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Duties and liabilities of insurance brokers – Focus on the information exchange and duty to advise in Greek, Serbian and UK law –

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Abstract

This article focuses on the issue of the liability of an insurance broker towards its client, when the client is the policyholder or the insured. For this, it is necessary first to establish what the obligation of brokers towards the client would be and what would be considered as its breach. There is considerable diversity between the European countries regarding the definition of insurance brokerage services, duties of insurance brokers and consequences of their breach. This article will particularly address those in Greek, Serbian and UK law. EU legislation attempts to provide the minimum harmonization established for the protection of the policyholders. “At the moment the insurance market, like many other markets, is characterized by imperfect information by each party to the transactions, significant search costs to find the best deal and asymmetric bargaining power”¹.

Here the emphasis is on the exchange of information between a broker and the insured before and after the conclusion of the insurance contract, and on the imputation of knowledge of the broker and of the insured. The issue of when it is considered that a broker has an obligation to provide advice and several cases of liability of brokers for providing the advice are presented. Some relevant issues in regard to the proposals of the amendments to the EU Insurance Mediation Directive (IMD)² are mentioned.

Key words: Intermediation, insurance, intermediaries, brokers, broker liability

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¹ The European Federation of Insurance Intermediaries (Bipar) – Insurance intermediation, <http://www.bipar.eu/en/home/multidimensional-activity> accessed 10.12.2011.

² Directive 2002/92/EC of the European Parliament and of the Council of 9 December 2002 on insurance mediation called the Insurance Mediation Directive or IMD.

1. INTRODUCTION

Duties of insurance intermediaries are usually regulated in several pieces of legislation, agreement between the insurance broker and the insured and codes of conducts. The laws covering this issue are the laws on private insurance or *lex specialis* on insurance intermediation, the civil codes with their provisions on agency, intermediation, liability for breach of contractual obligation or regulation and precedent law on liability for negligence in case of duty to care, regulation on protection of consumers, provisions on the distribution of financial products and package financial products. “The WFII³ encourages trade associations and interested parties to develop a code of conducts.”⁴ It concludes that such codes can be considered supplemental to regulation and legislation and they are important for the increasing of public confidence in the industry. They also may improve and clarify the relations between the insurer, intermediary and consumer.

Definition of insurance broker differs between jurisdictions. Often it is considered as independent entity, acting on the behalf and for the benefit of the insured while receiving remuneration from the insurer. Here particularly the solutions of Greek, UK and Serbian law are presented. The IMD does not make clear distinctions between insurance agents and brokers.

Some of the broker liability issues are subject to EU regulations and are largely discussed in literature, particularly those related to the independence of brokers, influence of the broker’s remuneration on his conduct through the precise disclosure obligation of its

³ The World Federation of Insurance Intermediaries (WFII).

⁴ WFII Principles: Regulation on insurance intermediaries, June 2002, <http://www.wfii.net/en/key-issues-positions/regulation>, accessed 12.12.2011.

relations with the insurers offering the relevant product on the market⁵, information obligation and handling of the client's monies. Other relevant issues such as the issue of liability for not concluding the appropriate insurance cover on behalf of the client have so far been only insufficiently and indirectly regulated in EU regulations.

2. DEFINITION OF INSURANCE BROKER AND DESCRIPTION OF HIS DUTIES

The IMD does not follow the traditional distinction between insurance agent and insurance broker. It recognizes a tied agent and an insurance intermediary. The mediation is defined as "the activities of introducing, proposing or carrying out other work preparatory to the conclusion of contracts of insurance, or of concluding such contracts, or of assisting in the administration and performance of such contracts, in particular in the event of a claim."⁶ Consequently, an insurance intermediary is a natural or legal person who performs insurance intermediation as a profession. Most EU Member States (hereinafter: the MS) propose that in the Revision of the Insurance Intermediation Directive (hereinafter: the IMD2) this activity-based definition be supplemented with the basic definition of agents and brokers, as these categories appear to exist in most MS.⁷ It is considered to be a starting point for further harmonization in this field.

Greek law provided that an insurance broker acts on the orders of the insured, so the broker was considered to be their representative, although he was paid by the insurer.⁸ Thus he is different from the intermediary in commercial agreements as his position is not considered to be in the middle, between two parties. His duties are to connect the insured with insurers or reinsurers; conduct all preparatory activities for the conclusion of insurance agreement; receive acceptance from the insurer and the insured; and to help during its execution, particularly in case of the occurrence of a risk.

⁵ IMD, Article 12.1-4.

⁶ IMD, Article 2 paragraph 3.

⁷ The Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) advise on IMD's Revision as of 10 October 2010, Ref: CEIOPS CCP-59/10, <https://eiopa.europa.eu/publications/submissions-to-the-ec/index.html>, accessed 10.12.2011.

⁸ Article 15a of the Greek Law no 1569/1985 on Intermediation in the Agreements of Private Insurance, Organization of the Association of Experts for Motor Car Accidents, Operation of the Office of International Insurance and other Provisions.

