COMMENTS BY THE CITY OF LONDON SOLICITORS COMPANY, INSURANCE LAW COMMITTEE, ON THE LAW COMMISSION'S ISSUES PAPER 3 – INTERMEDIARIES AND PRE-CONTRACT INFORMATION

The City of London Law Society (CLLS) represents approximately 12,000 City lawyers, through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues.

The CLLS responds to Government consultations on issues of importance to its members through its 17 specialist committees. This response has been prepared by the CLLS Insurance Law Committee made up of solicitors who are expert in their field. The members of the Committee are Ian Mathers of Allen & Overy (Chairman); Martin Bakes of Herbert Smith; Christian Wells of Lovells; Michael Mendelowitz of Norton Rose; Stephen Lewis of Clyde & Co; Geoff Lord of Kennedys; Kenneth McKenzie of Davis Arnold Cooper; James Bateson of Norton Rose; Martin Mankabady of Lawrence Graham; Maxine Cupitt of CMS Cameron McKenna; Richard Spiller of Kendall Freeman; Paul Wordley of Holman Fenwick & Willan; Glen James of Slaughter & May; Terry O'Neill of Clifford Chance; Catherine Hawkins of Berrymans Lace Mawer; Charles Gordon of DLA Piper; and Victoria Sander of Linklaters.

1. In this note, we set out comments made in relation to Issues Paper 3. As noted in paragraph 2.7 of the paper, "the issue of whether an intermediary is acting for an insurer or insured is complex." We deal now with each of the tentative proposals in turn.

2. **Is it agreed that an intermediary should be regarded as acting for an insurer for the purposes of obtaining pre-contract information, unless it genuinely searches the market on the insured's behalf? (Paragraph 6.29)**

   We broadly support the idea that an insurer should not be able to avoid a consumer's claim as a result of the mistakes of an intermediary who might be regarded as less than wholly independent. One point to note, however, is that making the intermediary the agent for the insurer in the limited manner proposed is that it may result in the insurer and intermediary adopting a united position (that is, to avoid the policy) against the consumer. This may dissuade the consumer from pursuing the claim and, if the intermediary is no longer his agent for the purpose of obtaining pre-contract information, leave the consumer without remedy. It is not difficult to foresee that where errors have been made in the gathering of pre-contract information the insured's and the intermediary's recollection of who said what to whom may well differ.

3. **Should the test for whether an intermediary acts as the consumer's agent depend upon whether the intermediary conducts a "fair analysis", as defined by the Insurance Mediation Directive? (Paragraph 6.32)**

   The predominant risk, it seems to us, lies where the intermediary has a relationship with one or more insurers which results in a lesser standard of care being paid to insureds than would perhaps otherwise be paid if the intermediary were purely serving the interests of the insured. In other words, because the intermediary is serving both the insured and the insurer, he does not focus his full efforts on the insured in the same way that a truly independent broker might (and may find himself in breach of his duty to the insured). It is not necessarily the case that where an intermediary has conducted a "fair analysis" of the market he is in a much different

position to that of a "tied" agent. It is perfectly possible for an intermediary to conduct a "fair analysis" of a niche market, whilst having a binding authority from each insurer in that market. Indeed, it is perhaps likely that the "standard product" consumer market will continue to be dominated by direct writers and "white-labelled" providers. Niche intermediaries could have an important role but are also likely to have close ties to insurers.

We wonder whether the more appropriate approach is to have a rebuttable presumption that the intermediary is the insurer's agent where either:

(a) the intermediary has the power to issue cover on behalf of the insurer without reference, in general (that is ignoring specific risks or limits that require reference to the insurer), to the insurer; or

(b) the intermediary is a single or multi-tied agent.

4. **Is any additional protection necessary when consumers have been given bad advice about completing proposal forms by intermediaries who are not subject to FSA regulation? (Paragraph 6.34)**

We do not see any need for additional protection because consumers will be adequately protected under our proposed approach in paragraph 3. Whether travel agents and retailers should be subject to some or all of the FSA's rules is a separate issue.

5. **Is it agreed that an intermediary who would normally be regarded as acting for the insurer in obtaining pre-contract information remains the insurer's agent while completing a proposal form? (Paragraph 6.39)**

In principle, we agree with this proposal. However, our comments in paragraph 2 regarding the potential detriment to consumers apply equally here.

6. **Is it agreed that the insured's signature on an erroneous proposal form should not be taken as conclusive evidence of the insured's honesty or lack of care in the way that a proposal form was completed? (Paragraph 6.50)**

We would not seek to change the law in relation to this issue. We do not believe that a signed proposal form is, as the law currently stands, conclusive evidence as to the insured's honesty or lack of care. We would allow the ordinary rules of evidence to continue to establish:

(a) whether statements made in a proposal form are in fact attributable to the insured; and

(b) if that is established, the state of mind (i.e. whether innocent, negligent or fraudulent) of the insured in making those statements.

7. **We welcome views on whether there are any reasons to preserve section 19 (b) for consumer insurance. If so, should a breach grant the insurer a right in damages against the intermediary? (Paragraph 6.54)**

We support the retention of section 19(b) with insurers having a sole remedy of damages against the intermediary.

