to a third-party.

The third more positive pressure on the modern model has been the brokers' determination to sell the ancillary skills which they have developed as a discrete product. This has led to the emergence of risk management as a separate if related business. It comprises the analysis and reporting of risk, the establishment of captive insurance companies and the creation of sophisticated financial software enabling clients the better to understand and track their exposures so that they can make intelligent decisions about self-insurance and third-party insurance.

All this risk management work is fee-based, and may be entirely unrelated to the purchase of insurance. Indeed a number of clients take the view that their risk management consultant and their insurance broker should be completely different people.

In any event, I will call the person now providing these services the Supermodel. This is not to suggest that they have anything in common with the waifs on the catwalk, although a few of them are women and some of us would prefer to see a bit more of that. Let me give you some examples of the sorts of work now being undertaken by these Supermodels.

Health and safety surveys, originally targeted at construction sites, now extend to multi-storey office blocks, covering a range of accident and disease-related risks. Radiological contamination surveys in known damaged regions have also been conducted. Bidders have commissioned reviews of possible environmental pollution of the sites occupied by the target companies as part of the pre-acquisition due diligence. These sorts of reports are light years away from the traditional fire survey which was their origin.

The trend is also reflected in the corporate activity, certainly at Willis Corroon. In the last six months we have established an international joint venture company called Global Liability Management, which addresses risk management and disaster planning for multinationals. We have also taken an interest in a risk management operation based in Australia, but with international service bases, Richard Oliver.

The implications for the insurance broking businesses venturing into these fields are many. To begin with they must employ people with a much more diverse range of skills than those employed by the insurance broker, which implies a hard look at their recruitment and training programmes. Product description and the related pricing arrangements for this fee-based work are also providing a lot of mental exercise.

There is also the question of who will be our competitors and who will be our allies in this new business, and indeed are these two groups of people always different. Insurance companies themselves and a number of management consultants might regard themselves as being in the business, or capable of it. Accountants, who believe they can do anything at all, will also hold themselves out as being in this business. On the other hand, there may be more temporary alliances of different specialist skills in order to supply a particular combination of service to a client. Flexibility will be the key.

In thinking about the implications for the insurance broker's liability in this new area, I have concluded that there are more opportunities for positive results than negative, although it will be most important that the developing area is actively and thoughtfully managed.

Top of my list of positive aspects is the opportunity to introduce terms and conditions between the customer and the risk management consultant. This provides the opportunity not only to lay out the terms of reference and specify the role which is to be fulfilled, but it also provides the opportunity to include terms limiting the liability of the consultant.

Another positive feature is that the work normally results in a reasonably prompt written report. This is in sharp contrast to the old model of insurance broking where the policy might or might not be available by the time of the next renewal. Such a report provides the opportunity to describe the work which has been undertaken, including any qualifications on the process as well as with respect to any recommendations.

There is also one very simple benefit which is easily overlooked. This is that the risk management relationship is between two parties, whereas even the modern model of insurance broking involves three. There is automatically less opportunity for misunderstanding, never mind that a consultant is not of course dealing with the doctrine of utmost good faith.

Turning now to the negative features, it has to be acknowledged that the exposures on the face of it are just as great as in any conventional insurance broking business. Pre-acquisition due diligence reports are highly risky pieces of work, and a limitation of liability clause may or may not be effective. Another danger is of course the perennial risk of overselling the product. Finally, there are bound to be continuing tensions between the risk management business and the established broking relationships under the same ownership.

In the drive for added value, and the differentiation of the products offered, I believe that this trend to risk management advisory work is inevitable, although timing is very unpredictable. You will see that the title of the talk was actually a trick question. Insurance brokers if they are any good have always been both intermediaries and advisors. The real answer to the question is that in some respects we are ceasing to be insurance brokers altogether. From a liability point of view, the model litigators in the audience, whether they be old, modern or super, are not redundant yet.