Contrary to the above, Serbian law⁹ sees the insurance broker more in its intermediation role. It may be acting on the behalf and for the account of the insurer or of the insured. The insurance broker's activity is to connect the insured or policy holders with insurers for the purpose of negotiation conclusion of insurance, based on the order of the insurers or on the order of the insured or policyholders. Apart from strict intermediation, the broker may provide advisory services, assistance in claims handling and in the estimation of risks and damages. However, when acting for the insured he is obliged by law to provide explanation and advice.

In the UK (England and Wales) there is a legal duty of the broker to act in good faith in what he believes to be the interest of his client. There is no legal definition of an insurance broker. An authorization from the Financial Services Authority (hereinafter: the FSA) is required in accordance with the Financial Services & Markets Act for performing activities, such as assisting in the administration and performance of a insurance contract ; advising on investments; advising on insurance policies; arranging deals in investments.¹⁰ Brokers must abide by the FSA's Handbook, including the Insurance Conduct Business Sourcebook (hereinafter: the ICOBS) for non-investment insurance, the Conduct of Business Source Book (hereinafter: the COB) for insurance investment products and the new rules and guidance from 2009 on the effective management of conflict of interest which form the systems and controls (SYSC) section of the Handbook¹¹. It has been noted that a tendency of the FSA is to move away from a rules-based regime to a principles-based regulation, which gives brokers much greater flexibility but may be a challenge to interpret the principles and respond accordingly.¹²

⁹ Article 72 of the Serbian Law on Insurance, Official Journal no. 55/2004, 70/2004, 61/2005, 61/2005, 85/2005, 101/2007, 63/2009 and 107/2009.-

¹⁰ FSA regulation of insurance selling and administration information sheet at http://www.fsa.gov.uk/pubs/other/ins_reg.pdf, accessed 8. 12. 2011.

¹¹ Alexis Roberts, Insurance broker remuneration: law and regulation, as of 11 March 2008, p. 2, www.out-law.com, accessed 10. 12. 2011.

¹² Wynn, Richard (2008) "Regulation brings responsibility", *PI Matters*, the Broker, p. 33. <http://www.biba.org.uk/PDFfiles/regulationbringsresponsibility.pdf>, accessed 10. 12. 2011.

3 GENERAL ON INSURANCE BROKERS' DUTIES AND LIABILITIES

The IMD imposes an obligation on the insurance brokers to acquire professional liability (hereinafter: PL) insurance cover or other comparable guarantee against liability for professional negligence in the amount of one million Euros per claim and in aggregate amount of one and a half million Euros per year unless the insurer has taken on full responsibility for the intermediary's actions.¹³ It does not define the duties which should be covered by the PL insurance.

Based on the different definitions of insurance brokers including the IMD definition and developed practices the duties of insurance brokers may be divided into three categories based on the time of their fulfillment:

- *Preparation and mediation to the conclusion of insurance contracts*

These are considered to be the main obligations of brokers. They include providing of all necessary information about the broker himself, the insurer, their relations, on the insurance product and the risks it covers. They may include providing advice on the insurance products available on the market and choosing the best suitable for the client, particularly in cases of complex insurance investment products. Representation of the insured before the insurer, particularly assistance in completing the application form and advice regarding disclosure of all relevant and material information, is often included in their duties. Receiving the insurance premium and passing it to the insurer is common. Brokers also have a duty to keep personal data information confidential.

- *Assistance during the contract*

A commonly mentioned duty is reminding the insured about the renewal of the insurance cover and assisting in the conclusion of the new agreement. It may include other relevant provision of information and, when applicable, obtaining of such information.

- *Assistance after the occurrence of an insured event*

It is customary that insurance brokers check and explain the terms of the insurance policy and possibly objections, assist in collecting data of events, legal grounds, amount of damage, instruct the insured on the procedures of collecting evidence, assist in filling

¹³ IMD, Article 4.3.

in the application form and contacts with the insurer until payment of the damage or benefits. It may include receiving the monies from the insurer and transferring them to the insured. Any wrongful conduct of the broker, which made the insured sustain loss, could be qualified as an error and omission which caused the liability. The majority of the investigated countries "accept that a broker should pursue the performance of the insurance contract serving the best interest of its clients, assist its client with the filing of a claim against the insurer and provide claim-handling services"¹⁴. Furthermore, most of the investigated countries require that the broker act with the attention of a good professional, with skill and due care expected by a professional while executing instructions it has received from its client.¹⁵

The brokers may limit their exposure to indemnity through a PL insurance policy and through exemption clauses in their agency agreements but the limitations would not normally apply neither to an intentional breach and nor to gross negligence. It is believed that claims linked to brokers exceeding underwriting authority will be on the rise. "And with insurers similarly feeling the heat from the economic downturn, they are far less likely to back a broker who has overstepped the mark."¹⁶ Furthermore, clients are likely to be more demanding.

The most common breaches of brokers' duties are: failure to provide insurance cover in time; failure to renew insurance; failure to carry out the client's instructions; granting of insufficient or faulty advice; failure to provide adequate information regarding its own intermediation services; and failure to place the risk with a reliable and creditworthy insurer.