8. **We ask whether section 19(a) of the Marine Insurance Act 1906 should cease to apply in consumer cases, so that the agent to insure would have no duty to disclose matters other than those which the consumer is bound to disclose in response to the questions asked by the insurer. (Paragraph 6.57)**

   We support the position that section 19 (a) should cease to apply in consumer cases.

9. **If there are reasons to preserve an extended duty under section 19(a):**

   (1) Should the remedy lie in damages against the intermediary, rather than in avoidance against the insured?

   (2) Should any information given in confidence by a third party be excepted from the scope of the duty?

   (3) Should the duty be curtailed to information received in the course of the relevant transaction? (Paragraph 6.58)

   We have no comments on the basis of our response at paragraph 8 above.

10. **Is it agreed that the tentative proposal made in respect of tied agents in the consumer market should apply equally to tied agents who deal with small businesses? (Paragraph 7.8)**

    We support this proposal.

11. **It is agreed that for other businesses, the issue of whom an intermediary is acting for in respect of disclosure issues should be left to the common law? (Paragraph 7.9)**

    The distribution of commercial insurance is a dynamic industry and our tentative view is that the law must retain its flexibility to address the relationships that develop. The fact that an intermediary may in one and the same transaction be agent for insured and insurer is a matter which reflects the commercial reality of the market place and whilst it may result in uncomfortable, conflicting duties, those conflicts are perhaps best resolved or managed, in non-small business insurance at least, through intermediaries, insureds and insurers contracting on a basis freely agreed amongst themselves.

12. **Should the tentative proposals made in paragraph 6.39 and 6.49 [6.50?] apply to business insurance? (Paragraph 7.11)**

    In business insurance we do not, on balance, consider that any express statutory provision should be made in the context of the position of the intermediary in relation to completion of the proposal form. We would leave that issue to be decided by the common law. Prudent insureds, insurers and intermediaries will, no doubt, seek to provide for this issue in their contractual relationships.

    Our comments (at 6 above) in relation to the application of the ordinary rules of evidence apply equally to business insurance.

13. **We ask:**

(1) Is it agreed that where a broker breaches section 19(a), the insurer should no longer be entitled to avoid the policy against the insured. Instead should a remedy lie against the broker in damages?

The crux of this issue is whether the commercial insurance market is better served by allowing insurers to pursue intermediaries for breach of a statutory obligation or preserving the current position which, assuming insurers have successfully avoided the policy, requires insureds to pursue their agents for breach of duty. On the one hand, it seems to us (in theory at least) that shifting the burden of pursuing the intermediary might cause insurers to increase premium rates: their financial risk would be increased by the proposal, as they could not be certain to recover in damages the full amount of the claim that they would have already paid. Further, it might be argued that there is no reason why insurance should be treated differently from any other agency situation where the agent causes his principal loss as a result of his acts or omissions.

On the other hand, it could be argued that insurers are better placed to sue intermediaries and the commercial risk facing insureds is significantly greater than that facing insurers. The whole rationale for insurance is to provide indemnity when it is most needed (to enable, for example, a building to be rebuilt) and that insureds should not be financially prejudiced due to the acts or omissions of their agents.

On balance, we agree that there should be a sole remedy of damages available to insurers against the broker.

(2) If so, should the right to damages apply whenever insurance contracts are placed within the UK, or only where the contract is subject to the law of a part of the UK?

This is a difficult issue. On balance, we are of the view that the right to damages should apply where the insurance contract is subject to the law of a part of the UK. It may leave an insurer who agrees to a "non-UK" governing law clause without remedy, but that is likely to be a preferable outcome (insurers will after all be able to take advice on a case by case basis) to the extra-territorial effect (and potential conflicts of law issues) that are likely to result from the other alternative.

(3) Should producing brokers be obliged to pass relevant information up the chain to the placing broker?

Yes. The disclosure of material facts is critical to the underwriting of insurance risk and underpins pricing. However, the placing broker should not be liable for the default of a producing broker; and we agree that the precise extent of the obligation requires careful consideration.

(4) Should the law specifically state that an intermediary is not required to disclose information given to it in confidence by a third party? (Paragraph 7.20)

On the face of it this appears to be correct and attractive. Our concern though is that intermediaries may turn to it all too frequently as a defence.

Further, such a blanket approach could result in inappropriate outcomes. Suppose, for example, that a proposed insured, in the course of providing his broker, A, with

information necessary to get insurance for his building and his business, tells broker A that he pays a weekly fee to the local Mafia for protection, and broker A's response is: You'll never get cover; forget it. So having learnt his lesson, the proposed insured goes to broker B but says nothing about the protection money. But A learns that B is placing the risk and tells him in confidence about the protection money. Should B not have a duty to disclose the information he has received in confidence? There are difficult conflict issues that present themselves in these types of situations, but that does not necessarily mean that the broker should not have a duty to disclose.

Accordingly, we would wish to see a more detailed review of the kinds of information which might be at issue, as well as other cases where the law might be taken to be a bar to disclosure.

20th June 2007

Contacts:

David Whear of Norton Rose, 3 More London Riverside, London SE1 2AQ (020 7444 3361); email: David.Whear@nortonrose.com

Ian Mathers of Allen & Overy, One Bishops Square, London E1 6AO (020 3088 4781); email: ian.mathers@allenovery.com