4. INFORMATION REQUIREMENTS OF THE BROKER AND OF THE POLICYHOLDER

MID provides that prior to the conclusion of any initial insurance contract, and, if necessary, upon amendment or renewal thereof, an insurance intermediary shall provide the customer, but not in the insurance of large risks and mediation by reinsurance intermediaries, with

¹⁴ A comparative review on insurance mediation based exclusively on the answers received by AIDA National Chapters and on reports and speeches of the participants during the sessions of the Working Party, by Maria Demirakou, pg. 182, Insurance Intermediaries, Distribution of Insurance Products, edited by Ioannis Rokas, Ant. N. Sakkulas Publishers / Bruylant, 2010.

¹⁵ *Ibidem*.

¹⁶ Roddis, Mark (2008) "When the going gets tough", *PI Matters*, the Broker Magazine published by BIBA, p. 31.

at least those information required by the IMD that refers mostly to identification of the broker, issues related to his independence and out-of-court complaint and redress procedures.¹⁷ In regard to choice of insurer the intermediary is obliged to provide information whether it has exclusive agreements with one or more insurers and their names, or it gives advice based on a fair analysis of the market or it works with several insurers on non-exclusive basis without further analysis of the market, in which case it should provide their names.

Apart from the obligation of the insurer in relation to a specific insurance product, as well as, any additional information provided in the legislation of MS, an obligation for any additional information should be agreed in the agency agreement between the insurer and the brokers.

In the UK the FSA plans to introduce additional disclosure rules for sales of pure protection products (critical illness, income protection and non-investment life insurance) under the ICOBS rules. There is discussion on the EU level about imposing additional product related information e.g. related to PRIPs.¹⁸

MID further provides the obligation of the insurance intermediary to “at least specify, in particular on the basis of information provided by the customer, the demands and the needs of that customer.”¹⁹ Naturally, the policyholder has the obligation to provide relevant information, but this is not within the scope of this article. The broker is obliged to ask and learn the exact demands and needs of his client in order to propose insurance cover. He may be held liable for negligence in performing this duty.

5. REPRESENTATION AND IMPUTATION OF KNOWLEDGE AND FAULT OF BROKERS

Knowledge and fault of insurance brokers is imputed to either insurance companies or policyholders because they act either on the behalf of the insurer or the policyholder. In particular cases it is the matter of fact to determine for whom the broker acted. Imputation of knowledge is normally a legal consequence of representation, so that the knowledge of the agent is imputed to its principle. This applies to the information obligation of the broker and his assistance during filling in the application form and particularly answering the

questionnaire regarding the material facts relevant for the insurance risk. In the modern world the distribution network is growing and this is becoming more important and the issue of knowledge and fault of intermediaries appears more often in litigation and legal literature.²⁰

The justification for the imputation of the broker's knowledge to the insured differs among jurisdictions: it may be related to the exercising of control of the principal over the broker including the fact that the principal chose his agent or the rationale is in the risk allocation as the principle increases its profits through the use of agents plus he is in a position to take precautionary measures to prevent any fault.²¹

While for the insurance agents the situation is simple and clear as “naturally, what is known to the agent means that is known to the company”²² (insurer), it may not be so clear for the insurance brokers. The first question is who the broker represented and then if there is justification to impute the knowledge of the broker to the insurer.

An issue arises when a broker commits faults when providing guidance and advice to the insured. For example in *Winter v Irish Life Assurance plc*²³, the policyholders bought life insurance through a large firm of independent insurance brokers. The brokers knew that both policyholders suffered from cystic fibrosis, but this information was not disclosed to the insurer. The case was heard in the High Court before Sir Peter Webster, who held that the brokers acted for the policyholders, not the insurers. The relationship between the brokers and the insurers was insufficient to establish an agency. It was not sufficient that the insurers paid the brokers commission, or gave them publicity material over-printed with the brokers' name, or provided guidance and training about how the forms should be filled in. The judge laid particular stress on the fact that the policyholders approached the brokers to find the insurance.

On the contrary in case *Roberts v Plaisted*²⁴, Mr. Roberts insured a hotel through a Lloyd's broker. The hotel operated

²⁰ Chrssanthis, Christos (2010) “Representative power of Insurance Intermediaries, Insurance Intermediaries, Distribution of Insurance Products”, edited by Ioannis Rokas, Ant. N. Sakkoulas Publishers /Bruylant, pp. 49–71.

²¹ *Ibidem*.

²² Nektarios, Miltiadis (1998) *Introduction to Private Insurance*, Financial Forum, p. 106, (in Greek).

²³ *Winter v Irish Life Assurance plc*, [1995] 2 Lloyd's Rep 274 and the English Law Commission and the Scottish Law Commission Insurance Contract Law, Issues Paper 3, Intermediaries and Pre-contract information, March 2007, p. 16, http://www.justice.gov.uk/lawcommission/docs/ICL3_Intermediaries_and_Pre-contract_Information.pdf, accessed 10. 12. 2011.

²⁴ *Roberts v Plaisted* [1989] 2 Lloyd's Rep 341 and the English Law Commission and the Scottish Law Commission Insurance

¹⁷ IMD, Articles 12.1. 12.2. and 12.3 for the information provided by the insurance intermediary

¹⁸ Package Retail Investment Products.

¹⁹ IMD, Article 12.3.

a discotheque, which the broker was shown when he inspected the premises. Following a fire, Mr. Roberts made a claim for £70,000. The underwriters sought to avoid the contract on the grounds of non-disclosure of the existence of the discotheque. The Court of Appeal was able to decide in favour of Mr. Roberts by finding that the disclosure of information had been waived, although the basis of such a waiver is open to question.

It is common practice for intermediaries to complete proposal forms on behalf of the applicants. Applicants are often deterred by the length or complexities of proposal form and they easily agree to be led through the questions by the intermediary, often over the telephone. The intermediary then records the answers on the proposal form, which is then signed by the applicant.²⁵ The rules of imputation should particularly apply in the following cases: when the material facts are specifically raised in the questionnaire, the policyholder fully informs the broker, but the latter fails to communicate these facts to the insurer or the material facts inappropriately raised in the questionnaire and the broker incorrectly advise the policyholder on how to complete the questionnaire or the material facts are properly raised in the questionnaire, but falsely answered by the policyholder due to the wrong advice by the broker or the broker fails to properly advise the insured in respect to some other.²⁶

The question then arises — who is responsible for these inaccuracies? The precedent case of English law is *Newsholme Brothers v Road Transport and General Insurance Co Ltd*²⁷. In *Newsholme*, the plaintiffs had insured a motor-bus through a man named Willey, who was said to be appointed by the Road Transport and General Insurance Co Ltd to canvass and procure proposals for them. He completed a proposal form, which was later approved for cover by the insurers. When a claim occurred it was found that Willey had entered inaccurate answers to three of the questions on the proposal form, even though he had been given the correct information by *Newsholme Brothers*. The insurer repudiated liability for breach of warranty and rejected the claim. The Court of Appeal held that the insurer was entitled to repudiate liability since in completing the proposal form Willey had been acting as the agent of *Newsholme Brothers*. Lord Justice Scrutton set out the court's reasons as follows: "If the answers are untrue, and [the agent] knows it, he is

committing a fraud which prevents his knowledge being the knowledge of the insurance company. If the answers are untrue, but he does not know it, I do not understand how he has any knowledge which can be imputed to the insurance company. In any case, I find great difficulty in understanding how a man who has signed, without reading it, a document which he knows to be a proposal for insurance, and which contains statements in fact untrue, and a promise that they are true, and the basis of the contract, can escape from the consequences of his negligence by saying that the person he asked to fill it up for him is the agent of the person to whom the proposal is addressed."²⁸

A small number of reported cases reach a different result. However there are suggestions and developments related to the protection of the weak party and, particularly, the consumer. There are serious criticism in cases where the agent has committed a fraud on his own initiative (because, for example, he was anxious to gain his commission) and proposals that this should be an exemption to the above rule. If a sales representative is employed by the insurer as the insurer's agent, it might be thought that the insurer should carry greater responsibility for the fraud than the insured.²⁹ The criticism applies to the content of the questionnaire prepared by the insurer. There are cases, although rare, that the knowledge of the broker should be imputed to the insurer and not insured because the operation of brokers provide greater assistance to insurers to increase the number of policies concluded, than to the insured to obtain cover. The insurers benefited by the intermediation if the cover is rejected on the grounds of non disclosure of the facts.

In Serbian law the issue presented above is yet to be regulated. The general rules on representation do not deal with the knowledge of the agent while article 914 of the Law on Obligations regulates specific situations as the consequences of failure of policyholder to provide material information to the insurer or provision of false information shall apply also to a person who concluded the agreement in the name and for the account of another person, or for the benefit of a third person if these persons knew that the material information was false or not provided.

Contract Law, Issues Paper 3, Intermediaries and Pre-contract information, March 2007, p. 10.

²⁵ English and Scottish Law Commission, Issues paper 3, Intermediaries and Pre-contract information, London March 2007, p. 24.

²⁶ *Ibidem*.

²⁷ [1929] 2 KB 356.

²⁸ *Ibidem*, p. 374–5 and the English Law Commission and the Scottish Law Commission Insurance Contract Law, Issues Paper 3, Intermediaries and Pre-contract information, March 2007, p. 25.

²⁹ The English Law Commission and the Scottish Law Commission, Insurance Contract Law, Issues paper 3, Intermediaries and Pre-contract information, p. 27.

The Reinstatement of European Insurance Law³⁰ provides in article 1:206 the following solution: Imputed Knowledge: "If any person is entrusted by the policyholder, the insured or the beneficiary with responsibilities essential to the conclusion or performance of the contract, relevant knowledge which that person has or ought to have in the course of fulfilling his responsibilities shall be deemed to be the knowledge of the policyholder, the insured or the beneficiary, as the case may be." The proposed solution could be acceptable for Serbian law, with the exception that at least the fraudulent actions of broker, when known by the insurer, should not harm the insured.

6. AGENCY

Regulation of all agencies in civil codes applies to also to the agency issues of insurance intermediation. But the liability during negotiations of agency agreement between the broker and the policyholder is commonly regulated by separate rules and is considered to be either tort or quasi contractual liability. It may result in obligation to pay damages.

UK law defines agency as a relationship which arises when one person, called the principal, authorizes another, called the agent, to act on his behalf, and the other agrees to do so. The relationship arises out of an agreement, whose most important effect is that it enables the agent to make a contract between his principle and a third party³¹. An insurer's agent may become the insured's agent when helping him to complete the proposal form³². Insurance brokers are for most purposes agents of the insured persons and not of the insurers, but may be agents of the insurers for some purposes such as the provision of interim insurance cover until the policy is issued.³³ The agency does not have to be constituted by written agreement. The main duties of agent are: to carry out his instructions, to act with due care and skill and his fiduciary duty (loyalty and fidelity).³⁴

In any event, the general rule in all agency cases is that the agent depends on the authorization and the instructions given to him by the principal. If the instructions are

silent on a particular matter that is covered by insurance market usage, he may transact the business in accordance therewith. "The principal will not succeed in showing that the agent has departed from his instructions if these were ambiguously worded with the result that the agent has reasonably understood them in a contrary sense to what was intended, since such conduct is consistent with the exercise of reasonable skill and care. The agent will be answerable for loss caused by his negligence only if he fails to display a reasonable standard of skill and diligence in transacting the instructions in question."³⁵

Greek law provides that: "The liability of broker to the insured is limited to the correct execution and application of the written instructions of the insured³⁶" From the point insurance agreement validity, an intermediary relation should be evidenced, it may not be presumed.³⁷ Greek Civil code provides that an agent is liable for its fault meaning that he would be liable for intention, gross negligence and light negligence. However, the parties may agree that the agent is not liable for the light negligence. The agent may represent the principal before the third persons only if there is a written agreement of representation³⁸ and not based on a verbal agency agreement. The agency agreement regulates the obligations of the agent including the authorization of the agent to represent the principal. The agent may derogate from the principal's order only if he cannot inform the principal and it is obvious that the principal would have agreed with the derogation had he known the facts which caused the need for derogation. Although there is a general obligation of the agent to provide to his principle the relevant information and there is no explicit obligation to protect his interest, he would not have the obligation to research if the fulfillment of such instructions is really in the interest of the principle. He might have this obligation only if the agency is agreed based on a special knowledge of the agent, which the principal does not possess. He has a general obligation to inform the principle about possible risk and damage.³⁹

³⁵ Rokas, Ioannis (2010) "Issues attached to the role of Insurance Intermediaries", *AIDA*, p. 44.

³⁶ Article 15 e of the Greek no 1569/1985 on Intermediation in the Agreements of Private Insurance, Organization of the Association of Experts for Motor Car Accidents, Operation of the Office of International Insurance and other Provisions

³⁷ A. Argiriadis, R. Chatzinikolaou – Angelidou, L Skalides, *Ibidem*, p. 39 and I.K. Rokas, *Ibidem*, par. 1303 and notes 13–16, p. 881.

³⁸ Greek Civil Code, Article 217.2.

³⁹ Greek Civil Code, Article 713–726.

³⁰ Reinstatement of European Insurance Law, as of 27 July 2011, <http://www.restatement.info/>, accessed 10. 12. 2011.

³¹ Treitel, G. (2007) *The Law of Contract*, Sweet & Maxwell, p. 752.

³² *Ibidem*, p. 456.

³³ *Stockton v Mason* [1978] 2 Lloyd's Rep. 430 (except in cases of marine insurance).

³⁴ Treitel, *Ibidem*, p. 799.

The content of the brokerage agreement is often pre-drafted standardized terms, thus the additional protection of a consumer for these types of agreements would apply.

Serbian law on Obligation Relations⁴⁰ does not provide for an obligation of the agent to provide advice. An agent is obliged to execute the instructions of the principle with the care of a good business man, staying within the limits of the order and always protecting the interests of the principal. If an agent considers that execution of the instructions would be damaging for the principal, he is obliged to pay attention and to seek new instructions; if the principal fails to provide any specific instructions, the agent is obliged to protect the interests of the principal, act as a good business man. He may deviate from the instructions only after acquiring the approval of the principal or in case of lack of time or other cause, only if by judging all circumstances, he may have had a well grounded opinion that it would have been in the interest of the principal.

After the occurrence of the insured's risk, all countries⁴¹ accept that a broker should pursue the performance of the insurance contract serving the best interest of its client, assist its client with the filing of a claim against the insurer and provide claim-handling services. He should adequately cooperate with the insurer to affect a claim settlement.

Insurance brokers often agree to take responsibility for the ongoing management of the cover they have placed. They are often perceived as purely administrative, which may include duties to alert their client to potential breaches of policy terms and conditions.

Serbian law, in article 84, imposes the obligation of the broker to offer assistance to the insured for the duration of the insurance contract, before and after the occurrence of a risk; to take care that the insured respects the time limits for the actions which may have a prescription period; follows up with the application of the agreement and drafts the proposal for its amendments, if needed for better security of the insured.

7. DUTY TO ADVISE

IMD does not provide the obligation of the broker to provide advice. It regulates that in cases when a broker recommends a certain insurer and insurance cover he should state if the recommendation is based

⁴⁰ Serbian Law on Obligation Relations, Articles 749–770 on Agency.

⁴¹ A comparative review on insurance mediation based exclusively on the answers received by AIDA National Chapters, Insurance intermediaries, Distribution of Insurance Products, AIDA 2010 report.

on a fair analysis of the market or he works with several insurers. If he informs the customer that he gives his advice on the basis of a fair analysis, he is obliged to actually perform the adequate market search. The IMD considers a “fair analysis” to be analysis of a sufficiently large number of insurance contracts available on the market, to enable him to make a recommendation, in accordance with professional criteria, regarding which insurance contract would be adequate to meet the customer's needs. The IMD does not provide for an obligation to advise his client but if he provides the advise or recommendation to take insurance cover from a particular insurer, claiming to have made research of the market, it should be based on a significant large number of insurance contracts, should investigate the material facts and needs of the insured and provide him the reasons for such advice.

The duty of the broker to examine the financial situation of the insurer exists in most countries. The question is whether it is a theoretical obligation and whether the broker has any means to examine the financial situation of insurers. What if the check was performed but the estimation was not correct?

In Serbia brokers are obliged to provide explanations and advice on issues relevant to the conclusion of an insurance agreement. They are obliged to protect the interests of their clients and their license may withdrawn if it is establishes that the interest of the clients have been jeopardized.⁴² Furthermore the obligation to provide explanations and advice particularly includes the obligation to: perform risk analysis and proposes adequate cover; perform insurer's solvency estimation on the basis of the data on the insurer; mediate for the negotiation of the conclusion of the insurance agreement with an insurer, which based on the circumstances of a particular case, shall provide the best cover for the insured; inform the insurer on the insured's intention to conclude the insurance and offer the insured conditions and explain the method for calculation of the premium; and control the content of the insurance policy.⁴³ The obligation to propose the best cover under the circumstances seems to be rather burdening for simple insurance agreements.

In Greece the advice and recommendation are considered to be part of the obligation of an insurance broker but the liability for any damage arising from broker's advice or recommendation exists only if he undertook such liability in the brokerage agreement or he provided such wrongful advice or recommendation

⁴² Serbian Law on Insurance, Article 81.1 a).

⁴³ Serbian Law on Insurance, Article 84.

intentionally.⁴⁴ Advice in this provision is the dispositive norm related to certain performance in the interest of the one who receives such advice is thus different from providing of information. Contractual undertaking of liability may be a) by undertaking separate guarantee of liability (in which case the agent undertakes to pay for damages, possible limited amount of damage, if such advice was not correct regardless on the negligence b) undertaking contractual obligation to provide advice. Such obligation may be part of the agency or other agreement. The content of the obligation to provide advice should be providing of conscientious, well based, complete (entire), precise and comprehensible advice so that there is no incorrect (erroneous) picture. If the advice is agreed as a separate obligation, in case of delayed or bad performance, the agent shall have the obligation to pay damages in accordance with general rules on contractual damages including rules on prohibition of the exemption clauses for intention or gross negligence. The broker is liable for his fault for errors and omissions he had during the application of the agency which includes choosing of proper insurer for the particular risk, but not for the activities, errors and omissions of the insurer, unless explicitly agrees. The agreeing on the liability for the insurer would not be within the legal nature of the agency agreement. He may agree that he has increased level of diligence (e.g. to provide the best advice) as this is the reason for a policyholder to address to a broker. Errors and omissions of broker include breaches of the obligation of diligence and exceptionally an error or omission should be accepted to be without liability.⁴⁵

At the end of the day, it is the interpretation of the court about the intentions of the parties and the range of the obligation of the broker to investigate the circumstances related to the insured, relevant for the insurance cover, as well as, the level and the simplicity of the explanation of the insurance cover and the main obligations of the insured arising from the policy to be presented to the policyholder before signing or renewing the policy. Several recent decisions of the UK and Italian courts provide interesting examples:

In case *Jones v Environcom*⁴⁶ the court concluded that an insurance broker control whether the client fully

⁴⁴ Greek Civil Code, Article 729.

⁴⁵ Rokas, Ioannis K. (2006) *Private Insurance*, Ekdoseis Ant. N. Sakkoula, p. 885 and Greek Presidential decree 190/06 introducing the IMD in Greek law.

⁴⁶ *Jones v Environcom*, first instance judgment of Mr. Justice David Steel in the Commercial Court, *Nicholas G Jones v Environcom Ltd and MS plc trading as Miles Smith Insurance Brokers* [2010] EWHC 750 (Comm) at <http://www.out-law.com/page-11025>, accessed 10. 12. 2011.

understands the duty of disclosure in a property damage and business interruption policy. This usually requires specific verbal and written explanations when the insurance is first taken out and at renewal. Environcom recycled fridges. It this processing it uses some highly inflammable material which in the period between 2005 and 2007 resulted in several serious fires at the plant, which were reported to the insurer and several minor fires, which were not disclosed to the insurer as no insurance claim was made. The renewal of the policy came around in May 2007, the insurer at first rejected to provide cover, but was later persuaded by the broker to provide the cover under very stringent terms. More fires occurred in May, June and September 2007 culminating in the major fire in September 2007. The insurer declared non-liability due to the non disclosure of all the previous fires. In 2009 a settlement was reached at £.950.000 Environcom now pursued a claim against the broker for a further £ 6 million for negligently failing to warn it properly on its duty to disclose material facts. When renewing the policy, the broker sent the policy documents to Environcom under covering letter which reminded the insured of its duty to notify any material changes that might affect the cover. The judge found that the broker was in breach of its duty, but that the breach had not caused the insured any loss, as in he had disclosed all the facts about the frequent fires no insurer would accept to provide insurance cover. For this paper the conclusion of the judge is interesting in that a broker must advise the client of its duty to disclose all material facts and explain the consequences of failing to do so. The broker should indicate the sort of matters which ought to be disclosed and try to obtain all material facts from the insured particularly as the insured might not think some information relevant and might fail to mention them. In the judge's view the material sent to Environcom did not help it understanding when disclosure was required, what might be material or what would be the consequences of non-disclosure. In any event, it appeared that Environcom was operating in breach of its waste management license, so even if it had managed to obtain alternative cover, this material fact would not have been disclosed and the policy would have been avoidable. Nevertheless the final outcome of this case for the brokerage industry is seen to be further extension of the brokers' liability. "The warnings about the scope of a broker's duty to advise about disclosure should sound warning bells in the industry. It is difficult how a broker can provide generic advice 'with examples' to his clients about the nature of material facts without some understanding of the processes carried on by

them.”⁴⁷ The question is whether “it will be necessary for a conscientious (and non-negligent) broker to make quite extensive enquires of his clients about their manufacturing and other processes as well as giving advice about the nature of material facts.”⁴⁸

In a similar conclusion of the Italian Supreme Court⁴⁹, the court reaffirmed the due conduct requirements for Italian insurance brokers. *Intromeccanica Bertolini S.p.A* brought an action before the Court of Milan against the broker *MARSH S.p.A* alleging that the latter did not provide sufficient level of diligence, due by law, when assisting and advising him. The broker, on the other hand, claimed that Bertolini failed to provide sufficient and exhaustive information to him. The Supreme Court confirmed the previous court decision stating that it is broker’s duty to assist clients both in determination of the content of the contract and in the management and execution of the contract itself. The Court concluded that the broker acts as the client’s adviser, who has the duty to analyze which contractual models on the market best suits the client’s interests in order to offer it the most suitable insurance cover.

In the case *Ramco v Weller*⁵⁰ the issue of brokers’ liability is related to the sufficiency and adequacy of the insurance cover. The insured traded in army surplus stock. In some contracts with the Ministry of Defense his liability for stock losses was imposed in other not. He instructed the broker to obtain cover for goods entrusted to him. The insurance covered material damage to “stock ... in the property of the insured or held by the insured in trust for which the insured is responsible.” A fire, for which the broker was not liable, broke out at the premises but a great deal of stock was damaged. The insured claimed under the policy but the insurer successfully disputed most of the claim. The insured sued the broker. The insured was a bailee of the goods (had possession but the ownership remained with the Ministry of Defense until the sale). His insurance policy covered goods in “trust for which the insured is responsible”. As mentioned before, he was not liable for the damage of the goods. The broker obtained the policy which provided only limited cover, only for the liability of the insured and not for damage of goods regardless of the liability and legal costs of the insurance litigation. The judge found the brokers liable. The conclusion was

⁴⁷ Counson, Edward (2010) “Plasma gunfire – Insurance brokers’ duties and *Jones v Environcom* and *Miles Smith Insurance Brokers* (third party)”, *Wire*, Davies Arnold Cooper.

⁴⁸ *Ibidem*.

⁴⁹ *Bertolini v Marsh*, Italian Supreme Court decision no. 12973, 27 May 2010, Hogan Lovells Global Insurance and Reinsurance Bulletin Winter 2010 Issue 3.

⁵⁰ *Ramco v Weller*, at www.out-law.com/page-11025, accessed 10. 12. 2011.

that a broker owes his client duties in contract and tort to exercise all reasonable care and skill in advising them and obtaining appropriate cover. The insurance should meet the client’s requirements and be such that the client does not become embroiled in legal disputes. The broker should explore with the client the nature of his business. A broker had to consider the terms of the policy carefully before he could recommend the narrower insurance wording. There was not a suggestion that a policy with wider wording could not have been obtained or even that it would have cost more. The amount of the damage owed by the broker was equal to the full value of the goods. But the broker has, in accordance with his agreements with the goods owner, to account to the owner any insurance proceeds over and above his own loss.

8. AMENDMENTS OF THE IMD

The EU Commission is currently reviewing the IMD. It organized a public consultations on certain issues, which lasted from November 2010 until the end of January 2011. Among the issues related to the subject of this text is the proposal to set different information requirements when brokers are selling PRIPs, thus creating two regimes for selling of the insurance products: one for general insurance products and one for insurance PRIPs.⁵¹ This practically means the introduction of MiFiD rules.⁵² In this regard, the Report on Good Practices for Disclosure and Selling of Variable Annuities prepared by European Insurance and Occupational Pensions Authority (EIOPA) considers that good selling practices for variable annuities have to ensure that the demands and needs of a customer are taken into account, because of their inherent complexity, variable annuities should always be sold on an advised basis via a salesperson. The good selling practices should focus on the customer’s objectives to determine his demands and needs⁵³. The broker should check the personal circumstances, use clear product descriptions including illustrations, use clear language and understand potential future outcomes.

The revision of IMD should further be focused on the insufficient quality of information provided to

⁵¹ Consultation by Commission Services on legislative steps for the Packaged Retail Investment Products Initiative, http://ec.europa.eu/internal_market/consultations/2010/priips_en.htm, accessed 10. 12. 2011.

⁵² *Markets in Financial Instruments Directive* 2004/39/EC ili MiFiD

⁵³ Report on Good Practices for Disclosure and Selling of Variable Annuities prepared by European Insurance and Occupational Pensions Authority (EIOPA), EIOPA-CP-11/007, 27 October 2011.

consumers and conduct of business rules (conflict of interest and transparency). A potential conflict of interest is seen⁵⁴ in the dual role of brokers as advisors to their clients and as a distribution channel for the insurer. This conflict may influence the objectivity of the advice they provide to their clients and their own commercial considerations.

There were proposals that information on remuneration should be provided on request, while representatives of German insurers propose that the “quality of advice should be more important for consumers than remuneration disclosure.”⁵⁵ The FSA representative responsible for insurance intermediaries commented that retail consumers should know more about the products, services and the risk covered rather than the remuneration aspects.⁵⁶

The main criticism of the current application of the IMD in regard to the subject of this article are that the information given to consumers varies significantly in quality depending on the insurance products and the prevailing regulatory requirements. However, in general, the information is dense, legalistic, full of jargon and difficult to digest.⁵⁷

9. CONCLUSION

The review of the Greek, UK and Serbian legal solutions, proposals and development in the EU regulation and the developed practice and code of conducts show that providing information and explanation to the policyholder regarding the insurance cover and acquiring relevant information from the policyholder is essential for the broker to be able to advise or recommend a particular insurance cover. He must understand the needs of the insured. Often in order to do so, he must acquire at least the basic information on the insured's business or object of insurance and circumstances related to it. He should perform research of the insurance market in search for the best policy terms and check on solvency issues of the proposed insurers. In most cases he shall be considered better informed and specialized than the insured so that

he will be liable for the rightly posed questions to the insurer. He must be careful when assisting in filling in the application form and passing the information to the insurer and the insured. However, the level of research, explanation and advice shall not be the same for complex investment insurance products. Perhaps regulation of the area of brokers' liabilities at EU level in the area of representation and advice of the adequate insurance cover could help with additional harmonization and more universal application.

As regard to the Serbian market, the institute of insurance brokers is rather new and still underdeveloped in practice, in comparison with some other European insurance markets. There is space for improvement of the current provisions of the insurance agreement, in regard to the imputation of the knowledge of brokers and legislation on insurance intermediaries and in regard to the extent of brokers' research and advice.

SUMMARY

Duties of insurance brokers are numerous and complex. They require a high level of professionalism, knowledge and experience. The increased number of new insurance products requires additional attention and care, such as purely protective products or investment insurance products sold to consumers. There is an increase in information and performance requirements through developing of a code of conduct.

The area of high risk in which brokers should pay particular attention is related to the exchange of information with the insured and providing him with advice. Apart from the information obligation increase, there are additional requirement that a broker perform an inquiry on the insured, its businesses or other objects of insurance. The field of imputation of the knowledge of broker to policyholder or insured seems to be under revision in the UK and elsewhere, as the case law position that it is imputed always to the insured is much criticized. The difficult question is often related to the broker's advice on the choice of an insurer and sufficient insurance cover.

⁵⁴ The Commission's Business Insurance Sector Inquiry 2007.

⁵⁵ The Public Hearing on the Revision of the IMD – From IMD1 to IMD2, 10 December 2010, European Commission, Directorate General Internal Market and Services, p. 5.

⁵⁶ *Ibidem*.

⁵⁷ The Consultation document on the Review of the Insurance Mediation Directive, Commission Staff Working Paper, at: http://ec.europa.eu/internal_market/consultations/docs/2010/insurance-mediation/consultation-document_en.pdf, accessed 15. 12. 2011.